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1 October 6, 2015
 2 (9:05 a.m.)
 3 CHAIRMAN:
 4 Q. Once more into the trenches. I think we got
 5 one undertaking, is that correct, madam?
 6 MS. PENNELL:
 7 Q. We do, Mr. Chair. We have Undertaking 11.
 8 CHAIRMAN:
 9 Q. Okay, so you -
 10 MS. PENNELL:
 11 Q. Already done.
 12 CHAIRMAN:
 13 Q. So we're back to you, I think, Mr. Johnson, to
 14 start your cross-examination of Mr. Fagan.
 15 JOHNSON, Q.C.:
 16 Q. Yes, thank you very much, Mr. Chairman.
 17 MR. KEVIN FAGAN - CROSS-EXAMINATION BY THOMAS JOHNSON,
 18 Q.C.:
 19 JOHNSON, Q.C.:
 20 Q. Good morning, Mr. Fagan.
 21 MR. FAGAN:
 22 A. Hello, Mr. Johnson.
 23 JOHNSON, Q.C.:
 24 Q. In relation to the August 14 settlement
 25 agreement, one of the things Hydro has agreed

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1 is that Hydro will be filing a general rate
 2 application no later than March 31st, 2017,
 3 for rate changes based on a 2018 test year,
 4 right?
 5 MR. FAGAN:
 6 A. That's correct.
 7 JOHNSON, Q.C.:
 8 Q. And so given this, Mr. Fagan, the rates that
 9 we are going to be determining in this present
 10 GRA, these rates will be in place for 2016 and
 11 2017 period, right?
 12 MR. FAGAN:
 13 A. Yes.
 14 JOHNSON, Q.C.:
 15 Q. Okay, now Mr. Fagan, both Mr. Patrick Bowman
 16 and Mr. Greneman agreed during their
 17 testimony, as they both testified, that one of
 18 the underlying principles behind cost of
 19 service analysis is that it's never a precise
 20 tool for cost allocation, however, the
 21 analysis should reflect fair and reasonable
 22 estimation of the cost responsibility between
 23 customer classes for the periods in which the
 24 study is being applied. Do you recall those
 25 gentlemen agreeing to that statement?

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1 MR. FAGAN:
 2 A. Yeah, I take no issue with that, yeah.
 3 JOHNSON, Q.C.:
 4 Q. Mr. Fagan, likewise, I take it that you would
 5 be in complete agreement with that statement
 6 of principle as well?
 7 MR. FAGAN:
 8 A. Yes, I think sometimes in our jurisdiction it
 9 take a combination of both base rates and
 10 regulatory mechanisms to achieve that, but,
 11 yeah.
 12 JOHNSON, Q.C.:
 13 Q. Okay, so Mr. Fagan, I guess we would be in
 14 total agreement that rates are to be just and
 15 reasonable at all times, right?
 16 MR. FAGAN:
 17 A. To the extent possible, yes.
 18 JOHNSON, Q.C.:
 19 Q. Now Mr. Fagan, the other thing that's an
 20 element of the August 2015 settlement
 21 agreement is that the parties have agreed that
 22 the year to date net load variation for
 23 Newfoundland Power and the industrial
 24 customers shall be allocated among the
 25 customer groups based on energy ratios with

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1 effect from the date to be determined by the
 2 Board, right?
 3 MR. FAGAN:
 4 A. That's right.
 5 JOHNSON, Q.C.:
 6 Q. So the date from which it comes into effect is
 7 left to be determined by the Board?
 8 MR. FAGAN:
 9 A. And Hydro has proposed that to be September
 10 1st, 2013, I believe.
 11 JOHNSON, Q.C.:
 12 Q. Exactly. Before we get there, is the RSP
 13 designed whereby load variations shall be
 14 allocated on the basis of energy ratios? That
 15 would be consistent with what Hydro proposed
 16 at the 2006 GRA, isn't it?
 17 MR. FAGAN:
 18 A. That's correct.
 19 JOHNSON, Q.C.:
 20 Q. That's right, and coming out of 2006 GRA,
 21 that's where the parties, I think you'll
 22 agree, agreed to examine a redesign of the RSP
 23 to better meet design objectives, is that
 24 right, do you recall that?
 25 MR. FAGAN:

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1 A. Yes, that's correct.
 2 JOHNSON, Q.C.:
 3 Q. Okay, and so Mr. Fagan, I take it you'd agree
 4 that by the parties agreeing to undertake this
 5 study, the parties are acknowledging that the
 6 RSP rate design had inadequacies?
 7 MR. FAGAN:
 8 A. I think they agreed that it should be
 9 reviewed. I don't think there was an
 10 agreement necessarily on whether there was
 11 inadequacies by all parties. Some parties
 12 thought there was inadequacies, so everybody
 13 agreed to do a review.
 14 JOHNSON, Q.C.:
 15 Q. Okay, and that review or that study of the RSP
 16 rate design, as we know that was not
 17 completed, right?
 18 MR. FAGAN:
 19 A. That's correct.
 20 JOHNSON, Q.C.:
 21 Q. Mr. Fagan, does the allocation of the load
 22 variation component of the RSP on the basis of
 23 energy ratios, does that result in your
 24 judgment rates that better reflect costs and
 25 leading to rates that are more just and

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1 reasonable?
 2 MR. FAGAN:
 3 A. It simulate rerunning of cost of service study
 4 for energy, effectively, between test years.
 5 So it attempts to almost update customer rates
 6 to reflect - almost like recreation of a test
 7 year from an energy cost perspective between
 8 test years, so I think that probably better
 9 reflects the cost of serving the customer
 10 classes.
 11 JOHNSON, Q.C.:
 12 Q. Okay, and rates that better reflect costs,
 13 they would be seen as being more just and
 14 reasonable?
 15 MR. FAGAN:
 16 A. Yes, I think so.
 17 JOHNSON, Q.C.:
 18 Q. Now Mr. Fagan, can you confirm - my
 19 understanding is that when the original 2013
 20 GRA was filed, the industrial customers were
 21 paying approximately 65 percent of the cost of
 22 power determined in the 2013 cost of service
 23 study?
 24 MR. FAGAN:
 25 A. Could you just repeat the question? I just

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1 got distracted for a moment.
 2 JOHNSON, Q.C.:
 3 Q. No problem. Can you confirm that when the
 4 original 2013 Hydro GRA was filed, that the
 5 island industrial customers were paying about
 6 65 percent of the cost of power as determined
 7 in the 2013 cost of service study?
 8 MR. FAGAN:
 9 A. Subject to check, but it sounds reasonable.
 10 JOHNSON, Q.C.:
 11 Q. Yes.
 12 MR. FAGAN:
 13 A. Given the large percentage increase that was
 14 proposed.
 15 JOHNSON, Q.C.:
 16 Q. And just to - the reference that I would have
 17 on that, and I believe it's on the record as
 18 part of this GRA proceeding, is RSP-CA-NLH-12.
 19 I don't know if Jennifer can bring that up.
 20 MS. GRAY:
 21 Q. Sorry, just one moment.
 22 MR. FAGAN:
 23 A. It's a fairly long record to find everything.
 24 JOHNSON, Q.C.:
 25 Q. Yes.

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1 MS. GRAY:
 2 Q. I'm sorry, Jacquie, do you know where I can
 3 find -
 4 MS. GLYNN:
 5 Q. We're trying to find it as well.
 6 MR. COXWORTHY:
 7 Q. I think it's with the other CA-RFI. It's a
 8 separate group for the RSP.
 9 MS. GRAY:
 10 Q. Yes, thank you.
 11 JOHNSON, Q.C.:
 12 Q. I'm referring Mr. Fagan to Attachment 1 to
 13 that answer. You see the second - over to the
 14 right of the page, just back one column. It's
 15 headed up, "The ratio current average rate to
 16 test year and average cost of service rate",
 17 and as you see at the bottom, the total island
 18 industrial was 65.26 percent. So that just
 19 confirms that number.
 20 MR. FAGAN:
 21 A. Yes.
 22 JOHNSON, Q.C.:
 23 Q. And at the time, if we go up and look at
 24 Newfoundland Power, for instance, they're
 25 nearly up to the full cost of - they're at

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1 98.24 percent. Mr. Fagan, there's been some
 2 discussion of 37.6 million dollar figure that
 3 got transferred to the benefit of the
 4 industrial customers, and, I guess, we've
 5 termed it as a subsidy by small customers to
 6 the industrial customers. The small customers
 7 were paying for the rates and all the RSP
 8 adjustments through the time period, but, I
 9 guess, the question would be, the industrial
 10 customers rates, the reason that they were so
 11 far under the cost of supply was because their
 12 rates had been made interim or frozen, if you
 13 will, right?
 14 MR. FAGAN:
 15 A. That's correct.
 16 (9:15 a.m.)
 17 JOHNSON, Q.C.:
 18 Q. Now the 37.5 million dollar amount or subsidy
 19 became crystallized, I take it you would
 20 agree, by the Board's Order in PU-26-2013, an
 21 order that I would hasten to add the Board had
 22 no choice but to issue in light of the
 23 directive, right?
 24 MR. FAGAN:
 25 A. I don't know if I can accept the term

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1 "subsidy". The term "subsidy" is
 2 presupposing, I think - if the government had
 3 not issued direction on disposition of the RSP
 4 surplus, it would have went back for review by
 5 the Board. So I'm unsure if the Board would
 6 have necessarily used the energy ratios purely
 7 in determining the allocation of the RSP
 8 surplus between retail customers and
 9 industrial customers without considering
 10 potential impacts on industrial customers. So
 11 the Board may have come to some compromised
 12 solution as well, so I don't know if I can
 13 accept the assumption that energy ratios would
 14 have automatically fallen out had it come back
 15 to the Board for review.
 16 JOHNSON, Q.C.:
 17 Q. But one thing is certainly the case that Hydro
 18 believed that it should go by way of energy
 19 ratios. That was the fair and just approach,
 20 right?
 21 MR. FAGAN:
 22 A. Oh, yes, certainly.
 23 JOHNSON, Q.C.:
 24 Q. Yes, and so in terms of the hesitation then to
 25 calling it a subsidy, Mr. Fagan, I mean, you

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1 would be familiar with the fact that the 37.6
 2 million dollar amount, that would be in excess
 3 of the average annual amount paid by
 4 industrial customers for power from '08 to
 5 2012, right?
 6 MR. FAGAN:
 7 A. It's my understanding that the amount you're
 8 referring to, the amount in excess of what
 9 they would have - industrial customers would
 10 have received on just an energy ratio basis.
 11 That would be the basis for the 37 million.
 12 JOHNSON, Q.C.:
 13 Q. Right, right, indeed. So if the had - if the
 14 Board had acceded, say, to Hydro's and
 15 Newfoundland Power's, and Consumer Advocate's
 16 position that it should go by way of energy
 17 ratios, what amount would they have gotten as
 18 opposed to 37.6?
 19 MR. FAGAN:
 20 A. Well, had the change been made back then, then
 21 obviously the industrial customers wouldn't
 22 have received that money through government
 23 directive. It's really difficult to take it
 24 and look at it in isolation without looking at
 25 what's been done has been done with regard to

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1 the uncertainty of industrial rates over time
 2 due to the closure of the paper mills, and the
 3 funds were held in the industrial customer
 4 balance until it was determined how they would
 5 be disposed of. So to go back now and say
 6 that, well, they obviously didn't pay their
 7 way, they may be of the opinion that they've
 8 taken the risk somewhat with regard to the way
 9 the RSP was set up, that if their energy usage
 10 went up versus down, then they would bear the
 11 cost of it. That's the way the RSP rules were
 12 at the time. So to me, I don't think you can
 13 look at one piece in isolation without looking
 14 at the fact that it was in the industrial
 15 customers account. Now we've got to go back
 16 and - ignoring the government directive, we've
 17 got to go back and try and address this
 18 matter, and so if the Board was going back to
 19 try and address this matter, they'd obviously
 20 look at the energy ratios, but I think they'd
 21 also have to look at how do we recover those
 22 costs that have not been recovered from
 23 industrial customers since 2007. I think
 24 gradualism is a term that's generally used in
 25 rate design, so I don't think this is strictly

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1 cost allocation because you've also got to
 2 look at recovery of costs. They may have had
 3 some other views on would they have somehow
 4 used some of those funds to gradually phase in
 5 industrial customer rates back to costs, I
 6 don't know, but I don't think I can assume
 7 that they would have viewed it as an isolated
 8 matter of strictly recovering the cost.

9 JOHNSON, Q.C.:

10 Q. Okay, but in terms of what Hydro's position
 11 would have been, if Hydro's position would
 12 have been acceded to in terms of basing it on
 13 energy ratios, I take it that mathematically
 14 the industrial customers would have gotten
 15 only a small fraction of the amount that the
 16 ended up getting credit for, right?

17 MR. FAGAN:

18 A. Hydro put its position forward on energy
 19 ratios in 2006 before all the matters occurred
 20 with regard to the closure of the paper mills
 21 and the accumulation of the balances in the
 22 RSP. If Hydro had to come forward with a
 23 proposal to the Board to deal with the
 24 disposition of the RSP surplus rather than
 25 being a directive from the government, I'm not

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1 sure if Hydro would have proposed strictly
 2 energy ratio and a full recovery of all the
 3 costs from industrial customers.

4 JOHNSON, Q.C.:

5 Q. But in the proceeding four years after 2006 in
 6 2010, Hydro's - and that's the one that led to
 7 the jurisdictional issue, etc, but Hydro's
 8 evidence indicated that it should go by energy
 9 ratios at that time too, right?

10 MR. FAGAN:

11 A. I don't think Hydro deviated from the position
 12 that it should have been shared on energy
 13 ratios.

14 JOHNSON, Q.C.:

15 Q. That's right.

16 MR. FAGAN:

17 A. My only point is that with regard to
 18 implementation of industrial rates, you've got
 19 to look at the impact on customers as well,
 20 that's all, but Hydro's position was clear, it
 21 should be proposed on energy ratios since
 22 2007.

23 JOHNSON, Q.C.:

24 Q. That's right. I guess, there's no question
 25 that, in effect, the effect of OC-089, OC-

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1 2013-089, the effect of that is that the
 2 island industrial class received the
 3 equivalent of about 1.5 years of power based
 4 upon the annual amount that they had been
 5 paying over '08 to 2012, correct?

6 MR. FAGAN:

7 A. The 37 million you're referring to equates to
 8 that.

9 JOHNSON, Q.C.:

10 Q. Yes.

11 MR. FAGAN:

12 A. Yes, that's correct.

13 JOHNSON, Q.C.:

14 Q. Yeah, that's right. Now given the fact that
 15 the Order in Council did something quite
 16 different than an energy ratio approach, did
 17 Hydro consider this big transfer that occurred
 18 by virtue of the Order in Council when it
 19 decided to propose in this amended GRA that
 20 effective September 1, 2013, that the year to
 21 date net load ratio would be allocated based
 22 upon energy ratios?

23 MR. FAGAN:

24 A. Well, Hydro's view is that government made a
 25 policy decision on disposition of the

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1 historical balance, and so Hydro has
 2 maintained its approach and principle of how
 3 it should be done going forward, and how we
 4 believe it should be done going forward, and
 5 going forward, I mean from the point of August
 6 31st, 2013, when government made its decision,
 7 we propose it be done on energy ratios going
 8 forward, and we felt it's a principle basis,
 9 it's consistent with cost of service, so Hydro
 10 proposed it in that manner.

11 JOHNSON, Q.C.:

12 Q. Okay, but you would agree that Order in
 13 Council 2013-089 in no manner provides
 14 direction to the Board with respect to the
 15 amounts built up in the load variation account
 16 since September 1st, 2013, right?

17 MR. FAGAN:

18 A. Oh, I agree. However, I don't know if - even
 19 if Hydro disagreed with the government's
 20 disposition approach to the balance, I don't
 21 think you should deviate from your principles
 22 and say, okay, I'll try to claw that back in
 23 the future. I think you'd still want to look
 24 forward and say what's a fair way of doing it.

25 JOHNSON, Q.C.:

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1 Q. Would there be a case, Mr. Fagan, for the
 2 Board transferring the balance in the load
 3 variation that has accumulated from September
 4 1st to Newfoundland Power's RSP account on the
 5 basis of the fact that the 37.6 million dollar
 6 credit that went to the ICs was so materially
 7 different than what would have been the result
 8 on energy ratios approach?
 9 MR. FAGAN:
 10 A. I mean, from a consumer perspective, if one
 11 believed there was a subsidy, one would say,
 12 well, that wasn't fair, I should get that
 13 back, but from a community rate making
 14 approach, we're looking at government policy
 15 directs Hydro in certain matters, so
 16 government policy dealt with that historical
 17 matter. Now looking forward, we've got these
 18 costs, fuel cost variances due to load growth,
 19 so from a cost of service perspective, it
 20 should be shared based on the energy
 21 proportions between Newfoundland Power and
 22 industrial customers, so that's what Hydro is
 23 proposing.
 24 JOHNSON, Q.C.:
 25 Q. So if the Board concludes that it was, in

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1 fact, a subsidy that occurred there, you would
 2 think that the Board should be open to the
 3 idea of saying, look, monies that have built
 4 up from September 1st, 2013, could, in fact,
 5 legitimately go to Newfoundland Power
 6 customers?
 7 MR. FAGAN:
 8 A. I mean, the Board would have authority to
 9 determine the disposition of the load
 10 variation balance that's accumulated since
 11 September, but, I mean, the Board generally
 12 follows generally accepted practices, and
 13 these are fuel costs, and fuel costs are
 14 generally allocated based on energy usage. So
 15 from the perspective of fairness of sharing
 16 costs looking forward rather than looking
 17 backwards, I think they would lean towards the
 18 energy basis, but I wouldn't - I can't say
 19 what the Board would do with respect.
 20 JOHNSON, Q.C.:
 21 Q. Mr. Fagan, in light of what the Order in
 22 Council mandated happen, in your judgment did
 23 this result in rates covering the period of
 24 2008 through to August 31st, 2013, that were
 25 just and reasonable?

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1 MR. FAGAN:
 2 A. It's very unusual circumstances that occurred
 3 with respect to rates over the period 2007 to
 4 2013. It's hard to view that being the fault
 5 of industrial customers with respect to -
 6 there was a closer of paper mills, there was
 7 fuel savings. The RSP rules required those
 8 fuel savings to go into the industrial
 9 customer account. Then there was a debate
 10 over where these fuel savings should go. It
 11 took a fair bit of time to get it resolved,
 12 obviously, and a court case as well. What the
 13 government directive did effectively was
 14 almost effectively established the policy that
 15 we're settling this dispute and putting enough
 16 funds there to say the industrial customers
 17 would have - it would have recovered all the
 18 additional fuel costs between 2007 up to
 19 August 31st, 2013. I can understand one
 20 coming to that conclusion. It's difficult in
 21 the circumstances looking back whether you
 22 should judge whether rates reasonable
 23 reflected costs. I don't know looking back
 24 whether one would disagree necessarily with
 25 what the government did from, you know, the

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1 perspective of their judgment because they
 2 could view it that, well, it wasn't industrial
 3 customers fault with regard to what happened
 4 here, and so why should now we go back and
 5 impose - be accumulative towards industrial
 6 customers because of the unfortunate
 7 circumstances of the closure of the paper
 8 mills and the impact it had on customer rates.
 9 So it's a little bit of an unusual
 10 circumstance with regard to assessing whether
 11 the rates were just and reasonable. I think
 12 at this point we look and say the rates are
 13 not recovering current costs, so based on
 14 government direction dealing with historical
 15 now we'll try and make rates just and
 16 reasonable going forward. Looking back on it,
 17 it's kind of difficult to assess. Obviously,
 18 the industrial customers weren't paying rates
 19 that recovered their base rate cost plus the
 20 fuel cost as the fuel price went up over the
 21 period 2007 to 2013, but the industrial
 22 customers would probably argue that there was
 23 balances in the RSP accumulating that they
 24 felt entitled to which were appropriate to
 25 apply against that amount. So I think it

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1 depends which side of the fence you're on.
 2 JOHNSON, Q.C.:
 3 Q. But as you're aware, I mean, it's been
 4 determined by the highest court in the
 5 province that there was no entitlement, there
 6 was no vested right in the industrial
 7 customers in any of these monies.
 8 MR. FAGAN:
 9 A. Oh, no, I
 10 JOHNSON, Q.C.:
 11 Q. So they can say, well, we felt we were
 12 entitled to it, right?
 13 MR. FAGAN:
 14 A. I agree.
 15 JOHNSON, Q.C.:
 16 Q. I mean, that's the landscape, and during this
 17 period when industrial customers were paying
 18 65 percent - some of them actually lower, you
 19 know, Teck 56 percent, Vale 56.78 percent,
 20 during this period Newfoundland Power
 21 customers were paying the full freight, right?
 22 MR. FAGAN:
 23 A. Yes, Newfoundland Power customers were
 24 recovering the costs because their rates were
 25 adjusted each July for fuel price increases.

