

Page 1	Page 3
<p>1 (January 10, 2013)</p> <p>2 CHAIRMAN:</p> <p>3 Q. Good morning everybody. This is the</p> <p>4 Newfoundland Power 2013 General Rate</p> <p>5 Application hearing. My name is Andy Wells</p> <p>6 and I'm joined by my colleagues, Dwanda Newman</p> <p>7 and James Oxford. Glenda Gibbons from</p> <p>8 Discoveries Unlimited is assisting Cheryl</p> <p>9 Blundon with the transcripts of today's</p> <p>10 hearings. Our schedule for today's evidence</p> <p>11 should continue until about 1:30 today with a</p> <p>12 half-hour break between 11 and 11:30. As for</p> <p>13 tomorrow, we will just have to wait and see</p> <p>14 what the Good Lord sends us.</p> <p>15 Before we get started, could the panel</p> <p>16 introduce yourselves.</p> <p>17 KELLY, Q.C.:</p> <p>18 Q. Thank you, Mr. Chair. Ian Kelly here</p> <p>19 representing Newfoundland Power. Joining me</p> <p>20 is Gerard Hayes, Newfoundland Power, and Chris</p> <p>21 Wells who is assisting us with the documents.</p> <p>22 CHAIRMAN:</p> <p>23 Q. That's a good name.</p> <p>24 MR. JOHNSON:</p> <p>25 Q. Tom Johnson here, Mr. Chair, on behalf of the</p>	<p>1 conference, time was allowed for Requests for</p> <p>2 Information to be submitted and responses to</p> <p>3 be filed. Time was also allowed for the</p> <p>4 parties to retain experts as required.</p> <p>5 The Board requested the parties to</p> <p>6 participate in a Board facilitated settlement</p> <p>7 process to discuss the issues contained in the</p> <p>8 application. This negotiation process, as</p> <p>9 indicated by the Chair, was held the week of</p> <p>10 December 17th and a resulting settlement</p> <p>11 agreement was filed with the Board on December</p> <p>12 21st. All parties have a copy of this</p> <p>13 agreement and it will be entered onto the</p> <p>14 record as Consent Exhibit No. 1. I'd like to</p> <p>15 take a moment just to review the issues which</p> <p>16 have been agreed upon by the parties.</p> <p>17 The parties have agreed that the Board</p> <p>18 may rely upon the Customer Energy and Demand</p> <p>19 Forecast dated August 2012 which was submitted</p> <p>20 with the Application. Changes to the</p> <p>21 calculation and amortization of the defined</p> <p>22 benefit pension expense have also been agreed</p> <p>23 to. The deferral and amortization of</p> <p>24 conservation program costs over a seven-year</p> <p>25 period have been agreed to. However, the</p>
Page 2	Page 4
<p>1 consumer. Here with me is Dr. Lawrence Booth</p> <p>2 and counsel, Greg Kirby. Thank you.</p> <p>3 CHAIRMAN:</p> <p>4 Q. Okay. We will pass it on to Ms. Jacqueline</p> <p>5 Glynn to get things started.</p> <p>6 MS. GLYNN:</p> <p>7 Q. Thank you, Mr. Chair. Good morning to the</p> <p>8 panel and to everybody who has joined us here</p> <p>9 this morning. On September 14th, the Board</p> <p>10 received a General Rate Application from</p> <p>11 Newfoundland Power to establish new rates for</p> <p>12 its customers.</p> <p>13 Newfoundland Power is requesting that the</p> <p>14 Board approve, among other things, an overall</p> <p>15 average increase in current electricity rates</p> <p>16 of six percent as of March 1st, 2013, which</p> <p>17 includes proposed increases ranging from 0.6</p> <p>18 percent to 6 percent for commercial customers</p> <p>19 and proposed average increases of 7.2 percent</p> <p>20 for residential customers.</p> <p>21 The Board held a pre-hearing conference</p> <p>22 on October 11th, 2012 to identify the</p> <p>23 registered intervenors and to set the</p> <p>24 procedures and schedule for this public</p> <p>25 hearing. Following the pre-hearing</p>	<p>1 Consumer Advocate has reserved the right to</p> <p>2 cross-examine on the actual program costs.</p> <p>3 The parties agreed to changes in the Weather</p> <p>4 Normalization Reserve Account. The parties</p> <p>5 agreed to cost recovery for existing deferral</p> <p>6 accounts, the hearing costs and a revenue</p> <p>7 shortfall for 2013. The Forecast Average Rate</p> <p>8 Base for 2013 and for 2014 will be used for</p> <p>9 rate making purposes, subject to any</p> <p>10 adjustments from the Board's determination on</p> <p>11 issues that have not been settled. Proposed</p> <p>12 changes to the rate design and rate structure</p> <p>13 have been agreed to and proposed changes to</p> <p>14 the Rate Stabilization clause have also been</p> <p>15 agreed to. The remainder of the issues in the</p> <p>16 Application will be examined throughout this</p> <p>17 hearing.</p> <p>18 Notice of the start date for this hearing</p> <p>19 was published in papers throughout the</p> <p>20 Province started on December 15th, 2012. The</p> <p>21 only remaining deadlines are for public</p> <p>22 participation. Requests to make an oral</p> <p>23 submission must be submitted by noon tomorrow,</p> <p>24 Friday, January 11th. Any written letters of</p> <p>25 comments must be submitted by Friday, January</p>