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1 JOHNSON, Q.C.:
 2 Q. Right, exactly. So again I come back to, you
 3 know -
 4 MR. FAGAN:
 5 A. Well, in hindsight, it's hard to argue that
 6 the industrial customer rates were below cost
 7 in that period. So if you deem that to be not
 8 reasonable, I mean, we probably could agree
 9 it's not reasonable, but the circumstances
 10 were a little unusual which resulted in that.
 11 So it's hard to fix the past somewhat with
 12 respect to that.
 13 (9:30 a.m.)
 14 JOHNSON, Q.C.:
 15 Q. Well, in terms of - we're not talking about
 16 fixing the past, we're talking about a comment
 17 upon the past, and what I'm asking is Hydro's
 18 comment as to whether or not it believes that
 19 the rates covering the period 2008 through
 20 August, 2013, having regard to the Order in
 21 Council, produced just and reasonable rates?
 22 MR. FAGAN:
 23 A. I think it would be difficult to accept that
 24 the rates that the industrial customers paid
 25 over the period 2007 to 2013 were reasonable

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1 given the cost to provide service. One could
 2 certainly - they were outside the range of
 3 where one would want to take action to try and
 4 increase it, so from that perspective, I think
 5 I'd say that the rates were too low.
 6 JOHNSON, Q.C.:
 7 Q. And the monies that did happen to build up in
 8 the load variation account by reason of IC
 9 load dropping off, I mean, it's obvious, but
 10 I'll just state the question, that had nothing
 11 to do with the industrial customers responding
 12 to a rate signal in their rate and conserving
 13 or finding efficiencies of operations, right?
 14 MR. FAGAN:
 15 A. That's correct.
 16 JOHNSON, Q.C.:
 17 Q. It's just a shutdown that Hydro was left in
 18 the lurch on, as I understand it, I read about
 19 it in the paper.
 20 MR. FAGAN:
 21 A. It was a result of the closure of the mills
 22 and a fuel savings that resulted from it, yes.
 23 JOHNSON, Q.C.:
 24 Q. Of which Hydro was given no advance notice?
 25 MR. FAGAN:

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1 A. I really couldn't say on that, but I think
 2 there's been evidence on the record to that
 3 effect.
 4 JOHNSON, Q.C.:
 5 Q. Yeah. Now with respect to the industrial
 6 customer rate phase-in in this matter, Hydro's
 7 amended application requests that the phase-in
 8 of island industrial customer rates be
 9 completed by September 1st, 2016, as set out
 10 in the evidence in support of the application.
 11 That's what the formal application before the
 12 Board states at Paragraph 44, Sub 28.
 13 MR. FAGAN:
 14 A. That's correct.
 15 JOHNSON, Q.C.:
 16 Q. Mr. Fagan, what increase is needed and when to
 17 bring the island industrial customer rates up
 18 to the full cost of supply as required by
 19 2013-089?
 20 MR. FAGAN:
 21 A. Jenny, could you bring up response to PUB-NLH-
 22 485. We'll look at Table 1 first. So this
 23 table represents the proposed rates based on
 24 the fuel cost of \$93.32. So the industrial
 25 rate increase there will be 27 percent.

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1 Relative to the existing rates, okay, I think
 2 - if we go to footnote 3, there's an RSP
 3 surplus effect that's excluded here, okay. So
 4 it's 27 percent there. Now if we go to Table
 5 2, in Table 2 we're showing a change relative
 6 to the rates in place January 1, 2015, of 13.2
 7 percent. Now this is reflecting of fuel price
 8 of \$73.00 a barrel. That's probably close to
 9 what the forecasted fuel price is for 2016.
 10 We'll be filing next week, I think, it's
 11 around \$70.00 a barrel. I mentioned
 12 yesterday, and I expect Mr. Coxworthy will
 13 request an undertaking if Mr. Johnson doesn't,
 14 with respect to the calculations supporting
 15 rates for January 1, 2016, and September 1,
 16 2016, but we've done some preliminary work on
 17 the numbers which would indicate if the Board
 18 approved the proposed rates that we've filed,
 19 adjusted for the test year fuel price in this
 20 case would have been the \$73.00 a barrel,
 21 you'd have an increase to industrial customers
 22 that would bring them up to the full base rate
 23 January 1st. I don't know if it's before
 24 Table 2, mentioned RSP surplus adjustment that
 25 we would propose to be updated, so Hydro's

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1 proposal is that we'd have full base rates in
 2 play by January 1st, 2016, but with the RSP
 3 surplus adjustment updated to permit the
 4 remaining disposition of the approximately 11
 5 million dollars that was left there for
 6 phasing in industrial customer rates. I
 7 think, based on what the Board approved in
 8 July, I think there's about a 3 million dollar
 9 balance forecast at the end of 2015, which
 10 will continue to be used for phasing in
 11 industrial customer rates. If the Board
 12 approved the revised industrial customer
 13 rates, January 1st, to be an increase looks
 14 like between 7 and 8 percent to get them to
 15 full base rates, and then the RSP subsidy
 16 would be phased out, RSP surplus, not subsidy,
 17 RSP surplus adjustment will be phased out
 18 September 1, 2016, and so they'd have no RSP
 19 surplus adjustment and be at full base rates,
 20 and I think the increase there would be in the
 21 neighbourhood of around 13 percent. So still
 22 facing approximately a 20 percent increase
 23 between January to September to move them to
 24 full cost rates.
 25 JOHNSON, Q.C.:

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1 Q. Mr. Fagan, since you've hinted at an
 2 undertaking in that regard, I think I'll take
 3 you up on it.
 4 MR. FAGAN:
 5 A. We've got the numbers worked out for the
 6 industrial customers, excluding Teck. Teck is
 7 a little bit more complicated because of the
 8 closure and the - load demand, so just fine
 9 tuning the numbers for Teck, but we'll provide
 10 something, okay.
 11 JOHNSON, Q.C.:
 12 Q. Okay, thank you.
 13 MS. GLYNN:
 14 Q. The undertaking is noted on the record.
 15 MR. FAGAN:
 16 A. Okay.
 17 JOHNSON, Q.C.:
 18 Q. Obviously, there's a bit of complexity to this
 19 and, I guess, I'm going to ascribe to the view
 20 there's no such thing as a foolish question,
 21 but maybe there is, but it's one that I want
 22 to have answered in my head, and that is in
 23 order to complete the phase-in of IC rates by
 24 September 1st, 2016, will that require a
 25 specific order from the Board arising out of

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1 this GRA, or would you be contemplating
 2 further orders of the Board subsequent to the
 3 Board's GRA order to accomplish that?
 4 MR. FAGAN:
 5 A. Well, let's go to the January 1st concept I
 6 just put forward, okay.
 7 JOHNSON, Q.C.:
 8 Q. Yeah.
 9 MR. FAGAN:
 10 A. Normally there would be a fuel rider update
 11 for industrial customers, January 1st, okay.
 12 Hydro will be putting a fuel forecast on the
 13 record next week which would normally be used
 14 to establish a fuel rider. The current RSP
 15 rules have set the fuel rider to zero, subject
 16 to a further order of the Board, okay. So
 17 there will be required to be an order. I
 18 don't anticipate a final Board order on
 19 customer rates prior to January 1st. It would
 20 be nice, but it would be a bit of a stretch, I
 21 would think. Hydro has filed - when Hydro
 22 filed its amended application, it requested
 23 interim rates and the proposed rates that were
 24 put before the Board to become interim January
 25 1st, 2015. The Board approved interim rates

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1 in July. I'm not sure if an additional
 2 application is required for the Board to
 3 approve the proposed rates for industrial
 4 customers proposed base rates to become
 5 interim January 1, 2016, and the RSP
 6 adjustment to be updated, but probably may
 7 want to talk to Board staff about that to
 8 determine how we proceed with that.

9 JOHNSON, Q.C.:
 10 Q. Okay.

11 MR. FAGAN:
 12 A. That would be the desirable approach with
 13 regard to implementing industrial rates,
 14 January 1st, and permitting the remainder of
 15 the transition to full cost rates, including
 16 the RSP surplus credits, to come into play for
 17 September and - January and September.

18 JOHNSON, Q.C.:
 19 Q. Has Hydro had discussions with the ICs about
 20 what it sees coming in terms of the rate
 21 progression under the phase-in?

22 MR. FAGAN:
 23 A. Other than what I presented yesterday, we
 24 haven't had discussions on it, no. Now the
 25 information that I presented yesterday was

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1 provided in response to CA-NLH-363, so it's
 2 been out there.

3 JOHNSON, Q.C.:
 4 Q. Yes.

5 MR. FAGAN:
 6 A. It's just the actual impact of that proposal
 7 haven't been clear.

8 JOHNSON, Q.C.:
 9 Q. And CA-NLH-363 basically summarized the plan
 10 of Hydro to get to full phase-in by September
 11 1st, 2016?

12 MR. FAGAN:
 13 A. Yes.

14 JOHNSON, Q.C.:
 15 Q. Okay.

16 MR. FAGAN:
 17 A. Because there's - we got CA-NLH-363 presented
 18 here now, so in September, 2003, there was a
 19 large rate increase, right, and Hydro filed a
 20 number of applications since that time to try
 21 and increase industrial rates in an interim
 22 basis, but we were only successful in July of
 23 2015 to achieve increase in industrial rates.
 24 So fortunately the fuel prices declined, so
 25 that the impact on industrial customers is not

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1 as large as it would have been had it stayed
 2 up to \$93.00, but it's still a material
 3 increase.

4 JOHNSON, Q.C.:
 5 Q. Okay, turning to the rural deficit issue, and
 6 some of this ground is well trodden, and I
 7 understand sort of help in trying to focus a
 8 little bit, but just to confirm, Mr. Fagan,
 9 Hydro does believe that the rural deficit
 10 allocation issue should be dealt with at this
 11 hearing?

12 MR. FAGAN:
 13 A. Yes.

14 JOHNSON, Q.C.:
 15 Q. Okay, and, in fact, you offered yesterday that
 16 based upon your experience with the 1992
 17 hearing, you reckoned that there's been, in
 18 fact, more discussion of the rural deficit
 19 allocation at this hearing than what took
 20 place back in '92?

21 MR. FAGAN:
 22 A. Well, at the 1992 hearing, Mr. Brockman was an
 23 expert, Mr. Sarikas was an expert for Hydro,
 24 and Mr. Baker was an expert. So we've had
 25 more experts deal with it here, and all the

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1 experts that presented prefiled evidence, plus
 2 Dr. Wilson has also commented on it, that all
 3 except Mr. Brockman support Hydro's proposal,
 4 and there's been a lot of analysis and
 5 information provided to the Board, a lot more
 6 material I would suggest than was presented in
 7 1992.

8 (9:45 a.m.)

9 JOHNSON, Q.C.:
 10 Q. Mr. Fagan, when Mr. Brockman was testifying -
 11 if we could bring up the transcript from
 12 September 29th, Jennifer, Page 214. This is
 13 in discussion - he's being questioned by Mr.
 14 Luk, and Mr. Brockman is talking about this
 15 phase-in idea, and he says part way down his
 16 reply, "You don't necessarily have to phase it
 17 all in, maybe just say I'm going to do a
 18 little bit or maybe you don't do any if you
 19 think there's going to be a rate case. I
 20 guess, Hydro said they're going to file again,
 21 subject to check, next year, maybe 2017", and
 22 then he says, "But I wouldn't phase it all in
 23 by then, and I probably would never phase it
 24 all in because then everything is going to
 25 change again, so maybe I'd just give you 3

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1 percent and we'll see what happens, you know,
 2 once we review all the stuff. I don't change
 3 the methodology, I don't give you all of this
 4 either because there does seem to be a lot of
 5 controversy about it". Mr. Fagan, in your
 6 opinion, is this a realistic solution to the
 7 rural deficit allocation problem or is this
 8 just kicking the problem down the road?
 9 MR. FAGAN:
 10 A. Well, I struggle with phasing in a rate change
 11 based on what most people would agree that the
 12 cost is not an appropriate cost for recovery
 13 from the Labrador interconnected customers, so
 14 to me it's a bit of a leap that you'd proceed
 15 to try and phase something in when it's a cost
 16 that we don't think is reasonable to recover
 17 from that group of customers because you don't
 18 agree that it's a fair allocation between the
 19 customers of Labrador interconnected and
 20 Newfoundland Power.
 21 JOHNSON, Q.C.:
 22 Q. Okay.
 23 MR. FAGAN:
 24 A. So jumping to - I think this is in the context
 25 of jumping to the rate design issue too that

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1 Mr. Brockman was indicating that you could
 2 deal with it through rate design rather than
 3 necessarily through cost of service because
 4 the Board had mentioned that you could deal
 5 with the customer impacts through rate design.
 6 Now there's been discussion on marginal costs
 7 and the issue with Labrador. Labrador's
 8 average rate is below marginal cost of fuel -
 9 sorry, not marginal cost of fuel, marginal
 10 cost of Labrador interconnected system if one
 11 viewed marginal cost as the opportunity cost
 12 of export sales, but with or without the rural
 13 deficit, you could make rate design changes
 14 for Labrador interconnected customers for
 15 inclining block, for example, that you could -
 16 it was mentioned by Mr. Doug Bowman, that you
 17 could to deal with that and give customers an
 18 efficient price signal without having to
 19 burden them with an unfair cost share of the
 20 rural deficit. So you can deal - you don't
 21 necessarily have to pile the costs on to come
 22 up with a reasonable marginal price signal for
 23 customers on Labrador interconnected system.
 24 With respect to Mr. Brockman's statement, I
 25 just don't think the 28 percent increase is

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1 justified based on trying to recover rural
 2 deficit, which we don't believe is a
 3 reasonable share for Labrador interconnected.
 4 JOHNSON, Q.C.:
 5 Q. The comment that he makes at one part of his
 6 statement is, "Probably would never phase it
 7 all in because everything is going to change,
 8 so maybe I'd just give you 3 percent and see
 9 what happens". If the gave you, like, 3
 10 percent under this scenario, what would
 11 happen? Like, where does the rest of the
 12 money come from?
 13 MR. FAGAN:
 14 A. I'm not sure what the assumption was there. I
 15 got the impression from Mr. Brockman that it
 16 would continue to be paid for by Newfoundland
 17 Power's customers. Now I may have
 18 misinterpreted, but I thought he said that it
 19 would continue to be paid for by the customers
 20 that are already paying for it.
 21 JOHNSON, Q.C.:
 22 Q. Okay.
 23 MR. FAGAN:
 24 A. That's just my interpretation.
 25 JOHNSON, Q.C.:

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1 Q. Mr. Fagan, does the rural deficit have
 2 anything to do with the marginal cost and rate
 3 design studies that are being undertaken by
 4 Hydro later this year and next year?
 5 MR. FAGAN:
 6 A. No.
 7 JOHNSON, Q.C.:
 8 Q. In the interest of - this is on the question
 9 about information on bills. In the interest
 10 of transparency, shouldn't the amount of the
 11 rural rate subsidy be shown on the bills of
 12 customers who are required to pay it, and also
 13 those customers who receive the subsidy,
 14 there's been discussion of that throughout the
 15 hearing, as you'll recall. I'd like to get
 16 Hydro's position on that?
 17 MR. FAGAN:
 18 A. I struggle with it because when I look at 40
 19 percent of the rural deficit is on the island
 20 interconnected system, okay, so you've got the
 21 people in Baie Verte versus the people in Deer
 22 Lake, and so the people in Deer Lake are
 23 Newfoundland Power's customers and the people
 24 in Baie Verte are Hydro's customers and
 25 they're saying, oh, we got a rural subsidy

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1 that we're putting on your bill, oh, and
 2 that's associated with recovering the cost of
 3 the customers in Deer Lake, or even use of the
 4 term "rural" in the definition of the subsidy,
 5 this "urban" versus "rural", I mean,
 6 Newfoundland Power has a lot of small rural
 7 areas which are smaller than some of Hydro's
 8 rural areas, and if you took Newfoundland
 9 Power's cost of service study and did it by
 10 region, not necessarily their defined regions,
 11 but more rural regions - if you said let's
 12 take all the communities that are less than
 13 300 people, and let's look at the cost of
 14 those, you'd come up with a fairly large rural
 15 subsidy on Newfoundland Power's system. So
 16 the rural aspect of it, if you wanted to come
 17 up with something that says we've got a rate
 18 equalization policy surcharge or something
 19 like that - I don't know if we'd call it
 20 surcharge, but adjustment, and it's reflecting
 21 government policy that all customers in
 22 Newfoundland and Labrador should have
 23 reasonably priced electricity, so we have a
 24 sharing of it, something like that may have
 25 more appetite, okay, because I don't think

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1 Newfoundlanders necessarily have this problem
 2 with everybody pays a reasonable price, you
 3 know, that just because you're in rural you
 4 should pay more versus urban, so I think
 5 that's more fathomable for me, but not
 6 referring to something as a rural subsidy. I
 7 think it depends on how it's done. With
 8 regard to the people who are not paying the
 9 subsidy but receiving the subsidy, I should
 10 comment on that. I attended the rural rate
 11 inquiry back in '95 and we travelled around
 12 the province to a lot of the towns. You go
 13 into the towns and you have your town hall
 14 meetings, and you're in these towns that have
 15 always been resource suppliers to the island,
 16 right, fishing villages, and mining towns, and
 17 so they're saying, you know, you're using our
 18 resources to support the island, and then
 19 they're saying, you know, we should get
 20 something for that, and you've got the Innu
 21 nation and the Inuit, and they're saying it's
 22 our lands type thing, so there should be a
 23 sharing of resources, you're using our water
 24 from Churchill. So to tell them that they're
 25 being subsidized, they're often quite offended

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1 because they view that you're using their
 2 resources to support the rest of the province,
 3 so there should be something given back too.
 4 So it's a tough call with respect to it. When
 5 I was with Newfoundland Power back in 1996
 6 there was a proposal to introduce a rural
 7 surcharge on the bills. It was opposed by all
 8 intervenors at the time, and it was a hot
 9 topic in the media. It certainly wasn't very
 10 popular, so if something like that was going
 11 to be introduced, I think you'd have to be
 12 very careful about how it's positioned and the
 13 perception of fairness to all parties.
 14 JOHNSON, Q.C.:
 15 Q. Uh-hm. So if it's appropriately described, I
 16 take it that the transparency element is good?
 17 MR. FAGAN:
 18 A. I think it's -
 19 JOHNSON, Q.C.:
 20 Q. It's better than no transparency?
 21 MR. FAGAN:
 22 A. I may disagree with Mr. Brockman on a number
 23 of items, but I do agree with him with regard
 24 to his question on what's the purpose. It
 25 doesn't impact with respect to marginal cost,

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1 it doesn't create an efficiency issue, because
 2 you can still price reasonably to reflect
 3 marginal cost with and without the rural
 4 deficit. So if people believe it's a benefit
 5 that customers know that there's an
 6 equalization approach with regard to rates
 7 across the province, I think most people may
 8 actually already somewhat recognize that
 9 because Newfoundland Power has the same rate
 10 for all its customers, whether they're in
 11 small towns or in large towns, so most people
 12 know that there's economic differences with
 13 regard to the cost to serve customers. I
 14 think that may be just a view of people
 15 already, so I don't know if there's much of a
 16 benefit to it.
 17 JOHNSON, Q.C.:
 18 Q. Dr. Feehan mentioned yesterday that we already
 19 make reference to the northern strategic plan
 20 and the provincial rebate, and we show that on
 21 bills, and presumably that's legitimate use of
 22 the billing process to put that information
 23 there.
 24 MR. FAGAN:
 25 A. Well, the northern strategic plan would have

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1 to be put on bills because it's not an
 2 approved rate of the Board. It's an
 3 adjustment to customers bills in Labrador
 4 based on a government directive, so Hydro is
 5 required to use its published rates for
 6 billing customers in Labrador, so the northern
 7 strategic plan is an adjustment to approved
 8 rates. So you're required to put that on
 9 customers bills. This is more of a cost
 10 within the overall cost of service, so I don't
 11 think that one necessarily is the same thing
 12 as - what was the second one?
 13 JOHNSON, Q.C.:
 14 Q. The second one was the rebate of the
 15 harmonized sales tax.
 16 MR. FAGAN:
 17 A. The rebate of the harmonized sales tax, so it
 18 was called a residential rebate. Yeah, okay.
 19 JOHNSON, Q.C.:
 20 Q. Yeah.
 21 MR. FAGAN:
 22 A. It was a specific item of a credit to
 23 customer's bill. There may be a requirement.
 24 There may be requirement from Government to
 25 identify it separately from a billing

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1 perspective. I'm not sure on that, but it's
 2 possible it may have been. So there may have
 3 been direction on that from Government when it
 4 was implemented for the utilities. But
 5 they're not quite the same because it's an
 6 adjustment that's applying to all customers
 7 bills. What we're dealing with here is
 8 identifying adjustment which separates one
 9 group of customers from another. You're
 10 saying take your -- you're paying higher rates
 11 for another group of customers to have lower
 12 rates, and for the other group of customers,
 13 you're saying we're giving -- these other
 14 group of customers are giving you a break.
 15 So, it's -- they're different. They're
 16 different things. So I don't know if you
 17 could really apply the same practice to the
 18 decision.
 19 JOHNSON, Q.C.:
 20 Q. How aware do you think the customers are?
 21 We've seen the statistics in terms of cost of
 22 recovery in some of these systems, which is
 23 very, very low. I mean, you know, 18 cents on
 24 the dollar, 14 cents. You've seen the stats.
 25 There's no need to go there. But, how -- in

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1 what fashion would this type of information be
 2 getting to the customers who are being
 3 subsidized in fact now, that they're -- that
 4 the amount they pay reflects just a small
 5 portion of the cost?
 6 MR. FAGAN:
 7 A. I think from the customer perspective, you
 8 know, just based on my experience in attending
 9 the rural rate inquiry, the -- we were in
 10 L'Anse au Loup and the people in L'Anse au
 11 Loup were, at the time, paying rates, diesel
 12 rates, okay, and -- but the town of Blanc
 13 Sablon next door, they're paying Hydro Quebec
 14 rates, okay, and so it's really hard for the
 15 businesses up there to compete and they're
 16 saying, you know, we're paying -- having to
 17 pay diesel rates but if someone wants a hotel,
 18 they just go over to Blanc Sablon versus the
 19 hotel in L'Anse au Clair. So, the customers
 20 certainly know about the costs. I mean the
 21 average cost to serve a diesel customer is
 22 around 80 cents a kilowatt hour. So,
 23 everybody knows diesel costs are expensive and
 24 based when we were up there, there was -- it
 25 wasn't that there was a lack of understanding

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1 that the cost to serve them was very high, but
 2 they were viewing it more from, you know,
 3 we're trying to survive here. We're trying to
 4 run businesses, raise our families. So they
 5 were looking for affordable energy.
 6 So, it's a policy thing and Government
 7 made the policy with regard to affordable
 8 energy. So, it's a question, do we take that
 9 Government policy and then try and go out and
 10 tell people more about that Government policy
 11 from an equalization, you're being subsidized
 12 and you're subsidizing someone else. I don't
 13 know. It's difficult because you're somewhat
 14 cherry picking with regard to Hydro because
 15 you could do the same thing for Newfoundland
 16 Power and it's a question really of
 17 Newfoundland Power somewhat because it's their
 18 customers and the customers in Labrador
 19 Interconnected as well, Hydro's. Would they
 20 want to be telling their customers that
 21 they're -- okay, you're subsidizing rural
 22 customers in Labrador, so you're subsidizing -
 23 - because I mean some of Newfoundland Power's
 24 rural systems cost probably more than some of
 25 Hydro's rural interconnected systems, not

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1 systems but areas, pockets.
 2 JOHNSON, Q.C.:
 3 Q. I'm struggling with that, with that parallel
 4 though.
 5 (10:00 a.m.)
 6 MR. FAGAN:
 7 A. Have you driven down Twillingate? Like I
 8 mean, if you drive kilometres, maybe 20-30
 9 kilometres and all you see is poles, right,
 10 and then you get to the town. So, there's
 11 areas like that. I mean, I'm from St.
 12 Joseph's out in St. Mary's Bay and we had a
 13 fish plant which it load was growing, so they
 14 had to come upgrade the substation. Well, the
 15 fish plant closed. So the whole feeder is
 16 upgraded. You got a new substation.
 17 Currently there's probably maybe less than 100
 18 residents, most of them are seasonal. So, you
 19 go look at that and then you go look at some
 20 of Hydro's areas. They're not much different
 21 with regard to -- even in the diesel areas
 22 sometimes that you got to go upgrade the
 23 diesel because there's a fish plant goes in.
 24 But that could happen in interconnected
 25 systems as well and then the fish plants

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1 close. So, the difference between
 2 Newfoundland Power service areas in rural and
 3 Hydro's service areas on the interconnected
 4 system in rural, there's not much difference.
 5 JOHNSON, Q.C.:
 6 Q. But the case of Newfoundland Power's service
 7 area, I mean, that's probably replicated
 8 across the country. Like in say Nova Scotia,
 9 they've got small areas, you know, on the
 10 south shore of Nova Scotia versus Halifax,
 11 Dartmouth, and so I can see the idea of well,
 12 you wouldn't necessarily, you know, put that
 13 on a Nova Scotia power bill or a Newfoundland
 14 Power bill, but I think here, aren't we
 15 talking about something of a different
 16 magnitude altogether?
 17 MR. FAGAN:
 18 A. I don't think so, from the Island
 19 Interconnected because historically, I think
 20 it was -- I don't know if it was 1958 when
 21 they started, the Government was supporting
 22 the development of power and the diesel
 23 systems came into play and so eventually they
 24 started interconnecting and transferring some
 25 of these small systems over to Newfoundland

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1 Power. So, as they were interconnected, some
 2 towns became Newfoundland Power's customers
 3 and I think the principle was when it was
 4 economic to do so, and they wouldn't cause a
 5 big increase in Newfoundland Power's rates.
 6 So, the practice stopped. So some of them
 7 stayed with Hydro, and I'm not sure why the
 8 practice stopped, okay, but a number of the
 9 systems stayed with Hydro to remain
 10 interconnected. Had they all moved to
 11 Newfoundland Power, the Island Interconnected,
 12 well 40 percent of the rural deficit -- now
 13 the cost to serve may not be exactly the same,
 14 there's probably some duplication, but
 15 Newfoundland Power would say have an income
 16 tax expense from its customer where Hydro
 17 doesn't. So the average cost may not be that
 18 much different. If the Island Interconnected
 19 systems moved to Newfoundland Power, they
 20 wouldn't be part of the rural deficit. They'd
 21 be part of Newfoundland Power's rate. So that
 22 would be 25 million off the rural deficit.
 23 So it's -- so from an Island
 24 interconnected perspective and looking at the
 25 rural deficit, and it's a large part of the

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1 rural deficit, identifying one group just
 2 because they're Hydro's rural customers on the
 3 Island interconnected versus Newfoundland
 4 Power's and identifying that as a subsidized
 5 group, it's not much different than breaking
 6 Newfoundland Power's cost of service study
 7 into regions and coming up with rural deficits
 8 itself. That's my view on it.
 9 JOHNSON, Q.C.:
 10 Q. Where the amount of the rural deficit is both
 11 so large and so unconnected to the cost that
 12 these customers are imposing on the system, in
 13 terms of, you know, it's not cost based, the
 14 64 million dollars in terms of the group -
 15 MR. FAGAN:
 16 A. It's a large percentage, yes.
 17 JOHNSON, Q.C.:
 18 Q. Yes, and would there not be like more of a
 19 case where the customer in Labrador
 20 interconnected and on the Island
 21 interconnected, they're not responsible for
 22 these costs. In that circumstance, given the
 23 largeness of it, is there not more of a case
 24 to say, look, we should be transparent about
 25 this; I mean, this is not something that just

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1 arises through normal balancing and cost of
 2 service between customer groups on a system?
 3 MR. FAGAN:
 4 A. It is a large deficit. No one can doubt the
 5 magnitude of the rural deficit, I mean,
 6 because it's -- just the size of it has
 7 created all this debate before the Board. I'd
 8 only be careful about the messaging, that if
 9 you were going to do it, I think there should
 10 be some discussion with Newfoundland Power
 11 first with respect to it because it's their
 12 customers that you're putting the message out
 13 to and if you create this new message, it's
 14 Newfoundland Power is going to get most of the
 15 calls with regard to "explain this new thing
 16 on my bill. Why am I subsidizing these other
 17 customers, these Hydro rural customers on
 18 Isolated systems?" So it's just you don't
 19 want to create unintended consequences. So I
 20 think maybe some research prior to doing it,
 21 that you do some focus groups with customers,
 22 get their opinion on it before you'd move on
 23 something like that. I just wouldn't want to
 24 do it, arbitrarily select it, and then have to
 25 live with the results that were unforeseen.

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1 JOHNSON, Q.C.:
 2 Q. Following up on the issue of the quantum of
 3 the rural deficit, in 2015 it was 64 --
 4 forecast 64 million, in that vicinity. Now I
 5 understand -- if we could bring up CA-NLH-207,
 6 Revision 2 -- this contains -- yeah,
 7 Attachment 1, I'm sorry. If you could go down
 8 the graph a little bit or the table, I should
 9 say. This was filed yesterday and I take it
 10 it's an extract from the 2014 Annual Report on
 11 the Rural Deficit that Hydro filed?
 12 MR. FAGAN:
 13 A. That's correct.
 14 JOHNSON, Q.C.:
 15 Q. Okay. So in fact, the forecast deficit number
 16 is filed with the Board for '16, '17 and '18?
 17 MR. FAGAN:
 18 A. Yes. '16 and '17 are legitimate forecast.
 19 There's uncertainty of the numbers with regard
 20 to '18/19, so it's assumed to be the same as
 21 '17 for purposes of this.
 22 JOHNSON, Q.C.:
 23 Q. Okay. So I guess my question would be we're
 24 forecasting the rural deficit to fall in 2016
 25 to 61 million and 2017 to 59 million. Is that

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1 mainly fuel oriented?
 2 MR. FAGAN:
 3 A. Yeah, I questioned someone on that last night
 4 and I was told it's mainly fuel. I believe
 5 there may have been a reduction, slight
 6 reduction -- this was based on a fuel price
 7 forecast of the \$93 and I believe -- and of
 8 course, the accompanying diesel forecast at
 9 the time. So, when we get out to '16 and --
 10 we get out to '17, '16 and '17, the fuel price
 11 was slightly less.
 12 JOHNSON, Q.C.:
 13 Q. Okay. So I guess the -- I guess my question
 14 would be that would Hydro be over collecting
 15 from customers if the 2015 test year is based
 16 on 64,070,000, according to this table for
 17 2015? Would we be -- Hydro be over collecting
 18 as rates go into effect?
 19 MR. FAGAN:
 20 A. It's also my understanding that this reflects
 21 a lower ROE in future years because this -- we
 22 call it a fallout calculation. That it's
 23 assuming the rates that are proposed go into
 24 play, but additional costs would also be
 25 incurred and it's not effectively maintaining

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1 Hydro's return on equity at 8.8 percent for
 2 the subsequent years. So that's actually --
 3 if you were redoing a test year every year,
 4 then you'd maintain the ROE at 8.8 percent and
 5 that rural deficit number would be higher.
 6 But Hydro wouldn't be achieving that rural
 7 deficit -- that return on equity and that's
 8 causing somewhat of a contributing to a
 9 reduction in the rural deficit.
 10 JOHNSON, Q.C.:
 11 Q. But I guess, as a matter of fact, the rates
 12 will be reflecting a rural deficit of 64
 13 million, but the anticipated rural deficit
 14 will be about three to four million dollars
 15 less in 2016 and 2017 respectively?
 16 MR. FAGAN:
 17 A. To achieve the 8.8 percent ROE in the proposed
 18 return on rate base, the rural deficit would
 19 be 64 million. There's other cost changes
 20 going forward in '16 and '17 and the return on
 21 equity, it's an output rather than an input
 22 into deriving the numbers, and so that
 23 combined with the fuel price decline would be
 24 -- would contribute to that. Now, Hydro's
 25 proposed a deferral account for fuel price

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1 differences on the Isolated systems.
 2 Now, I believe Hydro's return on equity
 3 or return on rate base has been proposed to be
 4 plus or minus 20 basis points, which is
 5 equivalent to approximately three million
 6 dollars, plus or minus three to three and a
 7 half million dollars, that's my understanding.
 8 So, if -- when this was prepared, the fuel
 9 price was based on \$93 a barrel for No. 6
 10 fuel, which is fairly correlated to the cost
 11 of diesel fuel. If fuel price declined and
 12 Hydro's deferral account was approved, then
 13 the savings associated with the fuel price
 14 decline would go back to customers through the
 15 deferral account.
 16 Now, Hydro is at a position where fuel
 17 costs have declined, so we're down to a No. 6
 18 of around \$70 a barrel and correspondingly,
 19 the No. 2 serving diesel areas would also
 20 decline. So we're in a lower area now and if
 21 the Board approved rates based on these lower
 22 fuel costs without the deferral account and
 23 fuel costs go up, then Hydro would effectively
 24 have to eat those costs which will reduce
 25 return. If the deferral account was approved,

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1 then the additional costs would be recovered.
 2 So, when you don't have a deferral account to
 3 deal with fuel cost variances, as we currently
 4 don't on Isolated systems, there's a risk
 5 associated with it. If you're going in high
 6 where we got to do a fuel price forecast,
 7 Hydro would keep the savings. If you're going
 8 in low, Hydro will have to incur the costs as
 9 they increase.
 10 I mean, when Hydro filed this application
 11 in November 2014, it was mentioned it was
 12 based on the 93.32 and I think the No. 2 fuel
 13 cost in that was 18.8 million dollars. Hydro
 14 filed an interim rate application only a few
 15 months later based on a \$63 a barrel No. 6
 16 fuel and we also reflected 3.6 million
 17 savings, I believe, of No. 2 fuel just in a
 18 few months, which is more than the full 20
 19 basis points of return. So this just
 20 contributes to the argument with respect to
 21 having a deferral account to deal with fuel
 22 cost variances in Isolated systems. If you
 23 want the savings with regard to that fuel
 24 price difference, deferral account would be
 25 appropriate.

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1 JOHNSON, Q.C.:
 2 Q. So Mr. Fagan, the numbers that we're seeing
 3 for forecast 2016 and 2017, these are stale
 4 numbers?
 5 MR. FAGAN:
 6 A. Well, they're based on the forecast at the
 7 time of filing the return, yes.
 8 JOHNSON, Q.C.:
 9 Q. Right, and would a more recent forecast be
 10 available for the 2016 and 2017 forecast rural
 11 deficits?
 12 MR. FAGAN:
 13 A. I think we would -- in order to do that, you'd
 14 have to redo the whole cost of service study
 15 based on complete updated costs because rural
 16 deficit isn't just fuel costs, it's allocation
 17 of all your costs, your overheads, all your
 18 operating costs in the diesel areas as well.
 19 So, it may be higher on fuel in this
 20 particular forecast, but if you update it, it
 21 may not necessarily go down because other
 22 costs may go up to offset it. But, no, I
 23 would say there's not right now because we
 24 don't have an updated cost of service study
 25 reflecting new 2016 numbers to provide and

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1 estimate.
 2 JOHNSON, Q.C.:
 3 Q. Would it be possible to file a forecast for
 4 2016 and 2017, the change that would be made
 5 if you just adjusted the fuel?
 6 MR. FAGAN:
 7 A. I can inquire.
 8 JOHNSON, Q.C.:
 9 Q. Okay.
 10 MR. FAGAN:
 11 A. Okay, I'll check.
 12 JOHNSON, Q.C.:
 13 Q. Turning to specifically assigned O&M for a
 14 moment, Mr. Fagan, could I bring you to the
 15 rate schedule section of the application,
 16 specifically page six of 46? Yeah, there we
 17 are, okay.
 18 So just to understand here, this is your
 19 -- the rate schedules attached to your
 20 Application and it provides the specifically
 21 assigned charges for customer plant and
 22 service that is specifically assigned to the
 23 customer and we see: Corner Brook Pulp and
 24 Paper, 891,000; North Atlantic Refinery
 25 Limited 91,000; Teck 208; and Vale 499. Can

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1 you confirm, Mr. Fagan, that Hydro is seeking
 2 -- is actually seeking approval from the Board
 3 for the charges that are set out here in this
 4 schedule?
 5 MR. FAGAN:
 6 A. That's reflected in the Application, yes.
 7 JOHNSON, Q.C.:
 8 Q. That's right. So that's what are you seeking,
 9 Hydro is seeking in this Application? That's
 10 not been amended and not intended to be
 11 amended?
 12 MR. FAGAN:
 13 A. Well, Hydro's filed its application based on
 14 its standard approach to preparing the cost of
 15 service, I'd say with the exception probably
 16 of the rural deficit, which is proposed for
 17 change. But there's been additional evidence
 18 obviously provided by Mr. Dean and there was a
 19 number of RFIs on this matter and if we can
 20 bring up Vale-083, please?
 21 So Mr. Dean has identified the concern
 22 with respect to, I guess, the intuitive effect
 23 that because assets, new assets in the current
 24 cost of service methodology are reflecting a
 25 higher proportion of O&M which is certainly

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1 not intuitive because the customers got a new
 2 asset, so higher O&M gets allocated to them
 3 and it's based on the fact that the
 4 methodology uses the O&M as a percentage of
 5 the original cost. So, Hydro hasn't reflected
 6 -- amended this application to reflect that.
 7 I mean, Mr. Greneman has recognized that
 8 there's -- Mr. Dean's proposal is credible, I
 9 think, that it's -- adjusting the numbers to
 10 real dollars in calculating the O&M percentage
 11 would probably be fairer.
 12 But this is somewhat of a new issue
 13 before the Board and I know Hydro's employed
 14 the same calculation approach to its O&M
 15 percentages historically, but the fact that
 16 when you've got a new customer comes on just
 17 before a test year and you've got this
 18 investment of 10 or 11 million dollars for an
 19 industrial customer, all of a sudden this kind
 20 of jumped out at us. So it wasn't -- I think
 21 it was probably not reviewed closely enough
 22 with regard to the components and whether it
 23 was a reasonable number upfront, but I think
 24 Hydro recognizes that it's probably not really
 25 a fair approach with respect to specifically

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1 assigned charges.
 2 We haven't filed an application to change
 3 anything as of yet, but I don't know every
 4 time we get into a discussion of a particular
 5 issue before the Board and we realize that
 6 something else has merit and we're supportive
 7 of it, should we automatically amend the
 8 application or just say, "yeah, his
 9 recommendation has merit. The Board should
 10 consider it and in their final order of the
 11 Board."
 12 So, what Mr. Dean has presented seems
 13 like a reasonable approach and if we bring up
 14 -- actually, if we go to that table for a
 15 minute near the end of that, so if you do a
 16 bit of comparison of some of the dollars. The
 17 direct transmission O&M expense, I think maybe
 18 the last table summarizes it all. Yeah, total
 19 transmission, so we've got direct as well as
 20 administration and channel. So, we see -- now
 21 this is only the 212 versus the 70.
 22 JOHNSON, Q.C.:
 23 Q. What RFI is this one? Okay.
 24 MR. FAGAN:
 25 A. Is there another table, Table 4, please?