Page 5	Page 7
<p>1 18th.</p> <p>2 The Board's financial consultants, Grant</p> <p>3 Thornton, submitted a report on November 9th,</p> <p>4 2012. The parties have agreed to accept this</p> <p>5 report without the necessity of a</p> <p>6 representative from Grant Thornton appearing</p> <p>7 to adopt it and neither party wishes to cross-</p> <p>8 examine on that report. Again, the parties</p> <p>9 already have a copy and that will be entered</p> <p>10 onto the record as Consent Exhibit No. 2.</p> <p>11 Evidence will start today with the</p> <p>12 company witnesses. Cost of Capital is</p> <p>13 scheduled for next week and depreciation</p> <p>14 evidence for the end of the following week.</p> <p>15 As the Chair has indicated, the normal</p> <p>16 sitting schedule is from 9 to 1:30 with a</p> <p>17 half-hour break at 11. However, during the</p> <p>18 Cost of Capital evidence, we have agreed to</p> <p>19 sit at least an hour later, until 2:30. An</p> <p>20 additional break may be required on those</p> <p>21 sitting days. And of course, again, the storm</p> <p>22 may put some changes into that schedule.</p> <p>23 Mr. Chair, I confirm that the Application</p> <p>24 has been properly filed and appropriate</p> <p>25 notices published. There are no preliminary</p>	<p>1 event through the Energy Supply Cost Variance</p> <p>2 mechanisms. So this Application is really</p> <p>3 about the other 3.4 percent of the proposed</p> <p>4 increase.</p> <p>5 The second component is the Return on</p> <p>6 Equity. It amounts to 1.8 percent. Now it's</p> <p>7 important to remember that customer rates went</p> <p>8 down in 2011 when the allowed return was</p> <p>9 reduced from 9 percent to 8.38 percent through</p> <p>10 the operation of the Automatic Adjustment</p> <p>11 Formula. But rates did not go back up in 2012</p> <p>12 when the allowed return was increased to 8.8</p> <p>13 percent. It was already June of 2012 when</p> <p>14 that occurred, so the recovery of that</p> <p>15 increase was deferred. Only the return of</p> <p>16 8.38 percent is currently embedded in customer</p> <p>17 rates. The 1.8 percent increase covers the</p> <p>18 difference between that 8.38 and the 10.4</p> <p>19 percent based upon the evidence in the</p> <p>20 Company's Cost of Capital witnesses. And of</p> <p>21 course, the final percentage will obviously</p> <p>22 depend upon the determination of the Board as</p> <p>23 to the appropriate Return on Equity.</p> <p>24 And the final 1.6 percent represents</p> <p>25 everything else which is a relatively modest</p>
Page 6	Page 8
<p>1 matters which I have been made aware of. You</p> <p>2 may ask the parties for their opening</p> <p>3 statements.</p> <p>4 CHAIRMAN:</p> <p>5 Q. Okay. Newfoundland Power can proceed, sir.</p> <p>6 KELLY, Q.C.:</p> <p>7 Q. Thank you, Mr. Chairman. As Ms. Glynn has</p> <p>8 already explained, agreement has been reached</p> <p>9 with respect to many of the Company's</p> <p>10 proposals contained in this Application. The</p> <p>11 settled issues are set out in the agreement</p> <p>12 which has been entered, Consent 1. I won't go</p> <p>13 through them now. The Company's witnesses</p> <p>14 will not specifically speak to those settled</p> <p>15 issues in their testimony. However, they</p> <p>16 will, of course, be happy to answer any</p> <p>17 questions that the Board may have.</p> <p>18 In this hearing, Newfoundland Power is</p> <p>19 requesting an average increase in customer</p> <p>20 rates of approximately 6 percent. That 6</p> <p>21 percent breaks down into essentially three</p> <p>22 components. The largest component, 2.6</p> <p>23 percent, is simply the rebalancing of the 2013</p> <p>24 and 2014 energy supply costs. That increase</p> <p>25 would have flowed through to customers in any</p>	<p>1 increase, percentage wise, over the 2010 year</p> <p>2 test year costs. So the principal issues in</p> <p>3 this case are the cost of capital issues,</p> <p>4 return on equity, capital structure and the</p> <p>5 use of an automatic adjustment formula.</p> <p>6 In relation to capital structure, the</p> <p>7 Board has consistently approved a capital</p> <p>8 structure for Newfoundland Power of 45 percent</p> <p>9 equity. We believe that capital structure</p> <p>10 should be maintained. The Board has</p> <p>11 recognized that Newfoundland Power's 45</p> <p>12 percent equity ratio is an important factor</p> <p>13 which sustains Newfoundland Power's overall</p> <p>14 average risk profile. In relation to the</p> <p>15 formula, the company is again proposing</p> <p>16 discontinuance of the automatic adjustment</p> <p>17 formula. The purpose of the formula was to</p> <p>18 reduce regulatory burden, promote regulatory</p> <p>19 efficiency and reduce costs. Those objectives</p> <p>20 have not been achieved over the past several</p> <p>21 years. The abnormal capital market conditions</p> <p>22 which existed in 2009 continued throughout</p> <p>23 2010, 2011, 2012 and are continuing in 2013.</p> <p>24 Maintaining the formula since 2010 has</p> <p>25 increased the number of regulatory hearings</p>

Page 9	Page 11
<p>1 and added to regulatory cost rather than 2 promoting efficiency. So Newfoundland Power 3 continues to believe that the best approach is 4 to discontinue use of the formula until 5 financial markets return to more normal 6 conditions and a regulatory consensus emerges 7 as to the utility of a formula in the new 8 economic order.</p> <p>9 With respect to the other costs, as Ms. 10 Greene and Ms. Glynn have referred to, Grant 11 Thornton has conducted a detailed review of 12 Newfoundland Power's operating costs, the 13 amortization and deferred recoveries, the 14 demand forecast, rate base and other matters. 15 Grant Thornton has filed a comprehensive 16 report in which it found no basis to conclude 17 that there was anything unreasonable with any 18 of these items. The Board, I think, can take 19 comfort from Grant Thornton's analysis and 20 conclusions with respect to the overall 21 reasonableness of the company's operating 22 costs and these other items.</p> <p>23 I'd also like to mention that in 24 preparing its test year costs, Newfoundland 25 Power has built into those estimates certain</p>	<p>1 depreciation, as the Consumer Advocate 2 proposes, increases the rate base which in 3 turn adds to the required return on that rate 4 base. Customer rates are approximately 3.7 5 million dollars less today because of the 6 Board's decision to adopt ELG. Reversing that 7 process would result in a current reduction in 8 rates at the expense of higher rates in the 9 future and that would not be in the interests 10 of the long -- the long terms interests of 11 Newfoundland Power's customers.</p> <p>12 And on this point, Mr. Chairman, I 13 observe that in a GRA, which is where we are 14 now, the Board examines the company's test 15 year costs for reasonableness and prudence. 16 That's the test to be applied. And as our 17 Court of Appeal has pointed out, management is 18 entitled to exercise judgment in running the 19 company and is entitled to a presumption of 20 good faith. That applies to determining 21 depreciation expense. So the practical burden 22 here lies upon the Consumer Advocate to 23 demonstrate that the depreciation expense for 24 the test year is not reasonable and prudent. 25 Mr. Chairman, let me next turn to the</p>
Page 10	Page 12
<p>1 labour force efficiency assumptions. 2 Newfoundland Power will serve 1.3 percent more 3 customers with 1 percent less in labour costs. 4 Customers will receive the benefits of those 5 productivity assumptions whether or not the 6 company succeeds in achieving those 7 operational efficiencies.</p> <p>8 The only other item I wanted to address 9 at this time is the depreciation issue. This 10 is an issue which has been raised by the 11 Consumer Advocate. He challenges the 12 depreciation methodology, not simply the 13 application of that methodology to the current 14 assets. The Board determined the appropriate 15 methodology and ordered the implementation of 16 what's called the Equal Life Group or ELG 17 methodology over a five-year period from 1977 18 to 1983. The Board has ordered updated 19 depreciation studies based upon that 20 methodology every four or five years since 21 then. The company completed the most recent 22 update in 2010 using the approved methodology 23 and experience has demonstrated that the 24 Board's decision to adopt the ELG depreciation 25 methodology was correct. Reducing</p>	<p>1 witnesses that you'll hear in this proceeding. 2 Newfoundland Power intends to call six 3 witnesses. Mr. Earl Ludlow, the president and 4 chief executive officer, will testify first 5 and subject to tomorrow's weather, the next 6 witness will be Ms. Jocelyn Perry, the vice- 7 president finance and chief financial officer 8 of the company. She will deal with the 9 financial evidence, including depreciation 10 expense, insofar as it affects financial 11 parameters. During the cost of capital phase, 12 you'll hear the expert testimony from Ms. 13 Kathleen McShane and Mr. James VanderWeide. 14 Mr. John Wiedmayer of Gannett Fleming will 15 testify with respect to depreciation. And 16 finally, Mr. Gary Smith, Newfoundland Power's 17 vice-president of customer operations and 18 engineering will answer questions with respect 19 to operating costs.</p> <p>20 Mr. Chairman, those are my opening 21 comments, unless you have any questions. 22 Thank you.</p> <p>23 MR. JOHNSON: 24 Q. Mr. Chairman and Commissioners, Newfoundland 25 Power is back before this Board seeking a rate</p>