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1 Specifically assigned O&M, okay. So in our
 2 cost of service study, if we go to the third
 3 column under the first section, per 2015 cost
 4 of service study. Vale has 436,000 O&M costs
 5 allocated to it. Now these are legitimate O&M
 6 costs of Hydro with respect to the test year
 7 because we've got the full O&M costs in the
 8 cost of service study but it's been allocated
 9 among the parties. It's not like the O&M
 10 costs don't exist. It's just the way we're
 11 allocating it among the parties. So we're
 12 allocating to the specifically assigned assets
 13 here, 2.5 million, which is the third column
 14 at the bottom. And of that, Vale is getting
 15 436,000 and that's driven materially because
 16 of the newness of the assets.
 17 So if we go over to the alternate method
 18 which adjusts for real dollars, so it's real
 19 dollars rather than original costs, it's
 20 145,000 for Vale versus 436. So the magnitude
 21 of the difference is pretty large. It almost
 22 reminds me somewhat of the rural deficit
 23 argument that we look at it and say the
 24 difference is just so large that, you know, it
 25 begs the question is it reasonable. And

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1 there's been some discussion about whether
 2 there's any precedent for dealing with this
 3 before the Board. I wonder if you could bring
 4 up Vale-125 for a minute, please?
 5 MS. GRAY:
 6 Q. 125?
 7 MR. FAGAN:
 8 A. Yeah, 125 is the last RFI, I believe, from
 9 Vale. No, the -- I don't know if it's on the
 10 Board's website yet, but there is a Vale-125.
 11 Okay. So there's a question here about the
 12 use of indexing approved by the Board in the
 13 past, and the -- so if we just move down to
 14 the response?
 15 So Newfoundland Power's contribution in
 16 aid of construction policy or CIAC policy in
 17 determining its charge to customers that pay
 18 contributions, it's based on a capital cost
 19 but also includes a O&M portion assumed over
 20 the life of the asset, and in determining the
 21 O&M portion, because actually the approach
 22 that Mr. Dean is proposing is consistent with
 23 the approach used and approved by the Board
 24 for determining the charges for Newfoundland
 25 Power that they use. They index the costs

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1 upon the Handy-Whitman index to the original
 2 cost of distribution index -- of the
 3 distribution asset, sorry. So, because the
 4 approach that Hydro uses now for specifically
 5 assigned charges is consistent with what was
 6 used in Newfoundland Power's CIAC policy up to
 7 I think September of 1997 and there was a
 8 change in the policy at that time to move to
 9 the indexing approach. The O&M percentages
 10 were materially higher for the customers
 11 paying contributions and it was determined
 12 that it should be changed, so it was changed
 13 in 1997 for Newfoundland Power.
 14 So what he's presenting has been dealt
 15 with in a different context before but the
 16 principle is the same.
 17 JOHNSON, Q.C.:
 18 Q. Okay. Let's just backup for a bit now,
 19 because you've jumped right into it and made a
 20 case for Vale.
 21 MR. FAGAN:
 22 A. All I said was that the application hasn't
 23 been amended, but the Board can rule on it
 24 without Hydro amending the application.
 25 JOHNSON, Q.C.:

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1 Q. Okay, very good. Now, Mr. Fagan, when Hydro
 2 undertook construction of the Vale connection
 3 facilities, do you know whether an estimate of
 4 the specifically assigned capital and O&M
 5 costs were provided to Vale?
 6 MR. FAGAN:
 7 A. I don't know.
 8 JOHNSON, Q.C.:
 9 Q. Okay. Who would know that?
 10 MR. FAGAN:
 11 A. It could be Mr. Humphries.
 12 JOHNSON, Q.C.:
 13 Q. Okay. And are you familiar with Hydro's
 14 procedure relating to new customer connections
 15 for like an industrial customer? What's the
 16 procedure that happens?
 17 MR. FAGAN:
 18 A. Well, generally -- now I'm not directly
 19 involved, but I can -- based on my knowledge,
 20 I'll give you my best response. New
 21 industrial customers, the most recent practice
 22 certainly is that new industrial customers
 23 come on and pay full contribution for their
 24 assets. So Vale paid full contribution
 25 effectively for the new assets provided

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1 initially to serve them, that are specifically
 2 assigned assets.
 3 JOHNSON, Q.C.:
 4 Q. Okay.
 5 MR. FAGAN:
 6 A. So specifically assigned charges for
 7 customers, when the assets are provided by
 8 Hydro, for example, with the frequency
 9 converter for Corner Brook Pulp and Paper
 10 which was many years ago, and all the assets
 11 and the investment over time, Hydro -- the
 12 specifically assigned charge is based on a
 13 return on the asset plus depreciation, plus
 14 O&M charges. When a customer pays a
 15 contribution to recover the capital
 16 investment, then there's no return and there's
 17 no depreciation. The customer only pays the
 18 specifically assigned charges.
 19 As capital is invested over time for the
 20 assets, if the customer doesn't pay for it and
 21 Hydro pays for it, it goes in and determines a
 22 return over time. But, for Vale, the vast
 23 majority of the charge is associated with the
 24 O&M because pretty well all the assets on
 25 Hydro's books would pretty well close to have

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1 been almost fully paid for by Vale. So,
 2 that's just -- so that's -- I just wanted to
 3 give a background on the approach.
 4 With regard to the -- so in Vale's case,
 5 which I think also probably would have been
 6 Teck's at the end of the day, they would have
 7 paid their full contribution on the assets.
 8 So, what they've been paying for would be O&M
 9 charges.
 10 JOHNSON, Q.C.:
 11 Q. Okay. But to your knowledge, part of Hydro's
 12 procedure in dealing with a Teck or a Vale
 13 would be to actually say "now, listen, this is
 14 how O&M costs are calculated and this is what
 15 they would likely be"? Would that be your
 16 understanding?
 17 MR. FAGAN:
 18 A. Well, the customers are certainly informed
 19 that they've got to pay O&M. With regard to
 20 the detail of the calculation of O&M, it'd
 21 never get into the detail of whether it would
 22 have been based on the original cost versus
 23 the real dollars aspect of it. So, the
 24 principle of the specifically assigned charges
 25 is that they're going to be paying it. The

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1 customers are aware of that.
 2 JOHNSON, Q.C.:
 3 Q. And they would be told that it would be in
 4 accordance with Board approved methodology?
 5 Wouldn't they be told that?
 6 MR. FAGAN:
 7 A. Oh, I expect so, yes.
 8 JOHNSON, Q.C.:
 9 Q. Yeah, okay. So we can follow up some of that
 10 with Mr. Humphries.
 11 MR. FAGAN:
 12 A. But I mean, at this stage, we're considering
 13 what the Board approved methodology would be.
 14 JOHNSON, Q.C.:
 15 Q. Right, and it would be your evidence, as we've
 16 heard from others, that Hydro's rules on O&M
 17 contributions, that would be -- for
 18 specifically assigned assets, that would be
 19 generally in keeping with what we see in other
 20 jurisdictions? Is that right?
 21 MR. FAGAN:
 22 A. Well, I asked Mr. Greneman to review and so he
 23 did some investigation and he had difficulty
 24 finding information with regard to
 25 specifically assigned charges for Industrial

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1 Customers. Hydro's approach of allocating O&M
 2 within the cost of service study, excluding
 3 the issue of specifically assigned charges,
 4 according to Mr. Greneman is clearly
 5 consistent with what's done in industry
 6 practice. Specifically assigned charges and
 7 recovering O&M costs for industrial customers,
 8 sometimes it's my understanding is done
 9 differently. Sometimes you may have an
 10 agreement with a customer that you could have
 11 it that you'll do the O&M and you bill them on
 12 an as-required basis, and there may be some
 13 fixed amount that you're trying to recover
 14 your administration and general costs type of
 15 thing. So you may have a fixed amount, but
 16 you may have a premium based on the amount
 17 required, which would be outside of a cost of
 18 service study allocation. That could cause
 19 O&M costs to go up or down, depending on the
 20 amount of activity over the years. If
 21 customers want more stability with regard to
 22 what their O&M would be, you could have it set
 23 up so it comes out of the cost of service and
 24 so you pretty well know what it's going to be
 25 between test years. So there's different

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1 approaches to dealing with it. He had
 2 difficulty finding much information on
 3 practices in other jurisdictions with respect
 4 to industrial customers.
 5 JOHNSON, Q.C.:
 6 Q. And certainly was not able to find an instance
 7 where Mr. Dean's methodology had been adopted
 8 in another jurisdiction for Industrial
 9 Customers?
 10 MR. FAGAN:
 11 A. No, he wasn't.
 12 JOHNSON, Q.C.:
 13 Q. Right. And so just to understand, now Mr.
 14 Dean is Vale's witness. He's indicated he's
 15 not an expert witness but he has come up with
 16 this new methodology and he would like that to
 17 be implemented in this GRA or he can live with
 18 the Hydro \$150,000 figure. So are you telling
 19 us that Hydro is now comfortable with the
 20 Board just getting on with it and making a
 21 change to the methodology now in this
 22 proceeding?
 23 MR. FAGAN:
 24 A. Well, I wasn't close to Hydro's methodology on
 25 specifically assigned O&M when I moved over to

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1 Hydro. When Mr. Dean identified his concern
 2 in his evidence, I looked at it, and I said
 3 "oh, I've seen that before" because I recalled
 4 the CIAC policy issue that we recognized the
 5 problem and made the change back in 1997. So,
 6 I saw the merits of his position at that time,
 7 but I wasn't close -- I wasn't involved with
 8 regard to the original filing with respect to
 9 the standard approach, so it wasn't looked at
 10 closely before Hydro filed its application. I
 11 think what he's provided is a reasonable
 12 thing, a reasonable certainly starting point
 13 and if we want to look at it further in the
 14 cost of service methodology review, we've
 15 actually put that in our scope of our review.
 16 JOHNSON, Q.C.:
 17 Q. Yeah.
 18 MR. FAGAN:
 19 A. But that's probably not a bad starting point.
 20 JOHNSON, Q.C.:
 21 Q. Yeah, and that's what Mr. Greneman said. It's
 22 the discussion piece, but I mean, by no -- I
 23 mean, I never heard Mr. Greneman saying well
 24 now let's get on with it here now, Board, make
 25 this change for the Vale.

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1 MR. FAGAN:
 2 A. With respect to Mr. Greneman's statement on
 3 discussion piece, he was referring to his
 4 rebuttal evidence is my understanding. His
 5 rebuttal evidence where he presented an
 6 adjustment approach going back to 2007 as a
 7 discussion piece. I was under the impression
 8 that he thought Mr. Dean's approach was
 9 reasonable, but you can check the transcript.
 10 JOHNSON, Q.C.:
 11 Q. But let me just get this right now. To answer
 12 my question, Mr. Fagan, is Hydro now in favour
 13 in this proceeding of having the Board make a
 14 change to the specifically assigned cost
 15 methodology such as suggested by Mr. Dean?
 16 (10:30 a.m.)
 17 MR. FAGAN:
 18 A. Hydro believes Mr. Dean's approach would be a
 19 good approach to start with until it can be
 20 further reviewed in the cost of service
 21 methodology hearing, and so change the
 22 approach now and use that until it's further
 23 reviewed in the cost of service methodology
 24 hearing.
 25 JOHNSON, Q.C.:

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1 Q. Okay. So we would go, what, to Mr. Dean's
 2 \$85,000 a year? Is that what we'd do now?
 3 MR. FAGAN:
 4 A. Let's go back to the RFI, Vale-083. No, it's
 5 not \$85,000 a year. Table 4 would show the
 6 specifically assigned O&M portion of the
 7 charge being \$145,000.
 8 JOHNSON, Q.C.:
 9 Q. Yeah, but that's the method that Hydro came
 10 back with, but I think Mr. Dean confirmed in
 11 his evidence that he thought it was -- I
 12 thought it was 87,000 or something.
 13 MR. FAGAN:
 14 A. Mr. Dean didn't have all the numbers to do the
 15 analysis. Actually, when the RFI started,
 16 Hydro had difficulty finding the data that Mr.
 17 Dean was requesting to do the analysis. We
 18 checked with someone who was retired and they
 19 actually told us where we could find the
 20 information. So we managed to do what Mr.
 21 Dean requested because we found the data that
 22 he was requesting us to do the analysis on.
 23 So, this is applying Mr. Dean's analysis to
 24 I'll call it more full data and Mr. Dean was
 25 coming up with some estimates, I understand.

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1 JOHNSON, Q.C.:
 2 Q. Okay. And I take it that to your point, you
 3 indicated a few moments ago that the total
 4 cost of the O&M of 436,000, that doesn't go
 5 away. It's just that Vale pays less of it?
 6 MR. FAGAN:
 7 A. Yes, it's a real O&M cost incurred by Hydro
 8 that's currently being considered specifically
 9 assigned, but based on the information that we
 10 looked at here, one review that rather than
 11 having 2.5 million dollars of O&M costs as the
 12 total at column three being specifically
 13 assigned O&M, we think it would be more
 14 reasonable to have 1.9 million which is the
 15 total at the bottom being specifically
 16 assigned. So Hydro would revise its cost of
 17 service to reflect that for purposes of
 18 determining specifically assigned charges. I
 19 don't know if I lost you there, Mr. Johnson.
 20 JOHNSON, Q.C.:
 21 Q. No, you didn't lose me. So, then the balance
 22 then, that just gets picked up by Newfoundland
 23 Power and these other customers. They pick up
 24 the extra 600,000 bucks?
 25 MR. FAGAN:

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1 A. Well, the other 600 -
 2 JOHNSON, Q.C.:
 3 Q. In large part.
 4 MR. FAGAN:
 5 A. The other 600,000 would go into the pot to be
 6 allocated as common, which would be mostly to
 7 Newfoundland Power, some to Hydro rural, some
 8 to Industrials as well, but yes, the same as
 9 other costs. Because Mr. Dean's analysis or
 10 his methodology would indicate that those were
 11 putting too much costs in has specifically
 12 assigned from an O&M perspective and they
 13 should be common.
 14 JOHNSON, Q.C.:
 15 Q. Has Hydro called Vale up in Sudbury to see how
 16 they do it up there? Mr. Dean, he's been
 17 retained by Vale. He told us he didn't call
 18 them and find that out. Do you guys know
 19 that?
 20 MR. FAGAN:
 21 A. No.
 22 JOHNSON, Q.C.:
 23 Q. No. And has Hydro determined -- has Hydro
 24 done any studies comparing O&M costs of
 25 facilities that are from one to five years of

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1 age or from five to ten years of age, 10 to
 2 15, et cetera, to determine the cost
 3 differences of things like terminal stations,
 4 transformers and transmission lines?
 5 MR. FAGAN:
 6 A. Ask that of maybe the operations panel.
 7 JOHNSON, Q.C.:
 8 Q. You're not aware of though in terms of your
 9 analysis of the O&M issue?
 10 MR. FAGAN:
 11 A. No.
 12 JOHNSON, Q.C.:
 13 Q. No. And Mr. Greneman wasn't?
 14 MR. FAGAN:
 15 A. No.
 16 JOHNSON, Q.C.:
 17 Q. Mr. Fagan, it just seems to me that, you know,
 18 this is a fairly significant change that you'd
 19 be inviting the Board to make when it's -- I
 20 don't think it's -- I put it to you, I don't
 21 think it's been adequately studied. If you
 22 can't say that you've even looked at the
 23 differences in O&M costs from one to five or
 24 five to ten, you know, we don't know -- I
 25 think there's a number of things we don't know

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1 about this and I'm just wondering wouldn't
 2 this really be better just properly studied?
 3 I mean, maybe Vale has a point; maybe they
 4 don't. But wouldn't it be better looked at in
 5 the cost of service study?
 6 MR. FAGAN:
 7 A. Well, I know when we -- I only be from my
 8 experience that we looked at it when we were
 9 doing it at Newfoundland Power with respect to
 10 contributions in aid of construction and we
 11 thought using real dollars in the analysis
 12 made more sense, and so the change was
 13 approved, and so the principle of the O&M
 14 versus the O&M approach proposed by Mr. Dean
 15 is exactly the same. So, I think to me it's
 16 more of -- there's clearly some issues.
 17 There's issues with the current methodology in
 18 that it's charging more O&M to a customer with
 19 new assets which one would indicate we'd like
 20 to get less O&M. So the -- so that, just that
 21 issue itself, and that's why that change was
 22 made at Newfoundland Power, that you were
 23 charging too much O&M costs to customers that
 24 were paying contributions, which is
 25 effectively a specifically assigned asset when

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1 you're charging someone a contribution for it.
 2 So it's the same principle.
 3 So, I think from a principle perspective,
 4 starting with this, like if -- here's my
 5 struggle. Vale doesn't pay a specifically
 6 assigned charge right now. So you're starting
 7 them out with a \$436,000 specifically assigned
 8 charge on a methodology which you really can't
 9 support because it's based on a presumption
 10 that because they've got new assets which are
 11 higher costs than the original cost of the
 12 assets that are there for 20 or 30 years that
 13 they should pay a higher O&M charge, and it's
 14 really hard to defend that. I mean, to me,
 15 being able to explain the rationale of a rate
 16 to a customer and say "okay, this is why this
 17 rate makes sense" is an important component of
 18 communicating with the customer. If you can't
 19 defend your approach to the charge, I'd have a
 20 hard time proposing it.
 21 JOHNSON, Q.C.:
 22 Q. But I mean, again though, you're making that
 23 statement in the context of Hydro not having,
 24 to your knowledge, studied whether there's a
 25 difference in O&M costs at various time

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1 intervals on the equipment in question.
 2 MR. FAGAN:
 3 A. Well, even if you did, which I expect you'd
 4 find the difference, I think there was -- when
 5 Teck Resources announced that they were
 6 closing their operations, I phoned out to one
 7 of our operations people and said "okay, what
 8 will we do with that Teck line because you
 9 know, now that the business is closing?" and
 10 he said "gee," he said, you know, "why would
 11 we take it down." He said "it's pretty well a
 12 new line. We haven't even started our
 13 inspections on that yet. We do this one
 14 flyover once a year type thing. So" he said
 15 "there's very little operating and maintenance
 16 costs associated with it." He said "we're
 17 just starting to get into that now going
 18 forward." So, he said "I don't know why you'd
 19 want to go taking it down now. I mean, it
 20 could be used for some other business may want
 21 to start" type thing.
 22 So, when -- just based on my discussions
 23 with the field people about O&M practices for
 24 transmission lines would somewhat support the
 25 concept that the schedule which Mr. -- the

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1 operations panel could probably talk to more
 2 that you don't have a lot of O&M for the
 3 initial years for your transmission assets.
 4 So it just doesn't seem practical to me that
 5 you're ramping up your O&M costs charging to
 6 the customer in advance of really implementing
 7 your maintenance plan.
 8 JOHNSON, Q.C.:
 9 Q. You know, I appreciate the anecdote, Mr.
 10 Fagan, but it's hardly -
 11 MR. FAGAN:
 12 A. It's the truth.
 13 JOHNSON, Q.C.:
 14 Q. - a substitute for analysis though.
 15 MR. FAGAN:
 16 A. Well, the analysis has been done -- like I
 17 mentioned, if we go to Vale-125 that the
 18 methodology has been changed to reflect real
 19 dollars because of the problem on the CIAC
 20 policy at Newfoundland Power because of the
 21 problem with using original cost in the
 22 calculation. So that principle has been
 23 accepted in this jurisdiction and approved by
 24 the Board. So, I don't think the principle
 25 changes whether it's for contribution in aid

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1 of construction versus for O&M for a new
 2 customer coming on that's an industrial
 3 customer of Hydro.
 4 JOHNSON, Q.C.:
 5 Q. So in essence, you're saying do it and then
 6 we'll study in cost of service as well?
 7 MR. FAGAN:
 8 A. All I'm saying is that the current methodology
 9 that we have got presented to the Board in the
 10 application appears to have a flaw based on
 11 what's been analyzed already with respect to
 12 determining Newfoundland Power's contribution
 13 policy and so, just hitting the customer with
 14 the charge recognizing the flaw in the policy
 15 doesn't seem to be a reasonable approach. Mr.
 16 Dean's method, which is consistent with the
 17 methodology that's used by Newfoundland Power,
 18 is probably a good starting point until we do
 19 a more comprehensive review of specifically
 20 assigned charges for industrial customers as
 21 part of the cost of service methodology
 22 review.
 23 JOHNSON, Q.C.:
 24 Q. Mr. Fagan, I don't know if we should take this
 25 up with another panel, perhaps you can tell

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1 me, but what does Hydro's average OM&A
 2 represent as a percentage of capital costs on
 3 the transmission system? Would that be best
 4 for Humphries, the Humphries panel?
 5 MR. FAGAN:
 6 A. Humphries or Mr. Henderson, yeah.
 7 JOHNSON, Q.C.:
 8 Q. Have you had cause to look at how Hydro's
 9 average OM&A as a percentage of capital cost
 10 compares to Mr. Dean's proposed methodology?
 11 MR. FAGAN:
 12 A. Well, the actual analysis in Mr. Dean's
 13 methodology is really similar to what you're
 14 talking about because what we're dealing with
 15 here is our test year operating and
 16 maintenance relative to the historical capital
 17 expenditures put in the same dollar terms. So
 18 to me, that is really, from a long-term
 19 average, what you're talking about, because
 20 the OM&A that Hydro is putting forward in its
 21 test year is not solely associated with its
 22 current capital expenditures. It's related --
 23 it's more related to historic capital
 24 expenditures. So, what we're presenting here
 25 with regard to expressing it in real dollars

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1 would be a reasonable representation of what
 2 the operating and maintenance costs are as a
 3 percentage of historical asset investment
 4 expressed in the same dollar terms.
 5 JOHNSON, Q.C.:
 6 Q. The service agreement with Vale is attached to
 7 Order P.U. 6(2012), in particular Schedule A
 8 of that particular Board Order. Mr. Fagan,
 9 the ramp-up period is defined in 1.01(s) means
 10 "the time required from the start of
 11 processing of ore concentrate to the time that
 12 the customer's Long Harbour facilities meets
 13 its full capacity as determined in accordance
 14 with Article 2.06(c) and (f)". So do you know
 15 when the ramp-up period started?
 16 MR. FAGAN:
 17 A. That issue is probably better for Mr.
 18 Humphries' panel.
 19 JOHNSON, Q.C.:
 20 Q. Okay.
 21 MR. FAGAN:
 22 A. Now I'm familiar with the fact that they're
 23 not paying a firm -- establishing a firm
 24 demand that's being reset as they ramp up, but
 25 with respect to the details on the actual

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1 ramp-up period, Mr. Humphries' panel.
 2 JOHNSON, Q.C.:
 3 Q. Okay. And he could also tell us when the
 4 ramp-up period would have ended?
 5 MR. FAGAN:
 6 A. Yes.
 7 JOHNSON, Q.C.:
 8 Q. Okay. Do you know if the ramp-up period has
 9 ended?
 10 MR. FAGAN:
 11 A. No, I'm pretty sure it hasn't.
 12 JOHNSON, Q.C.:
 13 Q. It hasn't, okay.
 14 MR. FAGAN:
 15 A. But it's best to check with him, but I don't
 16 think so.
 17 JOHNSON, Q.C.:
 18 Q. Okay. Now you've indicated that Teck
 19 Resources is closing operations. Are they
 20 closing or are they closed or what's the
 21 status of that?
 22 MR. FAGAN:
 23 A. It's my understanding that they're -- well,
 24 they've reduced -- they're no longer in
 25 production, so I thought it's more of a clean-

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1 up phase, environmental clean up for the next
 2 year or so.
 3 (10:45 a.m.)
 4 JOHNSON, Q.C.:
 5 Q. Okay. I notice under the agreement with Vale
 6 in 15.04(b) that it indicates that "subject to
 7 Article 10, if the customer voluntarily or
 8 forcibly abandons its operations, commits an
 9 act of bankruptcy or liquidates its assets,
 10 then there shall be forthwith become due and
 11 payable to Hydro by the customer a stipulated
 12 and liquidated damages without burden of proof
 13 thereof, a lump sum equal to .85 of its then
 14 billing demand for firm power at the firm
 15 power demand charge multiplied by 24, plus the
 16 remaining net book value of the specifically
 17 assigned plant less its salvage value net of
 18 any contributions towards that value made by
 19 the customer."
 20 Is there a similar provision in the Teck
 21 agreement, do you know?
 22 MR. FAGAN:
 23 A. I'm not the best person to talk about the
 24 agreements, but I would anticipate there
 25 probably is, but Mr. Humphries would probably

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1 be the best one to talk to that.
 2 JOHNSON, Q.C.:
 3 Q. Okay.
 4 MR. FAGAN:
 5 A. I think that's probably more of a standard
 6 term.
 7 JOHNSON, Q.C.:
 8 Q. Okay. Mr. Fagan, turning for a moment to the
 9 Corner Brook Pulp and Paper co-generation
 10 costs and just a few very brief questions on
 11 that. We've heard that these costs are in the
 12 cost of service study for 2015.
 13 MR. FAGAN:
 14 A. That's correct.
 15 JOHNSON, Q.C.:
 16 Q. And these costs are allocated to customers as
 17 common? Is that right?
 18 MR. FAGAN:
 19 A. That's correct.
 20 JOHNSON, Q.C.:
 21 Q. Okay. And it's around 10 million dollars in
 22 the test year? Is that right?
 23 MR. FAGAN:
 24 A. That's correct. I think it's in Schedule 6 of
 25 regulated activities.

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1 JOHNSON, Q.C.:

2 Q. Okay. And so, these would be costs of course

3 that'll be picked up by Newfoundland Power,

4 Vale, North Atlantic Refinery, in due course?

5 MR. FAGAN:

6 A. Well, they're purchased power costs.

7 JOHNSON, Q.C.:

8 Q. Yes.

9 MR. FAGAN:

10 A. So, each year. They're reflected in the test

11 year.

12 JOHNSON, Q.C.:

13 Q. Okay. And would you be able to provide an

14 undertaking indicating what each of

15 Newfoundland Power, Vale, and NARL will be

16 picking up from that purchase cost?

17 MR. FAGAN:

18 A. I can. But I can give you a high level

19 description, I mean, if we brought up, I

20 believe it's Schedule 6 to the regulated

21 activity. Okay. The ten million -- I'm okay

22 with -- move over to the right.

23 The 10,281,000 is the purchase power cost

24 reflected in the test year. Now there's 51

25 gigawatt hours forecast, so that's

Page 86

1 approximately 20 cents per kilowatt hour. So

2 that's the purchase power price in the test

3 year. Now, the purchases from Corner Brook

4 co-gen reduce the purchases in the test year

5 assumed for Holyrood and the average Holyrood

6 cost is around 15 cents per kilowatt hour in

7 the test year, based on the \$93 a barrel. So

8 there's a five cent premium with respect to

9 the purchases for Corner Brook co-gen. So if

10 you took the five cent premium and applied it

11 to the 51 gigawatt hours, you get about 2.5

12 million dollars and I think in the test year,

13 the revenue requirement on the Island

14 Interconnected system is around 620 million

15 dollars.

16 So it's about a .4 percent impact, which

17 would generally be pretty close across all

18 customers because I think the purchases from

19 Corner Brook co-gen and the purchases from

20 Nalcor, purchases in general, have been

21 classified based on system load factor. So,

22 it's split between demand and energy and

23 system load factors. So, it's spread over

24 both demand and energy. So the .4 percent is

25 a fairly good number on what the impact on

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1 customer rates is of the premium associated

2 with purchases from Corner Brook co-gen.

3 JOHNSON, Q.C.:

4 Q. But the premium was actually larger than five

5 cents because, as you say, the 15 cent

6 Holyrood figure is based on the \$92 a barrel.

7 MR. FAGAN:

8 A. In the application, yes.

9 JOHNSON, Q.C.:

10 Q. Yes.

11 MR. FAGAN:

12 A. Yes. Now, if the price drops to \$70, so

13 you're down closer to slightly less than 12

14 cents, so the premium would be more like eight

15 in that particular circumstance.

16 JOHNSON, Q.C.:

17 Q. Yes.

18 MR. FAGAN:

19 A. So then you're into about four million dollars

20 over the six -

21 JOHNSON, Q.C.:

22 Q. Right.

23 MR. FAGAN:

24 A. So then you're into about .6, so between .4 to

25 .65 percent.

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1 JOHNSON, Q.C.:

2 Q. Yes. So based upon what Hydro believes will

3 be the forecast for No. 6 fuel that'll be

4 filed shortly, could Hydro undertake to put on

5 the record what portion Newfoundland Power,

6 Vale, North Atlantic will be paying out of

7 that?

8 MR. FAGAN:

9 A. Actually I should correct something, because

10 if the Holyrood price drops, okay, the price

11 for Corner Brook co-gen would probably drop as

12 well because I believe it's based on No. 6

13 fuel as part of a component of the price. So,

14 it wouldn't necessarily -- the premium

15 wouldn't necessarily increase because of the

16 price decline. I think the Corner Brook co-

17 gen number might decline as well, but the

18 operations -- sorry, the system planning panel

19 would know that better, but we can certainly

20 get you the details. So that .4 may be still

21 reasonable.

22 JOHNSON, Q.C.:

23 Q. Okay. So you can undertake, can you, to

24 provide what portion or how much in dollar

25 terms Newfoundland Power, Vale, North Atlantic

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1 will be paying based both on test year and the
 2 projected fuel price?
 3 MR. FAGAN:
 4 A. Yes.
 5 JOHNSON, Q.C.:
 6 Q. Okay.
 7 MS. GLYNN:
 8 Q. Noted on the record.
 9 JOHNSON, Q.C.:
 10 Q. Okay. And of course, we've seen that Vale's
 11 load is going to be increasing fairly
 12 materially over the next couple of years, so
 13 with that, I guess, we can expect that Vale
 14 will be picking up an increasing amount of
 15 this cost as time goes on?
 16 MR. FAGAN:
 17 A. Well, the test year sets the rate, so from now
 18 until the next rate setting process, unless
 19 there's a deferral account to deal with cost
 20 variances associated with purchases, what's in
 21 the test year would be the rate for purposes
 22 of -- as a proportion of their bill. But
 23 certainly if they're using more, the dollar
 24 effect would be different.
 25 JOHNSON, Q.C.:

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1 Q. Yes. But certainly by the time the next GRA
 2 rolls around and Vale's load is fully up, then
 3 they'll be -- they can expect to be paying
 4 more for this expensive power?
 5 MR. FAGAN:
 6 A. Certainly the dollar effect would be more.
 7 JOHNSON, Q.C.:
 8 Q. Yeah. Now -
 9 MR. FAGAN:
 10 A. The percentage change may not be.
 11 JOHNSON, Q.C.:
 12 Q. Okay. Now as regards to supply costs
 13 mechanisms, we understand, Mr. Fagan, that
 14 following the conclusion of the GRA -- and
 15 this is set out at paragraph 4.24 of the rates
 16 and regulations evidence.
 17 MR. FAGAN:
 18 A. Just a second now. Okay, I'm there. Did you
 19 say page 4.24?
 20 JOHNSON, Q.C.:
 21 Q. No, I'm sorry, paragraph 4.2.4
 22 MS. GRAY:
 23 Q. Page 4.6
 24 MR. FAGAN:
 25 A. Oh, page 4.6, okay. Sorry.

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1 JOHNSON, Q.C.:
 2 Q. It's 4.6, yeah.
 3 MR. FAGAN:
 4 A. Okay.
 5 JOHNSON, Q.C.:
 6 Q. Starting at line 23 indicates and states
 7 actually "following the conclusion of the GRA,
 8 Hydro plans to conduct a review of the
 9 requirements of regulatory mechanisms to deal
 10 with variability in supply costs. Hydro plans
 11 on filing a report to the Board prior to the
 12 end of 2016 on its review of regulatory
 13 mechanisms to provide for supply cost
 14 recovery."
 15 Mr. Fagan, if Hydro is going to be
 16 reviewing requirements for these regulatory
 17 mechanisms in the coming months, will that
 18 review also be considering how these
 19 regulatory mechanisms mesh with Hydro's
 20 currently directed ROE?
 21 MR. FAGAN:
 22 A. That was not the intention. The intention is
 23 to review the cost variances. I expect -- I
 24 wouldn't say ROE, but the -- I mentioned
 25 earlier that 20 basis points, so plus or minus

Page 92

1 20 basis points on return on rate base. 20
 2 basis points is equivalent to, you know,
 3 between three, three and a half million
 4 dollars type thing. So, when looking at
 5 supply cost mechanisms, you want to be looking
 6 at it in light of your range of return. So,
 7 the variability of the costs and the impact it
 8 would have on your rate of return on rate base
 9 for costs that are beyond your control, so I
 10 wouldn't say we're reviewing it in light of
 11 the fact that Government has directed us to
 12 earn an 8.8 ROE, but we'll be considering the
 13 range of return on rate base in looking at
 14 whether it's necessary to have certain supply
 15 cost recovery mechanisms.
 16 JOHNSON, Q.C.:
 17 Q. But like to the extent that some of these
 18 proposed mechanisms transfer risk away from
 19 Hydro and onto the customer, would you not
 20 think it sensible to analyze the
 21 appropriateness of that, given the fact that
 22 Hydro's ROE has dramatically increased from
 23 that which the Board found just and reasonable
 24 when it last determined it?
 25 MR. FAGAN:

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1 A. I think I'd have to push that one onto our
 2 Finance panel. Mr. Scott Pelley would
 3 probably answer that one. But our review
 4 would be focused more on supply cost variances
 5 that would be beyond Hydro's control. So, I
 6 mean, there's been a number of them presented
 7 in this proceeding because a lot of the costs
 8 that have been -- things have changed since
 9 2007. So there's new costs that Hydro is
 10 looking at.

11 For example, in the energy supply cost
 12 deferral for the Island Interconnected system,
 13 now the Holyrood gas turbine is a very
 14 expensive unit to run, so that cost is a new
 15 cost that wasn't there back in 2007 and it's
 16 been required to run fairly frequently. So,
 17 initially when there was a discussion of the
 18 energy supply cost variances, a lot of
 19 discussion around we purchase from Nalcor at
 20 four cents, but if water levels go up or down,
 21 then we've got to replace it with Holyrood
 22 fuel. So you're dealing with the four cents
 23 versus the 15 cents. So which is similar to
 24 the way the rate stabilization plan works.

25 Now it's been commented that -- I think

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1 by Mr. Patrick Bowman, that we should have
 2 just put it in the RSP and we actually -- it
 3 was talked about, but the RSP is so
 4 complicated now, we thought it would be easier
 5 to just set it aside as its own item for now
 6 and when we review the supply cost mechanisms
 7 going forward, we'd look at some aggregation
 8 of where supply cost variances should be. But
 9 so for purposes of transparency in looking at
 10 what's new proposed for the Board, it was
 11 presented as a -- these were all presented as
 12 single items so that the Board could look at
 13 them in that light, but the energy supply cost
 14 variance on the Island Interconnected system,
 15 the combustion turbine cost variances, which
 16 may be, you know, 30 cents a kilowatt hour
 17 when you're running that, it's not so much an
 18 issue of the price variability of No. 2 fuel,
 19 but the volume of running No. 2 fuel -- using
 20 No. 2 fuel that can cause a big impact on
 21 Hydro's financials.

22 So, when it was initially discussed at
 23 Hydro, we were talking about the difference
 24 between the four cents of purchases from
 25 Nalcor versus the 15 cents, and now it's

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1 transitioned into both a combination of
 2 shifting the levels, shifting costs that are
 3 also the Holyrood combustion turbine as well
 4 as the purchases from Nalcor. And it's not
 5 just about risk for Hydro with respect to
 6 purchases from Nalcor. If water levels are up
 7 and we get more purchases from Nalcor, then
 8 there's fuel savings. So similar to the
 9 hydraulic component of the RSP, those savings
 10 would be passed back to customers. So it's
 11 more consistent with a rate stabilization
 12 aspect, although it's been set aside in a
 13 separate account, than just strictly a risk of
 14 Hydro.

15 Now there's one issue with regard to
 16 that's often missed with respect to Hydro is
 17 that load growth on the system for Hydro is
 18 all through the RSP and the mechanics and way
 19 it works, it's all served at Holyrood. So the
 20 cost to Holyrood on our forecast is 15 cents a
 21 kilowatt hour. So, the revenue from the
 22 Industrial Customers for the increased sales,
 23 say in our forecast, is about five cents a
 24 kilowatt hour. So for every kilowatt hour of
 25 growth in load, there's a ten cent loss. So

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1 the rate stabilization, and that's the load
 2 variation component of the rate stabilization,
 3 provides a recovery of that cost.

4 (11:00 a.m.)

5 And that effectively, and with
 6 Newfoundland Power as well, the load growth is
 7 -- all load growth on the system, all those
 8 costs of providing the load growth and all the
 9 revenues that are incoming for energy load
 10 growth, all goes to the RSP. Hydro makes no
 11 earnings on sales growth. It's only if demand
 12 increases and that's sometimes it happens year
 13 over year. Hydro's industrial customers are
 14 typically stable load. They're in a current
 15 change because of the phase-in of the new
 16 customers, but it's typically stable. So you
 17 don't have growth in industrial customer
 18 demand. Newfoundland Power's demand creeps
 19 up. Some years it goes up; some years it
 20 doesn't. So, Hydro is almost effectively
 21 decoupled from getting earnings growth from
 22 sales increases from customers. Puts a big
 23 challenge on Hydro with regard to meeting cost
 24 increases. So you've got to provide your
 25 capital investment.

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1 So that's why when Hydro looks at the
 2 years going forward that you've got big
 3 challenges to meet cost increases, even just
 4 of capital investment, because you don't have
 5 sales growth earnings. I mean, most utilities
 6 -- I know in the US, marginal costs are below
 7 the embedded costs, so if there's sales
 8 growth, they're actually making money on the
 9 sales growth which allows them to stay out --
 10 they could stay out longer.

11 In Newfoundland Power's circumstance,
 12 they've got a deferral account which
 13 effectively protects their earnings on sales
 14 growth that it stabilizes the cost of
 15 purchases from Hydro, so that they manage to
 16 keep their two and a half to three cents a
 17 kilowatt hour as sales increases. But for
 18 Hydro, Hydro doesn't have that. So it's
 19 almost more important for Hydro to get
 20 deferral accounts because it allows us to
 21 recover costs beyond your control but you
 22 still got the challenges of meeting your
 23 normal increases in operating costs.

24 JOHNSON, Q.C.:
 25 Q. We're at past 11.

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1 CHAIRMAN:
 2 Q. I think we need a break, sir.

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

5 MR. FAGAN:
 6 A. Yeah, I agree.

7 CHAIRMAN:
 8 Q. Thank you very much.
 9 (BREAK - 11:03 a.m.)
 10 (RESUME - 11:38 a.m.)

11 CHAIRMAN:
 12 Q. So I understand before we proceed, there is a
 13 revision to an undertaking.

14 MS. PENNELL:
 15 Q. Yes, we had to revise Table 4 in Undertaking
 16 44 which we filed yesterday because the test
 17 year load normalization scenario presented by
 18 the Consumer Advocate. And Undertaking 35 has
 19 also been filed, our winter readiness report
 20 that we filed with the Board last week.

21 CHAIRMAN:
 22 Q. Okay. So Mr. Johnson, I do believe, sir, we
 23 are back to you.

24 JOHNSON, Q.C.:
 25 Q. Thank you, Mr. Chairman. Just a slight

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1 revisitation on O&M for a second or a few
 2 minutes, Mr. Fagan. I guess, you know, the
 3 application that we have in front of us that
 4 we've been dealing with is that Hydro has been
 5 proposing specifically assigned charges as set
 6 out in its rate schedule at page six of 46.
 7 So, I guess, Mr. Fagan, we don't know exactly
 8 now what methodology Hydro is now proposing
 9 and the details of how it will be
 10 implementing, the customer impacts and those
 11 type of things. We had an RFI reply. We had
 12 a bit of evidence from Greneman on the stand,
 13 Mr. Greneman on the stand. Like is Hydro
 14 going to be amending the application to set
 15 out these details, the customer impacts, how
 16 this is supposed to be implemented, you know,
 17 the basis for it?

18 MR. FAGAN:
 19 A. Well, Vale-083 presents the shift, I will call
 20 it, from the change in the approach in the
 21 application to the recommendation of the
 22 methodology of Mr. Dean. So the specifically
 23 assigned charges would be what's reflected in
 24 -- for O&M would be what's reflected in that
 25 particular document. With regard to the

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1 shifting of the cost to common, we'd have to
 2 run that through the cost of service study to
 3 determine the impact on Newfoundland Power and
 4 the Industrial Customers, but effectively
 5 would be a -- I think we could probably
 6 present a table which would illustrate the
 7 effects of that. But it would come out in the
 8 final cost of service study with regard to how
 9 -- the final numbers on it, but we can provide
 10 the impacts on Newfoundland Power and the end
 11 result if we followed that analysis with
 12 regard to specifically assigned charges and
 13 how the other rates would change to reflect
 14 it.

15 JOHNSON, Q.C.:
 16 Q. Okay. And so how are we going to go about
 17 checking the results that come out of Vale-083
 18 to ensure that they're sound and reasonable
 19 for immediate implementation in this GRA?

20 MR. FAGAN:
 21 A. When we file our compliance filing with the
 22 Board, the Board usually has Grant Thornton
 23 review our compliance filing to ensure it
 24 meets the methodology approved by the Board.
 25 So, I mean, that could be part of it.

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1 JOHNSON, Q.C.:

2 Q. I mean, Grant -

3 MR. FAGAN:

4 A. Or we could circulate it to -- and it would be

5 circulated to other parties. We could

6 circulate it to other parties for their

7 feedback on it. When we file a compliance

8 application, other parties have an opportunity

9 to review as well.

10 JOHNSON, Q.C.:

11 Q. So that's the method by which we're going to

12 test the soundness and reasonableness of the

13 numbers that come out of Vale-083?