Page 13	Page 15
<p>1 increase which in significant measure is 2 driven by a wholly unrealistic request for its 3 return on equity. It expects, to put this in 4 context, to earn a net income of 36 and a half 5 million dollars in 2012. But in 2013, it 6 wants this Board to set rates high enough to 7 let it earn 42 and a half million dollars. 8 That's just in 2013. And in 2014, rates high 9 enough to let it earn 44 million dollars in 10 net income. It seeks a return on equity of 11 10.4 percent in 2013 and 2014. This would put 12 Newfoundland Power at the highest allowed 13 return in Canada for any regulated utility, 14 whether electric, gas or anything else. In my 15 respectful submission, this is a gross 16 overstatement of Newfoundland Power's fair 17 return.</p> <p>18 I'll repeat what I said at the 2009 19 General Rate Application of Newfoundland Power 20 which Mr. Ludlow agreed with at the time, and 21 that is, Newfoundland Power has been and will 22 continue to be a very well protected, stable, 23 predictable, conservative, low risk utility 24 operating in a very supportive regulatory 25 environment where the company enjoys moderate,</p>	<p>1 Newfoundland Power is once again making a 2 case for a higher return based largely on cost 3 of capital witnesses from the United States 4 who say, in essence, that Newfoundland Power 5 is comparable to their US utilities and that 6 its return, in essence, should be similar. 7 Now we went down this road already with 8 Newfoundland Power in their last General Rate 9 Application and what did the Board conclude in 10 its decision? It concluded as follows, and I 11 quote: "The Board believes that in this type 12 of analysis it is not enough that the chosen 13 comparables are the best available. If this 14 data is to be relied on, it must be shown to 15 be a reasonable proxy or that reasonable 16 adjustments can be made to account for the 17 differences. The evidence showed significant 18 differences in virtually all of the 19 comparables including significant levels of 20 non-regulated and non-utility business, as 21 well as riskier generation projects, earnings 22 volatility, more competition and less 23 regulatory support. While it was argued that 24 on balanced, the US comparables are reasonable 25 proxies, the Board notes the overwhelming</p>
Page 14	Page 16
<p>1 yet fairly steady customer growth, free from 2 any significant competition. With only a 3 small amount of generation, Newfoundland Power 4 is predominantly poles and wires. In essence, 5 it is very low risk. That's what I said in 6 2009 and the same remains.</p> <p>7 The fact is that Newfoundland Power is 8 risk adverse. It has a penchant for 9 mechanisms that transfer risk to its 10 customers. Indeed, since the last hearing 11 before this Board in 2009, two further 12 deferral accounts have kicked in. One totally 13 removes the risk of forecasting pension 14 expense and the other set up in 2011 totally 15 removes any risk to the company associated 16 with forecasting costs of other post- 17 employment benefits.</p> <p>18 Newfoundland Power is left with next to 19 no risk and in order for customers to benefit 20 from the low risk environment that has been 21 set up, the return on equity that is used in 22 setting Newfoundland Power's rates must 23 reflect the lower risk to which the company is 24 exposed and the commensurate higher risk that 25 its customers face.</p>	<p>1 evidence of a lack of balance as it was clear 2 that on almost every measure, Newfoundland 3 Power would have to be considered less risky 4 than the US comparables."</p> <p>5 Mr. Chairman and Commissioners, as the 6 great Yogi Berra said, it's like deja vu all 7 over again. For what did Newfoundland Power 8 do in the face of these clear admonitions from 9 the Board? Did they change their approach? 10 No. In fact, they doubled down on it, hiring 11 not one US cost of capital witness, but two, 12 at considerable expense. These witnesses use 13 the same approach where once again they say to 14 the Board that companies such as Consolidated 15 Edison, Southern and Vectrin are comparable to 16 Newfoundland Power and that the Board should 17 get on with it, rely on the financial results 18 from these US companies without adjustments in 19 determining Newfoundland Power's fair return 20 on equity. Mr. Chairman and Commissioners, 21 these companies were not comparable in 2009 22 and they are not comparable today.</p> <p>23 What's more, in this case begs the 24 question with the doubling down on cost of 25 capital witnesses by Newfoundland Power is do</p>

Page 17	Page 19
<p>1 we really want to go down the road of 2 scrapping the automatic adjustment formula as 3 Newfoundland Power proposes it and replacing 4 it with nothing? They say the formula doesn't 5 work. Yet, they bring forward no constructive 6 suggestions at all as to how it may be 7 modified. One of the features of it, besides 8 reducing the frequency of general rate 9 applications, is to provide an incentive to 10 pursue productivity gains in the non-GRA 11 years. This Board held in its last GRA Order 12 that the automatic adjustment formula was 13 "fundamental to the multi-year regime in place 14 in this jurisdiction." Those words were as 15 true then as they are now.</p> <p>16 What is no longer a good incentive is to 17 reward Newfoundland Power's executives and 18 management team through customer funded short 19 term incentive pay which is tied to the amount 20 of profit Newfoundland Power can make for its 21 shareholders. While this has been the 22 practice for some years, it is time to end it 23 in this hearing. The primary beneficiary of 24 more company profit is the shareholder, not 25 the company, and that's not deniable.</p>	<p>1 I just want to state for the record that we 2 have a right to be here. Newfoundland Power 3 has a right to make an application. The 4 Consumer Advocate has a right to be here. It 5 has nothing to do with this other issue that 6 is a matter of concern to the protestors, the 7 strikers and it's deeply disrespectful of 8 people's right to peacefully assemble and go 9 about their business to have to be subjected 10 to this kind of interruption and harassment 11 and if it reoccurs again, all I can tell all 12 of the parties is that we shall deal with it 13 and deal with it resolutely. We're not going 14 to tolerate any interruptions in our right to 15 peacefully proceed with the business that is 16 before this tribunal. So, Mr. Johnson, I 17 think I'm back to you.</p> <p>18 MR. JOHNSON:</p> <p>19 Q. Mr. Chairman and Commissioners, our contention 20 in this hearing is that in relation to the 21 short term incentive pay aspect of the 22 company's executives and managers 23 compensation, it is very clear that the 24 primary beneficiary of more company profit is 25 the shareholder, not the customer, and</p>
Page 18	Page 20
<p>1 Accordingly, it is the shareholder who should 2 pay all the salary and associated costs of 3 incenting the executives and managers to 4 achieve the profit targets.</p> <p>5 CHAIRMAN:</p> <p>6 Q. Mr. Johnson, I'm going to stop you here just 7 for one second. I'm sorry, sir, that's not 8 permitted in here. I'll ask you to leave with 9 that placard.</p> <p>10 PROTESTOR:</p> <p>11 Q. It's just a -</p> <p>12 CHAIRMAN:</p> <p>13 Q. No, no, sir, you're not allowed to speak. I'm 14 sorry. I will ask you to leave. Well, I'll 15 ask you to take down the placard. We'll 16 adjourn for a couple of minutes and if you 17 don't leave, sir, I probably will call the 18 police.</p> <p>19 (OFF RECORD)</p> <p>20 (10:00 a.m.)</p> <p>21 CHAIRMAN:</p> <p>22 Q. We shall recommence our proceedings, ladies 23 and gentlemen. If there is any further 24 disruptions of our right to peacefully proceed 25 with this application, we shall deal with it.</p>	<p>1 therefore, it is the shareholder who should 2 pay all of the salary and associated costs of 3 incenting the company's executives and 4 managers to achieve profit targets.</p> <p>5 We also look forward in due course to 6 examination of the company's operating costs 7 in the coming days, in particular during the 8 phase when we'll be hearing from Newfoundland 9 Power's vice-president of operations, Mr. 10 Smith.</p> <p>11 In this proceeding, the Consumer Advocate 12 will be calling two expert witnesses. The 13 first expert witness I will be calling will be 14 Dr. Lawrence Booth. Dr. Booth is a professor 15 of finance at the Rotman School of Management 16 at the University of Toronto where he holds 17 the CIT Chair in structural finance, a chair 18 that he's held since 1999. His research 19 interests centre on the cost of capital 20 international corporate finance and capital 21 markets theory. His teaching area is in 22 domestic and international finance. 23 Incidentally, Dr. Booth also serves on the 24 governing council of the pension -- the 25 Pension Committee of the Governing Council of</p>

Page 21	Page 23
<p>1 the University of Toronto, and as such, brings</p> <p>2 a realistic perspective on the returns that</p> <p>3 are being forecasted on equities and bonds.</p> <p>4 Dr. Booth has testified widely in Canada and</p> <p>5 previously, as I alluded to, testified before</p> <p>6 the Board of Commissioners at Newfoundland</p> <p>7 Power's 2010 GRA. Dr. Booth will testify as</p> <p>8 to a fair and just return for Newfoundland</p> <p>9 Power and in relation to the automatic</p> <p>10 adjustment formula.</p> <p>11 As regards depreciation, the second</p> <p>12 witness I will call is Mr. Jacob Pous, who is</p> <p>13 a principal of the firm, Diversified Utility</p> <p>14 Consultants in Austin, Texas. He's a</p> <p>15 professional engineer and has participated in</p> <p>16 well over 400 utility rate proceedings in both</p> <p>17 the United States and Canada. He's also</p> <p>18 completed a series of programs in relation to</p> <p>19 depreciation and has testified extensively on</p> <p>20 matters of depreciation amongst other utility</p> <p>21 issues. He's testified on behalf of the staff</p> <p>22 of five State regulatory commissions and one</p> <p>23 Canadian utility regulator. Mr. Pous was</p> <p>24 retained by the Consumer Advocate to address</p> <p>25 the level of depreciation expense and rates</p>	<p>1 MR. EARL LUDLOW, SWORN, EXAMINATION-IN-CHIEF BY IAN</p> <p>2 KELLY, Q.C.</p> <p>3 KELLY, Q.C.:</p> <p>4 Q. Thank you, Mr. Chairman. Good morning, Mr.</p> <p>5 Ludlow. You are the president and chief</p> <p>6 executive officer of Newfoundland Power?</p> <p>7 MR. LUDLOW:</p> <p>8 A. Yes, that's correct.</p> <p>9 KELLY, Q.C.:</p> <p>10 Q. And you will introduce this General Rate</p> <p>11 Application on behalf of the company. Do you</p> <p>12 adopt Section 1, the introduction, as your</p> <p>13 testimony?</p> <p>14 MR. LUDLOW:</p> <p>15 A. Yes, I do.</p> <p>16 KELLY, Q.C.:</p> <p>17 Q. Are there any changes that you wish to make to</p> <p>18 the pre-filed testimony and exhibits at this</p> <p>19 time?</p> <p>20 MR. LUDLOW:</p> <p>21 A. No.</p> <p>22 KELLY, Q.C.:</p> <p>23 Q. First of all, how long have you been the</p> <p>24 president and CEO of Newfoundland Power?</p> <p>25 MR. LUDLOW:</p>
Page 22	Page 24
<p>1 proposed by Newfoundland Power based on its</p> <p>2 2010 Gannett Fleming depreciation study filed</p> <p>3 as part of this General Rate Application. In</p> <p>4 the first place, Mr. Pous will challenge the</p> <p>5 company's depreciation witnesses, average</p> <p>6 service lives in relation to several</p> <p>7 categories of property and assets of</p> <p>8 Newfoundland Power and he also challenges the</p> <p>9 company's Equal Life Group calculation</p> <p>10 procedure in favour of the average life group</p> <p>11 procedure that is in wide use in both Canada</p> <p>12 and in the United States in the utility</p> <p>13 context.</p> <p>14 To conclude, Mr. Chairman and</p> <p>15 Commissioners, we look forward to representing</p> <p>16 the customers of Newfoundland Power in this</p> <p>17 rate proceeding and to getting on with the</p> <p>18 hearing. Thank you very much.</p> <p>19 CHAIRMAN:</p> <p>20 Q. Back to you, sir.</p> <p>21 KELLY, Q.C.:</p> <p>22 Q. Thank you, Mr. Chairman. The next witness, or</p> <p>23 the first witness will be Mr. Earl Ludlow.</p> <p>24 The witness is ready to be sworn, Mr.</p> <p>25 Chairman.</p>	<p>1 A. Since 2007 and I've also served as a director</p> <p>2 of Maritime Electric Company and also Fortis</p> <p>3 Ontario, and prior to 2007, I held senior</p> <p>4 positions in Fortis Utilities in Prince Edward</p> <p>5 Island, Alberta and British Columbia.</p> <p>6 KELLY, Q.C.:</p> <p>7 Q. Mr. Ludlow, in this application, Newfoundland</p> <p>8 Power is proposing an average rate increase of</p> <p>9 approximately 6 percent. Would you explain to</p> <p>10 the Board the key drivers for this increase?</p> <p>11 MR. LUDLOW:</p> <p>12 A. Yes. As you indicated, Newfoundland Power is</p> <p>13 requesting a 6 percent average increase in</p> <p>14 customer rates. If we look at Exhibit EAL-1 -</p> <p>15 KELLY, Q.C.:</p> <p>16 Q. And that can perhaps be marked, Mr. Chairman,</p> <p>17 for the record. Thank you.</p> <p>18 MR. LUDLOW:</p> <p>19 A. - you'll see that there are three principal</p> <p>20 components of this increase. Rebalancing of</p> <p>21 the 2013-2014 energy supply costs accounts for</p> <p>22 approximately 2.6 percent. As you indicated</p> <p>23 in your opening comments, these costs would</p> <p>24 have been recovered to the energy supply cost</p> <p>25 variance mechanism if there had not been a</p>