14 MR. FAGAN:

15 A. No, I don't know if I'd quite say it that way.

16 I think the principle on which you'd determine

17 O&M costs can be established without having

18 the full numbers with regard to the rates for

19 every customer coming out of a compliance

20 filing. So, if the Board believes it's

21 reasonable to restate the original cost in the

22 cost of service for purposes of determining

23 specifically assigned charges based on real

24 dollars and calculate the specifically

25 assigned charges based on real dollars, we'll

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1 make changes to comply with the order of the

2 Board and we'll be presenting results to show

3 that for review by all parties and Grant

4 Thornton upon compliance filing. So I think

5 the Board can make a principle decision

6 without knowing how exactly that \$200,000

7 shift or two or three hundred thousand dollar

8 shift will work out in all the numbers on

9 everybody else's bills.

10 JOHNSON, Q.C.:

11 Q. Okay. And I guess you're saying that the

12 Board will have enough evidence before it in

13 this proceeding to say that like the 150, 000

14 or 149,000 that would get specifically

15 assigned to Vale that that is a reasonable

16 number and that's borne out by, you know, what

17 it should have cost to maintain assets of this

18 type?

19 MR. FAGAN:

20 A. Well, I think it's a principle decision that

21 you're looking at. You're looking at your

22 operating and maintenance costs as a

23 percentage of your investment in capital and

24 you're looking at it on a consistent basis in

25 real dollars. So using that to come up with a

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1 percentage for determining specifically

2 assigned O&M is probably reasonable, at least

3 initially, until we do a full review of the

4 specifically assigned charges methodology in

5 the cost of service review.

6 JOHNSON, Q.C.:

7 Q. Presumably we'll have a much better handle on

8 the reasonableness after the full review that

9 you're speaking of in the cost of service

10 study, right?

11 MR. FAGAN:

12 A. We would certainly review what we came up with

13 to see if there's any weaknesses with it or

14 anything, but based on a principle basis, I

15 wouldn't see that you would conclude

16 different, but I think it would be certainly a

17 more comprehensive review probably of what's

18 done in other jurisdictions would probably be

19 part of the cost of service methodology

20 review.

21 JOHNSON, Q.C.:

22 Q. Yeah.

23 MR. FAGAN:

24 A. So that would be -- that would certainly give

25 more support to a longer term approach.

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1 JOHNSON, Q.C.:

2 Q. Yeah, and that review of which you're

3 speaking, that may well in fact identify a

4 weakness that we're not seeing presently on

5 the record before the Board?

6 MR. FAGAN:

7 A. That's possible.

8 JOHNSON, Q.C.:

9 Q. Yeah, that's right, okay. Now in terms of -

10 MR. FAGAN:

11 A. But should make the -- sorry.

12 JOHNSON, Q.C.:

13 Q. In terms of that indexing idea, will that be

14 an annual exercise? Will the specifically

15 assigned charge be changing from year to year

16 or how do you see that happening?

17 MR. FAGAN:

18 A. Same as it has been in the past. Specifically

19 assigned charge is established in the test

20 year and it would remain the same.

21 JOHNSON, Q.C.:

22 Q. Okay.

23 MR. FAGAN:

24 A. Until the next test year.

25 JOHNSON, Q.C.:

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1 Q. Okay. Now, Mr. Fagan, we've already discussed
 2 in this hearing the fact or the phenomenon, I
 3 suppose, of the fact that the Island
 4 Industrial Customer class load is going to
 5 increase dramatically in 2016 and 2017 over
 6 levels included in the 2015 test year cost of
 7 service study, correct?
 8 MR. FAGAN:
 9 A. That's correct, yes.
 10 JOHNSON, Q.C.:
 11 Q. And you know, and would it be fair -- I've
 12 characterized it as a dramatic increase, and
 13 would that be -- that wouldn't be an
 14 overstatement, would it?
 15 MR. FAGAN:
 16 A. No, it's not. It's a dramatic increase in the
 17 Industrial Customer load.
 18 JOHNSON, Q.C.:
 19 Q. Yeah. Now and of course, that's being driven
 20 by the continued evolution of operations at
 21 Vale as it moves to full production?
 22 MR. FAGAN:
 23 A. Yeah. I just want to clarify, it's a forecast
 24 dramatic increase. So unless the numbers
 25 change, it's certainly a dramatic increase and

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1 as a result of Vale moving to full production.
 2 JOHNSON, Q.C.:
 3 Q. These numbers represent the considered view of
 4 these Industrial Customers as to what their
 5 operations are going to be even in a few
 6 months time, because we're late in -- fairly
 7 late in 2015 now.
 8 MR. FAGAN:
 9 A. Yes, it's just the forecast is based on the
 10 GRA forecast that was filed in November 2014.
 11 So, the numbers are not updated. So I'm not
 12 sure if it's the best estimate of what's there
 13 for 2016 and '17 right now.
 14 JOHNSON, Q.C.:
 15 Q. Okay. But you haven't been advised by these
 16 customers that these forecasts are no longer
 17 what they're standing by for those years?
 18 MR. FAGAN:
 19 A. I've got no better information with respect to
 20 a forecast. I think the experience so far
 21 this year for Vale may be that they're maybe
 22 12 megawatts less than what was anticipated.
 23 So they may be about six months behind of what
 24 we would have planned. But I think when you
 25 determine a test year, you come up with, you

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1 know, your best estimate of what your forecast
 2 is. So I don't know if that necessarily would
 3 change things.
 4 JOHNSON, Q.C.:
 5 Q. Okay. Now Mr. Fagan, I take it that you would
 6 have no trouble agreeing with me that the
 7 loads included in the 2015 test year cost of
 8 service are not reflective of the loads during
 9 the period that rates are expected to be in
 10 effect, right?
 11 MR. FAGAN:
 12 A. Well, if you want to say loads for Industrial
 13 Customers, but loads on the system are not
 14 that different. I mean, you've got -- in
 15 2017, you'd have a higher proportion that's
 16 industrial load.
 17 JOHNSON, Q.C.:
 18 Q. Yeah.
 19 MR. FAGAN:
 20 A. But the total loads are -- from a system
 21 perspective, I don't know if they're -- it's
 22 that big a difference.
 23 JOHNSON, Q.C.:
 24 Q. Okay. But you'll agree with me that the
 25 Industrial Customer loads then in the 2015

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1 test year cost of service are not reflective
 2 of the loads during the period that these
 3 rates are expected to be in effect?
 4 MR. FAGAN:
 5 A. Yes, and that's -- when we were preparing the
 6 application, we recognized the load growth of
 7 the Industrial Customers, so that's why we
 8 reviewed it, and I think we brought up IC-NLH-
 9 140, first revision.
 10 (11:45 a.m.)
 11 JOHNSON, Q.C.:
 12 Q. Yeah, but before -- okay.
 13 MR. FAGAN:
 14 A. Just it's -
 15 JOHNSON, Q.C.:
 16 Q. I'll let you go, but -
 17 MR. FAGAN:
 18 A. No, it's only a short response.
 19 JOHNSON, Q.C.:
 20 Q. Okay.
 21 MR. FAGAN:
 22 A. So with respect to the second paragraph, when
 23 we look -- the concern when you've got a
 24 customer, large customer coming on is you
 25 don't want -- you don't want the rates in the

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1 test year to be somewhat of an anomaly. So
 2 when we looked at the coincident peak load
 3 factor for 2015 test year of approximately 97
 4 percent and said, okay, well that's reflective
 5 of a high load factor Island Industrial
 6 customer, so presenting using Vale and
 7 Praxair's load in 2017 is not distorting the
 8 results. We viewed it from a cost of service
 9 perspective in determining rate design. That
 10 doesn't mean you're recovering all the costs
 11 associated with serving Vale and Praxair as
 12 they go going forward, but the actual unit
 13 rate you're deriving for the customers should
 14 be fairly stable. That was our view.
 15 JOHNSON, Q.C.:
 16 Q. Okay. So in connection with this topic, let
 17 me bring you to Undertaking No. 41, in
 18 particular Table 1 of that. Now this table is
 19 looking at the impact of normalization of the
 20 test year forecast on the Island Industrial
 21 Customer test year demand charge, according to
 22 the heading underneath Table 1 or where it
 23 says Table 1. Now, and we see, Mr. Fagan,
 24 that the Island Industrial Customer allocated
 25 demand costs increase as you go across from

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1 2015 to 2016 to 2017, right, from 8.9 to 10
 2 million to 11.6 million respectively. You see
 3 that?
 4 MR. FAGAN:
 5 A. That's -- if we redid cost of service to
 6 reflect those load forecasts, I think that
 7 just on the demand cost alone because we were
 8 looking at demand revenue requirement and
 9 reallocating it based on the load growth, yes,
 10 the cost would increase, but the unit rate for
 11 the customers wouldn't change a lot.
 12 JOHNSON, Q.C.:
 13 Q. Yes, so what we see there is the IC demand
 14 cost is 8.38, \$8.38 in 2015, 2016 it's 8.33
 15 and 2017 is 8.38, but you average them all out
 16 and you get to 8.38, right?
 17 MR. FAGAN:
 18 A. Yeah.
 19 JOHNSON, Q.C.:
 20 Q. Okay. And by the way, if you -- the numbers,
 21 I think you'll confirm, for Newfoundland
 22 Power's unit demand cost are for 2015, \$10.18?
 23 Is that right, based upon the -
 24 MR. FAGAN:
 25 A. I think that's in a table further on in the

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1 response.
 2 JOHNSON, Q.C.:
 3 Q. Yes. So if you want to go to that table,
 4 Attachment 1.
 5 MR. FAGAN:
 6 A. Sure.
 7 JOHNSON, Q.C.:
 8 Q. Line 14.
 9 MR. FAGAN:
 10 A. Yes, you're correct.
 11 JOHNSON, Q.C.:
 12 Q. Right. So, for Newfoundland Power, it would
 13 be 10.18 in the test year. In 2016, it drops
 14 to 9.96 and then drops in 2017 to 9.72 and
 15 averages out to 9.95 as a three-year average.
 16 MR. FAGAN:
 17 A. Sure.
 18 JOHNSON, Q.C.:
 19 Q. Okay. Now, and I guess we can observe there
 20 that the ICs have unit demand costs that are
 21 materially lower than what Newfoundland Power
 22 would have in those years. Would that be
 23 correct?
 24 MR. FAGAN:
 25 A. Yes, that would be really consistent with past

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1 practice, that the Industrial Customers have
 2 higher load factor and a lower coincidence
 3 with system peak. So their unit demand cost
 4 is generally lower than Newfoundland Power's
 5 unit demand cost.
 6 JOHNSON, Q.C.:
 7 Q. Yes, and while the Island Industrial Customer
 8 load is growing in 2016 and again in 2017, you
 9 would in fact expect to see Newfoundland
 10 Power's unit demand costs edging downward.
 11 Would that be the expectation?
 12 MR. FAGAN:
 13 A. Yes, in this particular scenario where we're
 14 keeping the total demand cost the same and
 15 divide by the increased loads for both
 16 parties, yes, that would be the normal result
 17 because the Industrial's load is growing
 18 faster than Newfoundland Power's from a
 19 percentage basis.
 20 JOHNSON, Q.C.:
 21 Q. Yeah, so unlike the scenario that was put
 22 forward in Undertaking No. 44 yesterday, we're
 23 not talking about a normalized unit cost for
 24 the Industrial Customers of anywhere near
 25 \$10.95 a kilowatt?

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1 MR. FAGAN:
 2 A. No, that's correct.
 3 JOHNSON, Q.C.:
 4 Q. That's correct.
 5 MR. FAGAN:
 6 A. Now the only thing is there's a -- one
 7 difference between Newfoundland Power and the
 8 Island Industrial Customers is that the unit
 9 cost becomes a demand charge, okay, and for
 10 Newfoundland Power, their demand charge,
 11 current one is four dollars a kilowatt, and I
 12 think in the settlement agreement we've put
 13 forward to the Board, it's \$4.75 a kilowatt.
 14 So, from a demand charge perspective, the
 15 Newfoundland Power demand charge is not
 16 derived strictly from the unit cost variance.
 17 So, from a revenue forecast perspective, but
 18 it wouldn't actually change the rate design
 19 for Newfoundland Power.
 20 JOHNSON, Q.C.:
 21 Q. It wouldn't change the rate design, no, okay.
 22 MR. FAGAN:
 23 A. Right.
 24 JOHNSON, Q.C.:
 25 Q. But these would represent the actual unit

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1 demand cost, yeah, okay.
 2 MR. FAGAN:
 3 A. Based on the assumptions we've made with
 4 regard to maintaining the demand cost the same
 5 for each year, yes.
 6 JOHNSON, Q.C.:
 7 Q. Okay. Now if you look under the table there,
 8 there's text on Table 1 of Undertaking No. 41
 9 that says "Table 1 shows that while the
 10 allocated demand revenue requirement to IIC
 11 increases materially using the 2016 and 2017
 12 forecast reflecting the higher demand
 13 requirements for the IIC, there is minimal
 14 change in the unit demand cost as a result of
 15 the higher demand billing units used to
 16 compute the unit cost." But just to focus
 17 here on the first part of that statement, I
 18 take it that there's no disagreement that what
 19 we're talking about is a material difference
 20 in relation to the allocated demand revenue
 21 requirement that we're seeing between test
 22 year 2015 and taking an average of 2015 to
 23 2017?
 24 MR. FAGAN:
 25 A. That's right.

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1 JOHNSON, Q.C.:
 2 Q. Hydro refers to that 1.3 million dollar
 3 difference as being quite material?
 4 MR. FAGAN:
 5 A. Yes, it is. The only thing is though it just
 6 also, in my view, would show that the demand
 7 charge proposed would reasonably recover the
 8 costs over those years, so as Vale's load
 9 ramped up, the charge they would be paying in
 10 those years would reasonably recover the
 11 demand costs effectively assigned to them.
 12 JOHNSON, Q.C.:
 13 Q. But by the same -
 14 MR. FAGAN:
 15 A. One thing, just for clarity, the demand costs
 16 don't -- if load grows on the system, goes up
 17 and down throughout the year and year over
 18 year between test years, demand costs don't
 19 necessarily change because of a single shift
 20 of one kilowatt of demand. You've got your
 21 fixed capacity on your system. The energy is
 22 if the load grows from the new customers
 23 coming on, it's driving variable costs on the
 24 system. So, the big issue with regard to the
 25 -- to me, from the Industrial Customers load

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1 is make sure that we're recovering the
 2 variable costs associated with the load growth
 3 and eventually when I go to Undertaking 44 and
 4 I can demonstrate how that would work, but the
 5 -- so our view is that the unit cost of energy
 6 that we proposed, in combination with the
 7 operation of the RSP, will recover the full
 8 energy costs from the load growth and within
 9 the -- because the load variation component
 10 that's proposed to be done on an energy
 11 allocation basis, the sharing of the
 12 additional load cost because of the ramp up of
 13 Vale and Praxair is done in the same way as it
 14 would be in the cost of service study because
 15 it would be based on the percentage of energy
 16 for the Industrial Customers versus the
 17 percentage of energy for Newfoundland Power.
 18 So, all the real system costs, additional
 19 system costs because of Vale and Praxair
 20 coming on the system are being shared
 21 consistent with the cost of service approach
 22 because they're really driving the energy
 23 costs.
 24 JOHNSON, Q.C.:
 25 Q. But the load variation component takes over

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1 after the test year anyway, right, I mean, in
 2 terms of we're putting certain values and
 3 assumptions in the test year and after that,
 4 you know, the RSP does its work, right? I
 5 mean, that's just normal.
 6 MR. FAGAN:
 7 A. That's right, but the key to the test year is
 8 -- and I think it was probably demonstrated in
 9 the original filing of the 2013 test year,
 10 that the demand charge for -- proposed demand
 11 charge for Industrial Customers I believe may
 12 have been slightly higher than the demand
 13 charge proposed for Newfoundland Power or
 14 certainly it was in the ballpark. I don't
 15 remember the exact number, but it may have
 16 been a few cents apart. And that wouldn't
 17 have been normal, based on the circumstances
 18 or the demands, forecast demands of Industrial
 19 Customers and their coincidence with system
 20 peaks.
 21 As I mentioned in my opening statement,
 22 every test year I've ever seen, the demand
 23 charges for -- or unit demand costs for Island
 24 Industrial Customers is always slightly below
 25 the unit demand cost for Newfoundland Power

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1 because Newfoundland Power has a lower load
 2 factor, they're on peak more. So when you
 3 look at that 2013 forecast, test year forecast
 4 which was provided in IC-140 original, it
 5 would set off alarm bells for me. And so
 6 that's why when the Industrial Customers
 7 questioned in IC-140 about doing a revision to
 8 reflect a normalized demand within the year,
 9 making an adjustment for assuming Vale and
 10 Praxair would be a high load factor in that
 11 year, even though it would have been a very
 12 small customer, it would have been estimated
 13 to be four megawatts, took the distortion away
 14 from computing the unit demand cost for
 15 purposes of setting a rate and so when we
 16 looked at Vale and Praxair and their load
 17 going forward, the key is when you're putting
 18 them in a test year is that you don't distort
 19 the unit cost.
 20 As their load grows, they're going to pay
 21 for their cost because as their load grows,
 22 they're going to pay the unit demand costs and
 23 they're going to pay their energy costs
 24 through either both the firm energy charge
 25 that's approved and the RSP, and that RSP

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1 sharing between Newfoundland Power and
 2 Industrial Customers is consistent with the
 3 sharing it would incur in the cost of service
 4 study anyway, so I think it -- I think that
 5 what's proposed with regard to the 8.38 demand
 6 charge is a reasonable one going forward that
 7 they're paying -- Vale and Praxair are paying
 8 the same demand charge as other customers
 9 would almost without Vale and Praxair being
 10 included because they're not distorting it
 11 because they're a similar load factor than the
 12 others.
 13 So, I think the test year works from that
 14 perspective, that it doesn't result in a
 15 distorted demand charge and the mechanism with
 16 regard to the RSP load variation doesn't
 17 result in any distortion to the recovery of
 18 incremental energy costs because of load
 19 growth on the system.
 20 JOHNSON, Q.C.:
 21 Q. Well, like if you look at Table 1, it's still
 22 there in front of us, and we picture the 2015
 23 test year column that Newfoundland Power's
 24 unit demand cost is \$10.18 and then it would
 25 fall off to 9.96, 9.72 and average 9.95,

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1 Newfoundland Power is being put in a demand
 2 cost which is 10.18 and there's no decreasing
 3 along the way. I guess my difficulty is, you
 4 know, what's happening to the spread between
 5 the 8.9 million and the 10.2 million. I mean,
 6 someone's picking that up. It's Newfoundland
 7 Power is picking it up, right?
 8 MR. FAGAN:
 9 A. No, I wouldn't agree with that. Newfoundland
 10 Power's demand charge will be -- assuming the
 11 Board would approve it, \$4.75 per kilowatt.
 12 So Newfoundland Power will be paying that
 13 demand charge going forward. The energy costs
 14 which would be flowing through through the
 15 RSP, Newfoundland Power will be paying
 16 approximately 90 percent of the Industrial
 17 Customer energy costs. So, that's what would
 18 happen within the cost of service. The only,
 19 okay, intricacy with respect to it, the
 20 difference, is that Newfoundland Power's tail
 21 block energy rate is set at the test year
 22 price of fuel, at least historically, and I
 23 think we've got a settlement agreement to deal
 24 with that on a go-forward basis. So their
 25 load growth going forward, which is, you know,

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1 fairly small each year, they'll pay that
 2 portion of it. But they're sharing in the
 3 portion of the load growth for Industrial
 4 Customers through the RSP. So their demand --
 5 Newfoundland Power's demand charge is not
 6 derived from -- on a unit cost basis the same
 7 way the Industrial customers is. So I don't
 8 think the comparison of the cost, the unit
 9 cost for Newfoundland Power is necessarily has
 10 rate implications.

11 JOHNSON, Q.C.:

12 Q. It mightn't have rate implications, but it has
 13 cost implication to Newfoundland Power,
 14 doesn't it?

15 MR. FAGAN:

16 A. When you say "cost implications", I think the
 17 revenue requirement allocated to Newfoundland
 18 Power and industrial customers within the test
 19 year is reasonable based on the forecast
 20 because we've got the test year cost there for
 21 both industrial and Newfoundland Power, and
 22 we've complied with the cost of service
 23 methodology approved by the Board. So where
 24 we're at now is looking at more of a rate
 25 design issue for industrial customers, and you

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1 don't want to distort the rate design for the
 2 industrial customers because there's a ramp up
 3 of load going to happen in the next couple of
 4 years. What happens actually is the
 5 additional demand charges for industrial
 6 customers, and in this particular case it
 7 shows an increase in demand charges of about
 8 1.1 million dollars between '15 and '16, and
 9 an additional 1.6 million dollars between '16
 10 and '17. That's additional revenues to Hydro
 11 to offset other cost increases, because I
 12 mentioned demand costs don't necessarily go up
 13 and down because of load changes, so this
 14 additional revenue to Hydro to offset other
 15 cost increases, capital investment,
 16 inflationary increases, because of demand
 17 growth. That's not usually the norm with
 18 regard to industrial customers because
 19 normally their load is stable, so they've set
 20 their firm demands, but because it's in a low
 21 growth position for Vale, there's additional
 22 revenues coming into Hydro because of that low
 23 growth to offset other costs in those years.
 24 It's not necessarily distorting what
 25 Newfoundland Power is required to pay in the

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1 test year.

2 JOHNSON, Q.C.:

3 Q. Well, if I look to that statement below Table
 4 1 that says that the allocated demand revenue
 5 requirement to the island industrial customer
 6 increases materially using the 2016 and 2017
 7 forecast, and given that, you know, as we've
 8 agreed, the cost of service analysis should
 9 reflect fair and reasonable estimation of the
 10 cost responsibility between customer classes
 11 for the period in which the study is being
 12 applied, I would ask are you saying that Hydro
 13 doesn't see any difficulty with this and is
 14 not proposing any adjustment for the cost of
 15 service study to -

16 MR. FAGAN:

17 A. I think your interpretation of the change in
 18 costs may be leading to a conclusion that I
 19 don't agree with. Column B is basically
 20 saying if you had the same demand cost on the
 21 system in 2016 as you got for 2015, you'd come
 22 up with a different demand revenue requirement
 23 for industrial customers, but you can't really
 24 bring that cost back to the 2015 and derive a
 25 rate, and I think that's what's shown in

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1 Undertaking 44. If you try and bring the cost
 2 back, you end up with too high a rate. So as
 3 long as - for instance, let's say Vale and
 4 Praxair weren't going to come on until 2016,
 5 you could come up with a reasonable rate for
 6 the industrial customers without Vale and
 7 Praxair being reflected in the test year as
 8 long as - and it would probably be reasonable
 9 for Vale and Praxair as well, as long as their
 10 load factor is comparable to a typical
 11 industrial customer. What happens is that
 12 when they come on, they pay the average cost
 13 that was reflected in the test year, and it
 14 recovers the cost from them at that time. It
 15 would be more of a windfall for Hydro to
 16 recover some other costs because Hydro would
 17 have demand charges - additional demand
 18 charges that wouldn't be reflected in the test
 19 year, so that would provide more security for
 20 Hydro in '16, but it doesn't - as long as the
 21 customers are similar load factor and similar
 22 coincident to peak as the other industrials,
 23 it doesn't result in the demand charge being
 24 incorrect. So if you try and bring it back,
 25 you'll distort the demand charges and

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1 potentially the energy charges as well. As
 2 long as the unit cost is comparable year over
 3 year, just in this particular circumstances
 4 shows that when Vale and Praxair are on fully,
 5 the demand charge wouldn't change very much,
 6 so they're paying their way. It works for
 7 both the industrial customers, for Vale, and
 8 Praxair, being partly phased in versus being
 9 fully phased in, the rate is still reasonable.
 10 That's my interpretation of it.
 11 JOHNSON, Q.C.:
 12 Q. But if we tried to incorporate or reflect in
 13 the 2015 test year the fact that they will be
 14 ramping up - if we tried to reflect that,
 15 wouldn't that be of benefit to Newfoundland
 16 Power customers?
 17 MR. FAGAN:
 18 A. I think the rate stabilization plan works to
 19 protect customers in that manner.
 20 JOHNSON, Q.C.:
 21 Q. But how about on demand?
 22 MR. FAGAN:
 23 A. To me, as long as the load factors are
 24 comparable and as long as they're billed in a
 25 unit cost basis, which Newfoundland Power

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1 isn't, and industrial customers are, you come
 2 up with a similar unit cost rate so it doesn't
 3 disadvantage either Newfoundland Power's
 4 customers because of them not being fully
 5 ramped up in the 2015 test year. You can't
 6 bring back their demands now and bring their
 7 costs in, in advance of having the loads to
 8 recover the cost, you'll distort the rates.
 9 JOHNSON, Q.C.:
 10 Q. Well, how then do we - this principle that
 11 everybody seems to agree upon about the cost
 12 of the service analysis reflecting fair and
 13 reasonable estimation of the cost
 14 responsibility between classes for the period
 15 in which the study is being applied -
 16 MR. FAGAN:
 17 A. That's achieved.
 18 JOHNSON, Q.C.:
 19 Q. You feel that that's achieved by not making
 20 any adjustment at all to the fact that there's
 21 going to be a dramatic increase in '16 and '17
 22 to industrial customer load?
 23 MR. FAGAN:
 24 A. As long as the rates that are approved are
 25 reasonable for Vale and Praxair, consistent

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1 with typical industrial customer, there's no -
 2 and within the rate stabilization plan
 3 mechanism to recover the incremental cost
 4 which shares that, I'll call it, on the cost
 5 of service basis of fuel, so sharing it based
 6 on energy ratios consistent with the cost of
 7 service, then I think it works well with
 8 respect to - this is one of the important
 9 aspects. The load variation component of the
 10 RSP is important especially when you've got a
 11 ramp up of a new industrial customer coming
 12 on, so you don't end up with an unfair rate
 13 for customers or potentially lack of cost
 14 recovery for Hydro.
 15 JOHNSON, Q.C.:
 16 Q. If you go to Table 2, again if we took an
 17 average of the industrial customer energy
 18 requirement over '15 and '16, and '17, you're
 19 talking about a very material sum of money in
 20 the difference, aren't you, from 32 million to
 21 38 million?
 22 MR. FAGAN:
 23 A. Table 2 doesn't show the - I mentioned that
 24 capacity is more of a fixed cost between test
 25 years unless there's all of a sudden a big

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1 ramp up of additional capacity on the system,
 2 but energy is the immediate impact of a change
 3 in cost. If we want to discuss the impact, I
 4 don't think this necessarily demonstrates it.
 5 I'd rather if we could go to Undertaking 44
 6 for a minute, and go to Table 4. There's a
 7 lot of numbers in this table, so I'll try and
 8 go slow. If we look at line 4, we see the
 9 industrial load going from 621 gigawatt hours
 10 to 873. So you've got 250 gigawatt hours
 11 increase. That's at Holyrood fuel which is
 12 about 15 cents a kilowatt hour. So that's
 13 around 37 million dollars of additional fuel
 14 cost incurred to provide that load. Now if we
 15 look at line 1, which is the proposed unit
 16 rate of 5.151 cents per kilowatt hour, and if
 17 we compare the 2017 revenues on the unit rate
 18 to the 2015 revenues on the unit rate, we've
 19 got 45 million versus 32. So we've got an
 20 additional 13 million recovered from the
 21 industrial customers on 5.1 cents per kilowatt
 22 hour rate. Now so that leaves us with about
 23 24/25 million dollars extra cost. If we move
 24 down to the RSP impact, footnote 1, and the
 25 first shaded number in the last column, the

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1 25.7 million dollars, that's the additional
 2 fuel cost from industrial customers load
 3 that's not recovered from the firm energy
 4 charge. So in cost of service study, we got
 5 energy costs and fuel costs that we share
 6 based on their proportion of energy. If we
 7 look at - we've got an IC allocation and an NP
 8 allocation down a few rows. There's a 3
 9 million dollar and a 27 million dollars to
 10 Newfoundland Power. So there was a 25. 8
 11 million dollars load variation for industrial
 12 customers. Newfoundland Power's load also
 13 grew relative to the test year, so we've got
 14 about 5 million dollars there, 4.997 million.
 15 So the combined effect of the load growth
 16 beyond the test year is 30.7 million. The
 17 industrial customers would pay 10 percent of
 18 that, and Newfoundland Power's customers would
 19 pay 90 percent of that. Now this is based on
 20 Hydro's proposed rates in the amended
 21 application. If those fuel costs were in the
 22 2015 test year conceptually, and Vale and
 23 Praxair were on the system fully implemented,
 24 then industrial customers would pay
 25 approximately 10 percent and Newfoundland

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1 Power's customers would pay approximately 90
 2 percent. So you still got this sharing going
 3 on - well, actually this 10 and 90 will change
 4 over time because as the load ramps up in the
 5 rate stabilization plan, the percentage of the
 6 load as a percentage of the last most recent
 7 12 months, so the 10 percent maybe in the 2015
 8 test year, it may be 11 percent in 2017. So
 9 you'd end up with the industrial customers
 10 still paying their share of the additional
 11 fuel cost that's incurred as a result of the
 12 load ramp up. So from a variable cost
 13 perspective, of all the real additional cost
 14 on the system because of the industrial
 15 customers coming on, the proposed rate in
 16 combination with the RSP operation does
 17 provide a fair recovery of those costs of the
 18 additional industrial load.
 19 (12:15 p.m.)
 20 JOHNSON, Q.C.:
 21 Q. Mr. Fagan, what would it require for you to
 22 believe that there would have to be some
 23 adjustment made to the 2015 test year? Like,
 24 obviously you're indicating that the 20
 25 percent increase in island industrial customer

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1 load in 2016 over 2015 levels is not
 2 sufficient, the 40 percent reflected in 2017
 3 over 2015 levels does not cause any need for
 4 adjustment, so what sort of magnitude of
 5 change would we need to see for Hydro to make
 6 or propose an adjustment to the 2015 test
 7 year?
 8 MR. FAGAN:
 9 A. There would have to be a change in loads and a
 10 change in demands, so that the load factor
 11 reflected in the test year is not really
 12 reflective of the long term load factor for
 13 the industrial customers, and if there was a
 14 big shift in load factor, then the demand
 15 charge and coincident factor kind of peak, the
 16 demand charge coming out of the test year may
 17 be flawed, but we haven't - looking at that
 18 Undertaking 41, we see that the costs are
 19 fairly stable. I mean, quite often in
 20 Newfoundland Power's case, when I was there
 21 before, you've got new customers coming on the
 22 system all the time, and sometimes fairly
 23 large. As long as a new customer coming on in
 24 the class doesn't change the load shape and
 25 the unit cost, the rates can still be

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1 reasonable even though there's a large
 2 increase in the load. So it's more about
 3 making sure the rate is reasonable and the
 4 load factor for the additional customers is
 5 still close to the load factor and the
 6 coincident for the other customers that are in
 7 the group, so you don't end up with a
 8 distortion in the rate to the customers.
 9 That's what I'd look at. That's why in that
 10 updated response to IC-NLH-40, we looked at
 11 the coincident peak load factor for the 2015
 12 test year, which indicated 97 percent load
 13 factor, and said, all right, so 2015 shouldn't
 14 be a distortion because we looked at that load
 15 factor versus the forecast years and said,
 16 that should be okay, we're going to come up
 17 with a reasonable unit rate that'll apply to
 18 all the customers over the period of 2015 to
 19 2017.
 20 JOHNSON, Q.C.:
 21 Q. And you adjusted the load factor to look like
 22 a year that might happen some time in the
 23 future?
 24 MR. FAGAN:
 25 A. Well, that was in the original IC-140. I was

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1 thinking about in the IC-140 revision. The
 2 original IC-140 was an example of when you'd
 3 want to make an adjustment because the average
 4 cost for industrials actually exceeded the
 5 average demand unit cost for Newfoundland
 6 Power, which wouldn't be expected for a high
 7 load factor group with a lower coincident type
 8 of peak. So that set off alarm bells for me
 9 with regard to the 2013 test year, that it
 10 would have been appropriate to make some
 11 adjustments, but for the 2015 test year, the
 12 relative difference in the unit demand cost
 13 for industrial customers and the unit demand
 14 cost for Newfoundland Power appeared to be
 15 reasonable.

16 JOHNSON, Q.C.:
 17 Q. But Undertaking 41 did purport to be a
 18 normalization exercise, didn't it?

19 MR. FAGAN:
 20 A. It was a normalization exercise with respect
 21 to estimating what the unit demand costs would
 22 be if we looked forward beyond 2016, and
 23 effectively we're redoing 2016, but this would
 24 have assumed in 2016 that you would have had
 25 those units to bill the customers in 2016. So

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1 when you're coming up with the 833 in 2016,
 2 you're matching the revenue requirement with
 3 the units that the customer is anticipating to
 4 use in 2016. The difficulty comes if you
 5 start trying to bring those units back into a
 6 2015 test year, that you distort the
 7 percentage allocations, and you come up with
 8 rates that don't really reflect the cost of
 9 serving.

10 JOHNSON, Q.C.:
 11 Q. Thank you, Mr. Fagan. Those are the
 12 questions.

13 CHAIRMAN:
 14 Q. I think Mr. Coxworthy, over to you.

15 MR. COXWORTHY:
 16 Q. Yes, thank you, Mr. Chair. There was an
 17 information document that I was seeking to
 18 have circulated.

19 MS. GLYNN:
 20 Q. We'll enter that as Information 11.

21 MR. KEVIN FAGAN - CROSS-EXAMINATION BY MR. PAUL
 22 COXWORTHY:
 23 MR. COXWORTHY:
 24 Q. Thank you. Mr. Fagan, you have Information 11
 25 there in front of you?

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1 MR. FAGAN:
 2 A. Yeah, I'm good.

3 MR. COXWORTHY:
 4 Q. I just want to make some comments, in fact,
 5 corrections or at least clarifications. The
 6 table is referred to as being 2013 from IC-
 7 NLH-002 revision 1, but in fact the
 8 information in the table comes from the
 9 unrevised version, which is over 800 pages of
 10 cost of service studies going all the way back
 11 to 2007.

12 MR. FAGAN:
 13 A. I appreciate the single page.

14 MR. COXWORTHY:
 15 Q. Well, I thought perhaps everyone would rather
 16 than going through 800 pages of cost of
 17 service studies. I don't know whether you had
 18 the opportunity to review these figures or
 19 whether you're familiar enough with these
 20 figures to be able to confirm that they are an
 21 accurate representation of the relationships
 22 between demand and between IC, and
 23 Newfoundland Power, in those respective years
 24 and also in relation to energy?

25 MR. FAGAN:

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1 A. I've reviewed them from a high level and some
 2 look like anomalies, so I did a bit of
 3 checking on them. To be clear, we've got a
 4 mixture here of test year cost of service
 5 studies and actual cost of service studies,
 6 and what happens with actual cost of service
 7 studies is in some cases it may be really a
 8 cold year, and Newfoundland Power may be
 9 driving the peak, and so you'd end up with the
 10 average cost and the demand basis for
 11 Newfoundland Power may be higher in that year.
 12 There's another year here in 2010, you'll see
 13 the average demand cost for industrial
 14 customers is \$2.78 per kilowatt. I believe in
 15 that year there may have been a fire at North
 16 Atlantic Petroleum, so they weren't in service
 17 at the time of peak, or they were maybe only
 18 partially in service, so the demand cost
 19 allocated to them was materially lower
 20 relative to their billing units. So when
 21 you're dealing with actual cost of service
 22 study year over year, they're not used for
 23 rate setting so you do have a fair bit of
 24 variability in the numbers, but with that
 25 caveat, yeah, the numbers, they don't really

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1 look unreasonable from what I would expect.
 2 MR. COXWORTHY:
 3 Q. And I haven't gone back and reviewed all those
 4 cost of service studies either. Mr. Patrick
 5 Bowman has done that, but I have looked at the
 6 2013, and for the interest of the record, this
 7 information can be derived from Schedule 1.3,
 8 page 1 of the 2013 actual cost of service
 9 study, and I presume a similar schedule would
 10 apply for the other cost of service studies as
 11 well.
 12 MR. FAGAN:
 13 A. Yes, I expect so.
 14 MR. COXWORTHY:
 15 Q. So in terms of the relationship, do they
 16 consistently show with respect to demand that
 17 IC demand is - whether it's test year or
 18 actual cost of service study, that industrial
 19 customer demand rates are consistently lower
 20 than Newfoundland Power's, somewhat lower?
 21 MR. FAGAN:
 22 A. Yes, that's a fair comment.
 23 MR. COXWORTHY:
 24 Q. And you've spoken to the reason for this, and
 25 you've spoken to the fact that the industrial

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1 customer class, as a class, has presumably
 2 over this whole period shown factors of being
 3 at a high load factor, but a relatively lower
 4 coincident peak, as compared to Newfoundland
 5 Power which has lower load factor, but higher
 6 peak?
 7 MR. FAGAN:
 8 A. Yes, from the Board's perspective, higher load
 9 factor - customer with the higher load factor,
 10 we ended up with less demand cost. We
 11 classify a lot of our costs on load factor,
 12 and so the higher load factor customers,
 13 they've got less demand costs allocated to
 14 them than lower load factor customers, and so
 15 Newfoundland Power is a lower load factor
 16 customer, they're more coincident with peak
 17 because electric heat in our system often
 18 drives the system peak, so the allocated
 19 demand cost on a unit basis would normally be
 20 higher for Newfoundland Power than it would be
 21 for the industrial customers.
 22 MR. COXWORTHY:
 23 Q. This, of course, only takes us to 2013,
 24 Information 11. When one looks at 2014, 2015
 25 forecast, and we've got some actual numbers,

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1 2016, 2017, will industrial customer class
 2 continue to be high load, relatively lower
 3 coincident peak, will the continue that
 4 pattern?
 5 MR. FAGAN:
 6 A. Based on the forecast, yes.
 7 MR. COXWORTHY:
 8 Q. Based on the forecast?
 9 MR. FAGAN:
 10 A. Based on the forecast, there will be no
 11 change.
 12 MR. COXWORTHY:
 13 Q. So even with the ramp up with Vale, that
 14 doesn't change that aspect of the demand
 15 relationship as between Newfoundland Power -
 16 MR. FAGAN:
 17 A. I spoke to our forecaster about the
 18 coincident, and Newfoundland Power's peak is
 19 assumed to be on average 99 percent coincident
 20 with system peak. The industrial customers on
 21 average is more around 88 percent. So we have
 22 no reason to think that will change.
 23 MR. COXWORTHY:
 24 Q. Looking at Information 11, and if we could
 25 move on to the energy comparison, the energy

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1 rate for the industrial customers, whether
 2 it's test years cost of service, actual cost
 3 of service, and those for Newfoundland Power
 4 for energy, they stay relatively close to each
 5 other over time?
 6 MR. FAGAN:
 7 A. That's correct.
 8 MR. COXWORTHY:
 9 Q. And I think you've already testified that
 10 that's as you would expect?
 11 MR. FAGAN:
 12 A. Yes, you wouldn't anticipate any reason that
 13 the energy costs would be different,
 14 materially different.
 15 MR. COXWORTHY:
 16 Q. Can you explain to a layperson like me why
 17 that's different from demand, why doesn't the
 18 unit cost for energy for industrial customers,
 19 why is that not different than for
 20 Newfoundland Power?
 21 MR. FAGAN:
 22 A. Well, a lot of the energy cost are fuel,
 23 right, so you're just taking it, dividing it
 24 by the amount of energy, so it's no different
 25 on a unit basis for industrial customers

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1 versus Newfoundland Power’s customers, so the
 2 unit cost of fuel at Holyrood, say, 15 cents a
 3 kilowatt hour, well, it’s 15 cents a kilowatt
 4 hour to provide the energy to an industrial
 5 customer, it’s 15 cents a kilowatt hour to
 6 provide it to Newfoundland Power’s customer.
 7 MR. COXWORTHY:
 8 Q. So there’s no reason for it to cost any
 9 different depending on what customer we’re
 10 talking about.
 11 MR. FAGAN:
 12 A. Not material, no.
 13 MR. COXWORTHY:
 14 Q. What class of customer?
 15 MR. FAGAN:
 16 A. You certainly wouldn’t anticipate any material
 17 difference.
 18 MR. COXWORTHY:
 19 Q. And with that I’d like you to turn to
 20 undertaking 44. And if we can turn to the
 21 second page of undertaking 44 which comments
 22 on Table 2, I believe, which appears on the
 23 first page. If we look at the first paragraph
 24 of the second page. We might need to go back
 25 to Table 2, as we discuss this paragraph. But