Page 25	Page 27
<p>1 general rate application.</p> <p>2 As second part of the increase relates to</p> <p>3 the return on equity. The application</p> <p>4 proposes a return -- a rate of return of 10. 4</p> <p>5 percent. Current electricity rates reflect a</p> <p>6 return on equity of 8.38 percent. This</p> <p>7 difference accounts for approximately 1. 8</p> <p>8 percent of the increase in customer rates.</p> <p>9 A third component, 1.6 percent,</p> <p>10 represents all the other costs. Changes in</p> <p>11 operating costs do not play a large part in</p> <p>12 this rate increase, especially bearing in mind</p> <p>13 the significant cost pressures in the</p> <p>14 Newfoundland economy. This demonstrates to me</p> <p>15 the efficient nature of our operations at</p> <p>16 Newfoundland Power.</p> <p>17 So this proceeding is really about the</p> <p>18 appropriate return for Newfoundland Power and</p> <p>19 a relatively small increase in other costs.</p> <p>20 Our residential customers will experience</p> <p>21 a somewhat larger rate increase at 7. 2</p> <p>22 percent. The increase for our smallest</p> <p>23 general service customers will only be 0. 6</p> <p>24 percent. These changes correct long standing</p> <p>25 cost recovery issues and ensures that all</p>	<p>1 believe we're doing a reasonable job with</p> <p>2 meeting our customers' expectations.</p> <p>3 Our workforce is a key factor in</p> <p>4 maintaining operational efficiency and</p> <p>5 customer responsiveness. We are managing our</p> <p>6 workforce to ensure that we provide safe,</p> <p>7 reliable service, not only today but into the</p> <p>8 future. As you know, skilled workers are in</p> <p>9 high demand in today's economy. We have</p> <p>10 increased our recruitment and training to</p> <p>11 ensure that we have the ability to provide</p> <p>12 efficient and reliable service for our</p> <p>13 customers.</p> <p>14 So, I think we're focused on the right</p> <p>15 things. The things that provide least cost</p> <p>16 reliable service to our customers.</p> <p>17 KELLY, Q.C.:</p> <p>18 Q. You've indicated that Newfoundland Power's</p> <p>19 rate of return on equity is one component of</p> <p>20 the proposed increase. Can you place this</p> <p>21 aspect of the application in context for us?</p> <p>22 MR. LUDLOW:</p> <p>23 A. Yes, I can. In the company's last General</p> <p>24 Rate Application in 2009, Newfoundland Power</p> <p>25 sought a higher return than the approximately</p>
Page 26	Page 28
<p>1 customers bear an equitable share of the cost</p> <p>2 of service.</p> <p>3 KELLY, Q.C.:</p> <p>4 Q. Next, would you give us a brief overview of</p> <p>5 Newfoundland Power's current operations?</p> <p>6 MR. LUDLOW:</p> <p>7 A. Certainly. Our operational focus at</p> <p>8 Newfoundland Power has two main components:</p> <p>9 operational efficiency and customer</p> <p>10 responsiveness. I believe our operations are</p> <p>11 efficient and well managed. The assets that</p> <p>12 make up our electrical system are in</p> <p>13 reasonably good condition. Currently, our</p> <p>14 operations provide reliable, electrical</p> <p>15 service to our customers, so our system</p> <p>16 operations are in good shape.</p> <p>17 Our customer satisfaction remains high.</p> <p>18 We continue to adapt to changes in our</p> <p>19 customer service expectations. A good example</p> <p>20 of this is the expanded customer energy</p> <p>21 conservation portfolio. Customers are looking</p> <p>22 for ways to save energy and lower their</p> <p>23 electricity bills. Our response increase our</p> <p>24 costs but reduces our customers' bills and</p> <p>25 reduces oil consumed at Holyrood. So I</p>	<p>1 7.5 percent indicated by the formula. The</p> <p>2 company also sought suspension of the formula.</p> <p>3 The Board ruled that a 9 percent return on</p> <p>4 equity was reasonable and that the formula</p> <p>5 should continue in use. For 2011, the formula</p> <p>6 reduced our return on equity to 8.38 percent,</p> <p>7 which I understand was the lowest allowed</p> <p>8 return for an investor owned utility in North</p> <p>9 America. For 2012, the formula indicated a</p> <p>10 further reduction in the company's return on</p> <p>11 equity to 7.85 percent.</p> <p>12 (10:15 a.m.)</p> <p>13 Now in late 2011, the company applied to</p> <p>14 suspend operation of the formula for 2012 and</p> <p>15 following a further application, Newfoundland</p> <p>16 Power's 2012 return on equity was set at 8.8</p> <p>17 percent.</p> <p>18 In this application, Newfoundland Power</p> <p>19 is again requesting that the Board establish a</p> <p>20 fair return on equity for 2013 and 2014 and</p> <p>21 discontinue the use of the formula.</p> <p>22 KELLY, Q.C.:</p> <p>23 Q. In Newfoundland Power's last rate order from</p> <p>24 the Board, the Board concluded that</p> <p>25 Newfoundland Power continues to be an average</p>

Page 29	Page 31
<p>1 risk Canadian utility. How do you see 2 Newfoundland Power's current risk profile? 3 MR. LUDLOW: 4 A. I believe Newfoundland Power's risk profile is 5 substantially the same as it was in 2009. We 6 face some unique challenges. We are a small 7 utility. We operate in an isolated system in 8 a harsh weather environment and the 9 demographics of our service territory are 10 changing. Our operational challenges may be 11 greater than that of many other Canadian 12 utilities. As this Board has observed in the 13 past, these challenges are offset by our 14 strong capital structure. We also have a 15 generally supportive regulatory environment 16 similar to other utilities in Canada. So, on 17 balance, we still consider our self an average 18 risk utility. 19 KELLY, Q.C.: 20 Q. Would you comment on Newfoundland Power's 21 relative operational risks? 22 MR. LUDLOW: 23 A. As I've indicated earlier, I've served as a 24 director or officer of Fortis utilities in 25 four provinces, in addition to Newfoundland</p>	<p>1 an aging workforce at a time when skilled 2 workers are in high demand in other sectors of 3 this economy. 4 In the coming years, our customers will 5 face higher costs due to increases in 6 Newfoundland Power's purchase power expense as 7 a result of the Labrador infeed, the 8 retirement of Holyrood and other capital 9 expenditures by Hydro. Those cost changes 10 will pose challenges for Newfoundland Power. 11 KELLY, Q.C.: 12 Q. Would you comment on the regulatory support in 13 this jurisdiction? 14 MR. LUDLOW: 15 A. Newfoundland Power has reasonable regulatory 16 support. However, this is not out of step 17 with the rest of the country. All 18 distribution utilities I have worked with have 19 full supply cost recovery flow-through 20 mechanisms through regulatory mechanisms. It 21 is also common to have regulatory mechanisms 22 which permit recovery of future benefit costs. 23 It is not unusual for there to be differences 24 in details from province to province. For 25 example, I know from my experience as an</p>
Page 30	Page 32
<p>1 and Labrador. Newfoundland Power certainly 2 has the most difficult weather conditions and 3 today being no exception, I might add, Mr. 4 Chairman. Of any of the five provinces I've 5 had the privilege of working in, Newfoundland 6 and Labrador has the most severe wind and ice 7 conditions in populated regions of Canada. 8 Maintaining reliable service in these 9 conditions is a particular concern since so 10 many of our customers rely on electric heat to 11 heat their homes. 12 Newfoundland Power has the most 13 challenging customer demographics I've 14 encountered. Newfoundland and Labrador is the 15 only Canadian province in which population has 16 declined over the past two decades. It is 17 also the only Canadian province in which 18 population is forecast to decline over the 19 next two decades. And in addition, 20 Newfoundland and Labrador has one of the most 21 rapidly aging populations in Canada. The 22 movement of population from rural Newfoundland 23 to urban centres requires that we maintain 24 service in rural communities while at the same 25 time providing for growth elsewhere. We have</p>	<p>1 officer of Fortis Alberta that storm damage 2 exceeding \$100,000 was automatically deferred 3 for future recovery. By comparison, the 4 increased operating costs for Newfoundland 5 Power of approximately 1.8 million dollars 6 resulting from Hurricane Igor in 2010 were 7 never the subject of a deferral application. 8 But Newfoundland Power also has some 9 relative strengths, including its stronger 10 capital structure which contribute to it being 11 an average risk utility on an overall basis. 12 KELLY, Q.C.: 13 Q. Why is a cost of capital important for 14 Newfoundland Power's customers? 15 MR. LUDLOW: 16 A. Newfoundland Power is first and foremost a 17 service company. Our primary obligation is to 18 provide safe, reliable, least cost service to 19 our customers. Our ability to provide service 20 to our customers depends upon continued 21 investment in long-life utility assets. The 22 money or capital required to fund this 23 continuing investment is a key aspect of 24 Newfoundland Power's provision of safe, 25 reliable service to our customers.</p>

Page 33	Page 35
<p>1 The capital to fund this investment comes</p> <p>2 from debt and equity markets. The annual cost</p> <p>3 of that capital is a substantial component of</p> <p>4 the price our customers must pay for the</p> <p>5 service we provide. So cost of capital is</p> <p>6 important for Newfoundland Power's customers</p> <p>7 because it is fundamental to the reliability</p> <p>8 of the service they receive and the price they</p> <p>9 must pay for that service. The return on</p> <p>10 equity must be fair to Newfoundland Power and</p> <p>11 also to its customers.</p> <p>12 KELLY, Q.C.:</p> <p>13 Q. Why does fairness matter?</p> <p>14 MR. LUDLOW:</p> <p>15 A. Equity investors in a regulated utility expect</p> <p>16 a fair return. Equity investors commit</p> <p>17 capital to fund long-lived utility assets</p> <p>18 which typically are in service for decades.</p> <p>19 This capital is essentially captive. In my</p> <p>20 experience, there are relatively few</p> <p>21 differences among electric utility operations.</p> <p>22 For example, an electricity utility pole</p> <p>23 installed in British Columbia would not be</p> <p>24 materially different than one installed right</p> <p>25 here in Newfoundland and Labrador. Capital</p>	<p>1 reasonable return on equity, then management</p> <p>2 would be in the difficult position to having</p> <p>3 to consider reducing other costs. Reductions</p> <p>4 in costs might not have an immediate impact on</p> <p>5 service levels. However, the need to earn a</p> <p>6 fair return could eventually result in</p> <p>7 deterioration of the service provided by</p> <p>8 Newfoundland Power to its customers.</p> <p>9 KELLY, Q.C.:</p> <p>10 Q. Can you give us an example of that, of how the</p> <p>11 need to earn a fair return can have a long</p> <p>12 term impact on service?</p> <p>13 MR. LUDLOW:</p> <p>14 A. Yes, I can. In the early 1990s, following the</p> <p>15 fisheries moratorium, economic conditions</p> <p>16 resulted in Newfoundland Power cutting its</p> <p>17 annual capital investment by as much as half.</p> <p>18 This was done to ensure the continued</p> <p>19 financial integrity of Newfoundland Power in</p> <p>20 difficult economic conditions. These capital</p> <p>21 cost reductions did not have an immediate</p> <p>22 impact on the service received by our</p> <p>23 customers. However, the cost reductions did</p> <p>24 have longer term impacts on reliability of</p> <p>25 service. By 1998, a review of the company's</p>
Page 34	Page 36
<p>1 markets are not provincial. There isn't a</p> <p>2 Newfoundland and Labrador capital market and a</p> <p>3 British Columbia capital market.</p> <p>4 Now in this proceeding, we have filed the</p> <p>5 expert opinions of Ms. Kathleen McShane and</p> <p>6 Dr. James Vanderweide. These experts indicate</p> <p>7 that a fair return on equity for Newfoundland</p> <p>8 Power is in the order of 10.4 to 10.5 percent.</p> <p>9 KELLY, Q.C.:</p> <p>10 Q. What are the implications of not having a fair</p> <p>11 allowed return on equity?</p> <p>12 MR. LUDLOW:</p> <p>13 A. Newfoundland Power's management has an</p> <p>14 obligation to maintain the company's financial</p> <p>15 integrity. This is consistent with least cost</p> <p>16 delivery of safe, reliable service to our</p> <p>17 customers over the long term. Maintaining</p> <p>18 Newfoundland Power's financial integrity</p> <p>19 requires it to achieve a fair and reasonable</p> <p>20 return on common equity and equity investors</p> <p>21 expect to earn a fair return. So, as CEO, I</p> <p>22 have an obligation to both our customers and</p> <p>23 to our equity investors to try to achieve an</p> <p>24 appropriate return. If Newfoundland Power is</p> <p>25 not allowed the opportunity to earn a just and</p>	<p>1 quality of service and reliability of supply</p> <p>2 by the Board's engineering consultant</p> <p>3 indicated that it was important that the</p> <p>4 company seek to improve its reliability</p> <p>5 performance. So in the early 1990s,</p> <p>6 Newfoundland Power reduced its cost to ensure</p> <p>7 its financial integrity. This didn't impact</p> <p>8 service to customers immediately. However,</p> <p>9 within five years or so, these cost reductions</p> <p>10 had clearly impacted the service provided to</p> <p>11 the company's customers.</p> <p>12 KELLY, Q.C.:</p> <p>13 Q. Could that logic apply today?</p> <p>14 MR. LUDLOW:</p> <p>15 A. Yes, it could. Currently, Newfoundland Power</p> <p>16 has increased its recruitment of skilled and</p> <p>17 technical labour to address workforce</p> <p>18 demographics. These efforts, which are aimed</p> <p>19 at maintaining customer service levels over</p> <p>20 the long term, tend to increase the company's</p> <p>21 costs. If Newfoundland Power were to curtail</p> <p>22 these increased recruitment efforts to</p> <p>23 maintain the company's financial integrity in</p> <p>24 the short term, there may not be an immediate</p> <p>25 impact on the service received by our</p>