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1 the first paragraph on the first page of
 2 undertaking 44 says that from an energy cost
 3 perspective, the average energy unit cost is
 4 generally approximately the same for
 5 Newfoundland Power and Industrial Customers.
 6 That’s what we were just talking about, is
 7 shown at Information 11.
 8 MR. FAGAN:
 9 A. That’s correct.
 10 MR. COXWORTHY:
 11 Q. You then comment on Table 2, your Table 2 or
 12 the Table 2 that was produced as part of this
 13 undertaking response, shows that under the
 14 normalized test year the proposed energy
 15 charge would be approximately 30 percent
 16 higher for the industrial customers. Is that
 17 a reasonable result?
 18 MR. FAGAN:
 19 A. No.
 20 MR. COXWORTHY:
 21 Q. And why not?
 22 MR. FAGAN:
 23 A. Well it doesn’t reflect the cost of serving
 24 them in the test year. The cost of serving
 25 Newfoundland Power in the test year on an

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1 energy basis and industrial customers on an
 2 energy basis is approximately the same. So if
 3 one saw that coming out of a cost of service,
 4 you’d wonder what you’ve done wrong, so we’re
 5 putting costs to be allocated to industrial
 6 customers in the test year that is not
 7 reflective of their load in the test year, and
 8 that’s driving it up.
 9 MR. COXWORTHY:
 10 Q. And won’t that also then be true for 2016 and
 11 2017?
 12 MR. FAGAN:
 13 A. If you brought those numbers back to the 2015
 14 test year, you’d have the same effect. So if
 15 you brought back--if you normalize,
 16 undertaking 44 is normalized based on a 2017
 17 forecast. If you brought 2016 forecast back,
 18 you’d have the same effect. The magnitude may
 19 be somewhat different, but you’d have the same
 20 effect.
 21 MR. COXWORTHY:
 22 Q. The energy cost would be higher for the
 23 industrial customers and would that be a
 24 reasonable result, though, for 2016 or 2017?
 25 MR. FAGAN:

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1 A. Well it wouldn’t be reasonable of the energy
 2 costs incurred to serve them.
 3 MR. COXWORTHY:
 4 Q. To serve the industrial customers, so it’s
 5 just that it’s--it’s just not that it’s not
 6 reasonable for 2015, it wouldn’t be reasonable
 7 for 2016 or 2017 either when you look at the
 8 cost of serving the industrial customer class?
 9 MR. FAGAN:
 10 A. Well, in setting a 2015 test year for rate
 11 setting, you need to reflect the energy cost
 12 incurred in 2015 and the only question with
 13 respect to normalization is whether that was
 14 still reasonable for ’16 and ’17 and I think
 15 it is.
 16 MR. COXWORTHY:
 17 Q. I just want to talk a little bit about the
 18 word "normalization" because I think, again,
 19 as a layperson, I hear that word and I think
 20 that sounds good, you know, anytime you
 21 normalize something, you know, how could that
 22 not be a good thing? Does every normalization
 23 exercise turn out a reasonable result in terms
 24 of setting rates or rate design?
 25 MR. FAGAN:

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1 A. Well I don't know, you need to look and see
 2 why you're doing normalization and if it's
 3 required first before you then could judge the
 4 result of the normalization. So we looked
 5 before we come up with the test year and
 6 assessed the load factor of the industrial
 7 customers, including Praxair and Vale in the
 8 2015 test year, based on their load and the
 9 result was we didn't think a normalization was
 10 required. I think we would probably agree
 11 that there would have been a normalization
 12 required to the original 2013 test year
 13 because it was an anomaly with respect to the
 14 load factor of Vale and Praxair for that
 15 purpose, because it was one of those things,
 16 you can look at the end result and it will
 17 send you back to look and see what's going on.
 18 But if there's no normalization required, then
 19 I wouldn't go there. If there was one
 20 required, then you assess the result, whether
 21 normalization makes sense based on the result,
 22 but the sensitivity we've done on a potential
 23 normalization in this particular circumstance
 24 would produce results that don't really
 25 reflect the recovery of the fair cost to serve

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1 the industrial customer.
 2 MR. COXWORTHY:
 3 Q. So is undertaking 44 representing
 4 normalization exercise that's not necessary?
 5 MR. FAGAN:
 6 A. Well it's actually helpful because it shows
 7 that if you actually try to do a normalization
 8 and reflect future cost patterns in the 2015
 9 test year, you wouldn't get reasonable
 10 results.
 11 MR. COXWORTHY:
 12 Q. Thank you. I'd like to move on to another
 13 area, at least for now, in relation to, I
 14 believe it's Consent No. 3, the August 2015
 15 RSP Report. and I'm going to get into this
 16 while Mr. Patrick Bowman is still here with us
 17 because I'm conscious of your comment of how
 18 the RSP is complicated and we don't want to
 19 make it more complicated.
 20 MR. FAGAN:
 21 A. Mr. Bowman probably knows it better than me.
 22 MR. COXWORTHY:
 23 Q. Well perhaps we'd be better off if he was the
 24 one that was asking the questions, but that's
 25 not how that works here. So I'd like to turn

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1 to page 4 and the hydraulic production.
 2 Perhaps you could help us explain, of course,
 3 this is a snapshot, I suppose, is that fair as
 4 of August 2015 of what's going on, of course
 5 with the hydraulic variation.
 6 MR. FAGAN:
 7 A. We have to be careful somewhat in the use of
 8 the August or the 2015 RSP because the
 9 comparisons that were presented here are
 10 relative to 2007 test year, so the normal
 11 hydraulic production that we'd be talking
 12 about here wouldn't be what's reflected in the
 13 current test year forecast, but what was used
 14 in the 2007. So I think the cost of service
 15 hydraulic production in the '15 will probably
 16 be higher than the, slightly higher than
 17 what's in this one, so your numbers will do
 18 something different.
 19 MR. COXWORTHY:
 20 Q. Will change. Will the pattern stay the same?
 21 MR. FAGAN:
 22 A. But the math--I think it's been a very wet
 23 year, so I think we'd -
 24 MR. COXWORTHY:
 25 Q. Yes, you did say in your evidence earlier that

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1 Hydro has high water, I think, is the -
 2 MR. FAGAN:
 3 A. Yes, so the storage levels have been high I
 4 think most of the year, so I think--so I don't
 5 think the pattern of the numbers will be
 6 different.
 7 MR. COXWORTHY:
 8 Q. And before we get into the pattern, you're
 9 adverting to the fact that this is going to
 10 change because the relationships here are
 11 based on the 2007 GRA, so there will be a
 12 restatement of this as part of the 2013
 13 process that we're into now.
 14 MR. FAGAN:
 15 A. In order to establish rates for 2015, for
 16 example, we talked about the load variation
 17 component, in order to run the load variation
 18 component for 2015, you take the rates coming
 19 out of 2015, compared to the fuel costs for
 20 2015 and so you'd need to have the RSP
 21 reflecting your 2015 forecast. So the
 22 intention is to rerun the RSP for 2015 based
 23 on the approved forecast numbers coming out of
 24 the GRA.
 25 MR. FAGAN:

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1 A. So that will only be after we have an order
 2 from the Board coming out of this GRA that
 3 that restatement will occur?
 4 MR. FAGAN:
 5 A. Yeah, I guess we would have to wait on that,
 6 yeah, we wouldn't have the numbers.
 7 MR. COXWORTHY:
 8 Q. You wouldn't at least normally attempt to
 9 restate it prior to that?
 10 MR. FAGAN:
 11 A. We're in a new world here, so I have to think
 12 about that, okay? It would be difficult
 13 because, for example, the rate proposed for
 14 Newfoundland Power in the amended application
 15 was, I don't know, 11 cents or so, but it
 16 wasn't a number that exactly reflected the
 17 test year fuel price. Historically
 18 Newfoundland Power's rate on the, it's a two-
 19 block rate, we call it a tail-block, the last
 20 block rate, is set based on the fuel price
 21 divided by the fuel efficiency factor. So in
 22 our amended application, it is \$93.00 and if
 23 you divide by the proposed fuel efficiency
 24 factor of 607 kilowatt hours a barrel, you'd
 25 probably end up with a rate of around 15.3

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1 cents a kilowatt hour, okay? So that was the
 2 practice employed back in 2007. With the fuel
 3 prices increasing materially, when Hydro filed
 4 its original application the fuel price was
 5 probably around \$106.00 a barrel in the
 6 original application, and so dividing that by
 7 the fuel efficiency factor, you'd end up with
 8 a price that was so high with regard to tail
 9 block, it actually created complications on
 10 what the first block rate would be, it might
 11 have to be negative in order to come up with
 12 the proper revenue requirement. So Hydro
 13 reviewed it and came up with an alternate
 14 approach reflective of the high fuel cost, so
 15 the price is slightly lower than the standard
 16 approach of taking the fuel price divided by
 17 fuel efficiency. In the settlement agreement,
 18 the fuel prices declined in forecast, like I
 19 say is probably down to about 70 barrels,
 20 \$70.00 a barrel and so the settlement
 21 agreement provides that we use the same
 22 approach as was in the 2007 test year and
 23 divide that by the 607 and come up with a rate
 24 somewhere in the neighbourhood of 11.5 to 12
 25 cents, so knowing what the rate would be would

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1 be an important component of running the RSP,
 2 so without knowing the rates for purposes of
 3 it, it would be difficult to--that would
 4 create some complexities.
 5 MR. COXWORTHY:
 6 Q. Sure, so there's no current plan to restate
 7 prior to? You did say we're into a new world,
 8 would there be some reason perhaps to attempt
 9 a restatement prior to getting a final order
 10 from the Board?
 11 MR. FAGAN:
 12 A. Well there's certainly advantages to it, okay,
 13 because in trying to phase in industrial
 14 customer rates for January, you want to get a
 15 feel for the activity in 2015 and if the
 16 hydraulic balances or the hydraulic transfers
 17 into the plan when a credit balance for 2015,
 18 even relative to the 2015 test year forecast,
 19 you could use that, that would somewhat reduce
 20 the impact of a January 1st rate change, if
 21 there's one to be implemented for industrial
 22 customers. So you could come up with an
 23 estimate, some sort of a forecast RSP for
 24 2015. I mean, the load variation component
 25 aspect, is probably small, and well, maybe

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1 that could be set aside.
 2 MR. COXWORTHY:
 3 Q. So would that be sort of an interim
 4 restatement, is that a -
 5 MR. FAGAN:
 6 A. We'd have to think about it, but I think it's
 7 worth looking at.
 8 MR. COXWORTHY:
 9 Q. And if you were to undertake--Hydro was to
 10 undertake that, I mean, how long would it take
 11 to do that?
 12 MR. FAGAN:
 13 A. I think the key would be just we may want to
 14 circulate our assumptions to the parties to
 15 have an agreement on how we would do that,
 16 because Hydro making the assumptions and
 17 coming out with some numbers may just be in
 18 disagreement with the parties, so presenting
 19 the assumptions before we actually went
 20 through it and get some feedback on it would
 21 probably be a good exercise.
 22 MR. COXWORTHY:
 23 Q. I think asking for an undertaking probably
 24 isn't appropriate under those circumstances
 25 and I'll discuss it with counsel and we'll see

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1 if there's consensus about whether that will
 2 be useful to the parties and to the Board to
 3 have that information before the industrial
 4 customer rates, for example, are set in
 5 January 2015 (sic.), there may be other
 6 reasons why it would be useful to have that
 7 information. Obviously that's the one that's
 8 of concern immediately to the industrial
 9 customers, given that January 1, 2016 is not
 10 that far away.

11 MR. FAGAN:

12 A. I understand that and I was actually
 13 discussing this with someone this morning, we
 14 were talking about the plan for January 1st
 15 rates for industrial customers and we were
 16 struggling somewhat because of the rate
 17 stabilization being in the interim state, and
 18 then also the fact that we've got the current
 19 rules of the RSP preclude the implementation
 20 of a fuel rider and if you actually
 21 implemented a fuel rider, it would be relative
 22 to the 2007 test year, so you'd come up with a
 23 positive fuel price that may not necessarily
 24 make sense with regard to the rate design, and
 25 so I think that's probably a good idea for the

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1 parties to work together in coming up with
 2 something.

3 MR. COXWORTHY:

4 Q. Thank you, Mr. Fagan. Going back then to page
 5 4 of Consent No. 3 and the page on the
 6 hydraulic production variation, August 31st.
 7 I wanted to look at June, July and August and
 8 I guess I'm looking at column C in particular
 9 where we see the production variance go from,
 10 as I would characterize it, a variance in
 11 favour of the customers, to one that's not, is
 12 that a fair way of my characterizing it as we
 13 move from May into June?

14 MR. FAGAN:

15 A. The adjustments for--if we went to column E
 16 for a moment.

17 MR. COXWORTHY:

18 Q. Yes.

19 MR. FAGAN:

20 A. So the adjustments by month were credit
 21 amounts to be, were owned customers and for
 22 the period June, July and August, primarily
 23 because load requirements are lower in the, I
 24 believe, yes, load requirements are lower in
 25 the summer months and maybe also that Hydro

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1 may be operating Holyrood for reliability
 2 purposes, I guess would be the term, to make
 3 sure they're maintaining certain reserves on
 4 the Avalon that hydraulic production may be
 5 down. So the hydraulic production -

6 MR. COXWORTHY:

7 Q. Sorry, are you spilling, is Hydro spilling
 8 water to achieve that--not to achieve, to
 9 arrive at that result?

10 MR. FAGAN:

11 A. I can't answer that, you'd have to ask I think
 12 probably either Mr. Henderson or Mr.
 13 Humphries, probably both of them could answer
 14 the question.

15 MR. COXWORTHY:

16 Q. You did mention perhaps Holyrood was being run
 17 more for reliability reasons during the summer
 18 and that that might be a driver to explain why
 19 this phenomenon is occurring in June, July and
 20 August.

21 MR. FAGAN:

22 A. Even without it though, even if it wasn't,
 23 okay, if loads were down and Hydro was
 24 providing all the loads with the combination
 25 of its hydraulic and its purchases because

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1 it's got, I guess it's take or pay contracts
 2 for its purchases, then you wouldn't have the
 3 hydrology savings with respect to the
 4 calculation of the RSP.

5 MR. COXWORTHY:

6 Q. Is this a phenomenon that recurs in the summer
 7 months? We don't have August 2014 here.

8 MR. FAGAN:

9 A. Well, there's been a change on the system
 10 since 2007. Hydro didn't have wind generation
 11 purchases at the time. Hydro didn't have
 12 purchases from Nalcor back then. I guess the
 13 CBPP Co-gem was still there, okay, so those
 14 additional purchases provided savings to Hydro
 15 since 2007, effectively the savings would have
 16 been the cost of the purchases, the difference
 17 in the cost of the purchases compared to the
 18 test year fuel price at Holyrood back in 2007.
 19 So those 8.8 cents and if Hydro was purchasing
 20 from Nalcor for 4 cents, the 4.8 cents would
 21 have been a savings for Hydro to its bottom
 22 line between test years. But the cost of
 23 Holyrood over the years since 2007 has gone
 24 materially above the 8.8 cents, so for
 25 example, it went over \$100.00 a barrel, so at

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1 16 cents, say, per kilowatt hour, the
 2 difference between the 8.8 cents and the 16
 3 cents, that savings would go to customers. So
 4 customers saved because Holyrood wasn't
 5 required to operate as frequently and Hydro
 6 saved the difference between what was in the
 7 test year fuel price and the 4 cents, say for
 8 the purchases from Nalcor. So that occurred
 9 over the years, because when the RSP was
 10 designed, it was all based on the assumption
 11 that you've got hydraulic and you've got
 12 Holyrood and it's a strict one-to-one shift
 13 type thing. It's not quite in that manner
 14 currently. Now in our current test year, all
 15 the savings as a result of Nalcor purchases
 16 and say wind purchases being less than the
 17 cost of Holyrood are now reflected in the test
 18 year, but the mechanics of the RSP are still
 19 the same with regard to the assumption that
 20 the difference from the hydraulic cost of
 21 service, hydraulic production it's an
 22 assumption that it's all shifting to a
 23 Holyrood cost.
 24 (12:45 p.m.)
 25 MR. COXWORTHY:

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1 Q. And I think your extended--thank you for your
 2 explanation, it's probably answered a number
 3 of my follow-up questions, but perhaps I'll
 4 ask just one and that's in relation to column
 5 E in information 11 on page 4 and the figure
 6 that appears at the bottom of that column for
 7 August, the 7.2 million dollar figure, so is
 8 that a figure that's derived from the cost of
 9 Holyrood fuel?
 10 MR. FAGAN:
 11 A. I would expect the 84 gigawatt hour variance
 12 and the monthly cost, if we converted the
 13 monthly variance to the number of barrels
 14 times the 5449, I believe that should get to
 15 7.3 million.
 16 MR. COXWORTHY:
 17 Q. We'll move on from Consent No. 3, I'm sorry,
 18 we will not, we'll move to page 14, to a
 19 different topic and relation, so still in
 20 Consent 3 and this is the page which deals
 21 with the industrial RSP surplus and you've
 22 been asked some questions about the phase-in,
 23 the industrial customer phase-in, the drawing
 24 down of the surplus, the RSP surplus that's
 25 been allocated for the phase-in purposes. In

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1 the context of the restatement of the RSP that
 2 we were talking about earlier, will that
 3 change, can you give us a sort of a high level
 4 overview and maybe we'll dig, drill down
 5 further from that as to how this will look
 6 different.
 7 MR. FAGAN:
 8 A. I don't think it will change. The RSP surplus
 9 disposition, Teck--there was a direction from
 10 government with respect to Teck being phased
 11 in differently from the other industrial
 12 customers, so the Board approved a specific
 13 Teck rate around a cent, okay, not exactly but
 14 approximately a cent credit, okay? So that's
 15 applied to Teck's load for, to determine that
 16 portion. The August and September numbers,
 17 could be July too, I was looking at it
 18 diagonally somewhat, the July and August
 19 numbers would have been based on the RSP
 20 surplus adjustment approved by the Board
 21 effective July 1st which would also be load
 22 base numbers of the industrial customers, so
 23 they're not impacted by any other factors
 24 within the RSP, so those should stay the same.
 25 MR. COXWORTHY:

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1 Q. Does the change in the cost of Holyrood fuel,
 2 if we go to the 70 cents, this is not based on
 3 70 cents here, is it?
 4 MR. FAGAN:
 5 A. No.
 6 MR. COXWORTHY:
 7 Q. It's based on 93?
 8 MR. FAGAN:
 9 A. Well it's irrelevant, the credit for
 10 industrial customers is based on, I think if
 11 we go to CA-363. Move down a little bit
 12 further, please? Okay, lines 1 to 4. Okay,
 13 the RSP surplus adjustment factors are 49
 14 cents per kilowatt and .296 cents per kilowatt
 15 hour credit, so those numbers are applying to
 16 the industrial customer loads for those
 17 months, so they wouldn't change.
 18 MR. COXWORTHY:
 19 Q. Thank you. Mr. Chair, I think it would be a
 20 more efficient use of my time and I think the
 21 Board's time if perhaps we could have a five-
 22 minute break to discuss with our consultant
 23 just how much further we need to delve into
 24 these issues.
 25 CHAIRMAN:

1 Q. Certainly sir.
2 (OFF RECORD - 12:50 P.M.)
3 (RESUMED - 12:59 P.M.)
4 CHAIRMAN:
5 Q. Well after a heated argument, we're going to
6 adjourn. (Laughter) That's it, I guess,
7 until tomorrow?
8 MR. COXWORTHY:
9 Q. That's correct. No further questions from the
10 industrial customers, Mr. Chair.
11 MS. GLYNN:
12 Q. Yes, and we thought it was more efficient use
13 of our time to take the afternoon and the
14 evening to prepare for tomorrow.
15 CHAIRMAN:
16 Q. Contemplate the meaning of it all, okay.
17 MS. GLYNN:
18 Q. Yes, thank you.
19 Upon concluding at 1:00 p.m.

1
2 CERTIFICATE
3 I, Judy Moss, hereby certify that the foregoing is a true
4 and correct transcript of a hearing in the matter of
5 Newfoundland and Labrador Hydro's General Rate
6 Application heard on the 6th of October, A.D., 2015
7 before the Commissioners of the Public Utilities Board,
8 St. John's, Newfoundland and Labrador and was transcribed
9 by me to the best of my ability by means of a sound
10 apparatus.
11 Dated at St. John's, Newfoundland and Labrador
12 this 6th day of October, A.D., 2015
13 Judy Moss

-\$-

\$10.18 [2] 110:22 119:24
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