Page 37	Page 39
<p>1 customers. However, such cost reductions</p> <p>2 could certainly have negative impacts on the</p> <p>3 service received by our customers in the</p> <p>4 future. The point here is a simple one.</p> <p>5 Newfoundland Power's operations are focused on</p> <p>6 long term, sustainable improvement in service</p> <p>7 to customers while earning a reasonable</p> <p>8 return. It's a balance and establishing rate</p> <p>9 making returns that are too low can affect</p> <p>10 that balance.</p> <p>11 KELLY, Q.C.:</p> <p>12 Q. Does Newfoundland Power believe that those</p> <p>13 kind of steps would be necessary?</p> <p>14 MR. LUDLOW:</p> <p>15 A. No, we do not. The Public Utilities Act</p> <p>16 provides that Newfoundland Power is entitled</p> <p>17 to the opportunity to earn a just and</p> <p>18 reasonable return each year in addition to its</p> <p>19 reasonable costs. This entitlement reflects</p> <p>20 the essential balance between the competing</p> <p>21 interests of utility investors and customers.</p> <p>22 In Newfoundland Power's view, the balance of</p> <p>23 these competing interests should not include</p> <p>24 placing the management of Newfoundland Power</p> <p>25 in a position where it has to choose between</p>	<p>1 have any confidence that anyone has proposed a</p> <p>2 better formula that will give reliable and</p> <p>3 reasonable results in current market</p> <p>4 conditions. Ms. Perry will address that point</p> <p>5 as we follow through in different parts of</p> <p>6 this proceeding. From my perspective, the</p> <p>7 better approach is to leave the question of a</p> <p>8 formula for another day. There is currently</p> <p>9 no consensus among regulators as to whether a</p> <p>10 formula should be used. The Board can revisit</p> <p>11 this issue at a future time when financial</p> <p>12 market conditions return to normal and a</p> <p>13 regulatory consensus emerges.</p> <p>14 KELLY, Q.C.:</p> <p>15 Q. Mr. Ludlow, the next issue I want to turn to</p> <p>16 is depreciation. The Consumer Advocate has</p> <p>17 raised some issues concerning depreciation in</p> <p>18 this proceeding. Can you give us your views</p> <p>19 on depreciation?</p> <p>20 MR. LUDLOW:</p> <p>21 A. I view this discussion very simply. If you</p> <p>22 reduce depreciation, the rate base grows. The</p> <p>23 return on rate base is a cost to our customer.</p> <p>24 Increasing the rate base adds to our</p> <p>25 customers' costs over the long term. Yes, you</p>
Page 38	Page 40
<p>1 reducing either its service levels or its</p> <p>2 financial integrity. Either choice would be</p> <p>3 inconsistent with the power policy of this</p> <p>4 province.</p> <p>5 KELLY, Q.C.:</p> <p>6 Q. Mr. Ludlow, Newfoundland Power, in this</p> <p>7 proceeding, has again proposed discontinuing</p> <p>8 the use of the automatic adjustment formula.</p> <p>9 Why has the company adopted that position?</p> <p>10 MR. LUDLOW:</p> <p>11 A. The purpose of the formula was to reduce</p> <p>12 hearings, increase regulatory efficiency and</p> <p>13 reduce costs. It largely fulfilled that</p> <p>14 function until 2008. Since then, it has not.</p> <p>15 Everyone seems to agree that since 2008,</p> <p>16 capital markets have not been normal and</p> <p>17 everyone seems to agree that they're still not</p> <p>18 normal today in 2013. Since the last hearing,</p> <p>19 the formula has added to the regulatory</p> <p>20 complexity, not lessened it. In 2012, the</p> <p>21 company had to go through a regulatory process</p> <p>22 because the formula did not yield a reasonable</p> <p>23 result. For a small utility like Newfoundland</p> <p>24 Power, these processes take time away from the</p> <p>25 critical job of running the company. I don't</p>	<p>1 can get a short term reduction today by</p> <p>2 reducing depreciation, but it comes at the</p> <p>3 price of higher rates tomorrow and on into the</p> <p>4 future. So I do not believe these changes are</p> <p>5 in our customers' best interest. The Board</p> <p>6 examined this issue many years ago and adopted</p> <p>7 the current ELG depreciation methodology.</p> <p>8 From everything I've seen, that seems to be</p> <p>9 the best approach. It best matches the</p> <p>10 expenses with the life of the asset. Our rate</p> <p>11 base would be significant higher if we had</p> <p>12 stayed on the ALG methodology and our</p> <p>13 customers would be paying approximately 3.7</p> <p>14 million dollars in higher electricity rates</p> <p>15 today. So I think it's very clear that the</p> <p>16 Board made the right decision in adopting ELG.</p> <p>17 I see no reason to depart from a policy that</p> <p>18 has proven to be in the long term interest of</p> <p>19 our customers.</p> <p>20 KELLY, Q.C.:</p> <p>21 Q. Mr. Ludlow, does that conclude your testimony?</p> <p>22 MR. LUDLOW:</p> <p>23 A. Yes, it does.</p> <p>24 KELLY, Q.C.:</p> <p>25 Q. Thank you, Mr. Chairman.</p>

Page 41

Page 43

1 CHAIRMAN:
 2 Q. Mr. Johnson.
 3 (10:30 a.m.)
 4 MR. EARL LUDLOW, CROSS-EXAMINATION BY MR. THOMAS JOHNSON
 5 MR. JOHNSON:
 6 Q. Good morning, Mr. Ludlow, again.
 7 MR. LUDLOW:
 8 A. Good morning.
 9 MR. JOHNSON:
 10 Q. You talked in your direct with Mr. Kelly about
 11 Newfoundland Power's returns over the last few
 12 years since the rate case, but I take it that
 13 you would confirm, Mr. Ludlow, would you not,
 14 that Newfoundland Power itself believes that
 15 its financial performance since the last
 16 general rate application through to 2012 has
 17 been absolutely consistent with the company's
 18 financial integrity, correct?
 19 MR. LUDLOW:
 20 A. I would agree, Mr. Chairman, that we have
 21 performed very well in the past two or three
 22 years and it has not had any negative impact
 23 on the financial integrity of the company.
 24 MR. JOHNSON:
 25 Q. And 2012 similarly, 2012 was a good year for

1 Newfoundland Power's financial integrity.
 2 Now, let us examine for a moment how much
 3 profit Newfoundland Power wishes to make from
 4 its customers in 2013 and 2014 by turning to
 5 Exhibit 6, line 25 in the 2013 proposed
 6 column. So you're proposing, are you not,
 7 that in 2013 that net income will go to 42.5
 8 million dollars and in 2014, under the
 9 proposed column, go to 44 million dollars in
 10 2014? That's correct, right?
 11 MR. LUDLOW:
 12 A. Those are the correct numbers according to the
 13 schedule, yes.
 14 MR. JOHNSON:
 15 Q. And then, as per line 32, that would be
 16 reflective of this Board allowing you a rate
 17 increase sufficient for Newfoundland Power to
 18 make a 10.4 percent return on its regulated
 19 equity, correct?
 20 MR. LUDLOW:
 21 A. That is correct.
 22 MR. JOHNSON:
 23 Q. And just to put the return on regulated -- the
 24 regulated return on common equity into some
 25 sort of perspective, could I ask you to turn

Page 42

Page 44

1 Newfoundland Power in terms of its results?
 2 MR. LUDLOW:
 3 A. Well, the books aren't closed on that one yet,
 4 Mr. Chairman.
 5 MR. JOHNSON:
 6 Q. In terms of what you're predicting or
 7 estimating, you're estimating, as I understand
 8 it from Exhibit 3, which is in your Volume 2,
 9 and referring to line 28, Mr. Ludlow, that you
 10 are forecasting -- and this has not been
 11 changed -- forecasting net income of north of
 12 36 and a half million dollars for 2012.
 13 That's correct, right?
 14 MR. LUDLOW:
 15 A. That's correct. That's our forecast.
 16 MR. JOHNSON:
 17 Q. Okay. And in line 35, you're forecasting
 18 making a regulated return on book equity of
 19 8.81 percent for 2012?
 20 MR. LUDLOW:
 21 A. That's our forecast, yes, that's correct.
 22 MR. JOHNSON:
 23 Q. And as you admitted, that financial
 24 performance, just like all the other years
 25 since your last GRA, would be consistent with

1 up the CA-NP-401?
 2 MR. LUDLOW:
 3 A. Just bear with me now. I'm going to use the
 4 paper, if you don't mind. 401?
 5 MR. JOHNSON:
 6 Q. Yes, sir. And I'm looking in particular at
 7 Table 2, Mr. Ludlow.
 8 MR. LUDLOW:
 9 A. Yes.
 10 MR. JOHNSON:
 11 Q. Which shows -- which focuses on the period
 12 over 2011 to 2012 forecast and then forecast
 13 for 2013 and 2014, right, and as between the
 14 difference between 2012 forecast and 2013
 15 forecast, you're looking for a return in
 16 millions of dollars, an incremental return of
 17 8.4 million dollars, right?
 18 MR. LUDLOW:
 19 A. That is according to Table 2, yes, that's
 20 correct.
 21 MR. JOHNSON:
 22 Q. And by percentage wise, that is what
 23 percentage greater than 2012 for 2013?
 24 MR. LUDLOW:
 25 A. According to the table, the third line?

Page 45	Page 47
<p>1 MR. JOHNSON:</p> <p>2 Q. Yes.</p> <p>3 MR. LUDLOW:</p> <p>4 A. Show 24.1 percent.</p> <p>5 MR. JOHNSON:</p> <p>6 Q. Greater than 2012?</p> <p>7 MR. LUDLOW:</p> <p>8 A. That's correct.</p> <p>9 MR. JOHNSON:</p> <p>10 Q. And just to be clear, 2011 when the company</p> <p>11 made -- just made slightly more than what you</p> <p>12 are projected to make in 2012, that was a fair</p> <p>13 return in 2011 and preserved the financial</p> <p>14 integrity of the company?</p> <p>15 MR. LUDLOW:</p> <p>16 A. 2011?</p> <p>17 MR. JOHNSON:</p> <p>18 Q. Yes.</p> <p>19 MR. LUDLOW:</p> <p>20 A. Our return, as stated, as I said earlier, was</p> <p>21 whatever I -- what we were saying earlier, it</p> <p>22 was reasonable at that point in time, yes.</p> <p>23 MR. JOHNSON:</p> <p>24 Q. Okay. And in 2014, you want more onto the --</p> <p>25 in addition to, relative to 2013 forecast, you</p>	<p>1 Johnson.</p> <p>2 MR. JOHNSON:</p> <p>3 Q. And in fact, that 10.4 percent return, Mr.</p> <p>4 Ludlow, that would, would it not, put</p> <p>5 Newfoundland Power amongst the very highest in</p> <p>6 Canada in terms of its allowed return on</p> <p>7 equity, correct?</p> <p>8 MR. LUDLOW:</p> <p>9 A. As I've looked at the Canadian utilities, I</p> <p>10 think the range now would go to about 9.9</p> <p>11 percent as to the highest in British Columbia,</p> <p>12 that is correct.</p> <p>13 MR. JOHNSON:</p> <p>14 Q. And that would be the highest that's known to</p> <p>15 you, but others are getting 8.7 -- other</p> <p>16 Fortis companies, I believe, are getting even</p> <p>17 lower than 8.7, are they not?</p> <p>18 MR. LUDLOW:</p> <p>19 A. Other companies are getting lower than 9, but</p> <p>20 at the same point, all companies are based on</p> <p>21 different characteristics of operating,</p> <p>22 business, regulatory and as well financial</p> <p>23 risk characteristics. What we have done on</p> <p>24 that point is again, we've engaged the expert</p> <p>25 witnesses of McShane and VanderWeide where</p>
Page 46	Page 48
<p>1 want another 1.6 million dollars through 2014</p> <p>2 to bring you up to about 45 million in net</p> <p>3 income or the regular return on common equity.</p> <p>4 Is that correct?</p> <p>5 MR. LUDLOW:</p> <p>6 A. According to the table, that is correct. Mr.</p> <p>7 Chairman, what I would say as well, is that -</p> <p>8 MR. JOHNSON:</p> <p>9 Q. That table, was that -</p> <p>10 MR. LUDLOW:</p> <p>11 A. Just as I said earlier, according to the table</p> <p>12 and what's been promoted, that is correct.</p> <p>13 The earnings that we have had during the past</p> <p>14 number of years, questionable whether we met</p> <p>15 them. It dealt with a lot of management and</p> <p>16 cost management within the business to perform</p> <p>17 and execute. As I said in my opening</p> <p>18 statement, this takes -- there's only so much</p> <p>19 room within the utility to work and that</p> <p>20 allowed return is key to giving us opportunity</p> <p>21 to work within that band to earn a reasonable</p> <p>22 return and what we have done here is we've</p> <p>23 promoted and come forward with cost of capital</p> <p>24 experts who are recommending a 10.4 percent</p> <p>25 and that's basically where we are, Mr.</p>	<p>1 their expert testimony which you will hear</p> <p>2 hopefully next week, if we can get past this</p> <p>3 weekend, and that was the basis upon which we</p> <p>4 have engaged those experts.</p> <p>5 MR. JOHNSON:</p> <p>6 Q. So, just for the record, I know that's what</p> <p>7 Ms. McShane and Dr. VanderWeide have put</p> <p>8 forward which would put you at the highest,</p> <p>9 but is it your contention as the president and</p> <p>10 CEO of Newfoundland Power that you really need</p> <p>11 to be at the highest? I mean, do you</p> <p>12 personally believe that as president of the</p> <p>13 company?</p> <p>14 MR. LUDLOW:</p> <p>15 A. Mr. Chairman, I look at a lot of factors when</p> <p>16 we put a rate case together. We look at where</p> <p>17 we're going. We look at a whole bunch of</p> <p>18 factors, and as I said earlier, striking that</p> <p>19 balance is a key one to hit. So, I'm not a</p> <p>20 cost of capital expert, that I can assure you.</p> <p>21 So, we go out, we find the best we can find</p> <p>22 and we put those numbers together and we look</p> <p>23 at it and instead of me turning around and</p> <p>24 casting my wand over it, I don't like this or</p> <p>25 I don't like that, there's parts I do and</p>

Page 49	Page 51
<p>1 there's parts I don't, we have accepted the</p> <p>2 expert testimony of McShane and VanderWeide</p> <p>3 and that's what we filed and that's what they</p> <p>4 will present here next week, and I'm sure</p> <p>5 that's what the debate will continue on.</p> <p>6 There's parts of this case I like and parts I</p> <p>7 don't like as well.</p> <p>8 MR. JOHNSON:</p> <p>9 Q. Pardon me?</p> <p>10 MR. LUDLOW:</p> <p>11 A. That's correct.</p> <p>12 MR. JOHNSON:</p> <p>13 Q. I didn't hear the last part. There's parts</p> <p>14 you -</p> <p>15 MR. LUDLOW:</p> <p>16 A. My point was, as we put this case together,</p> <p>17 there's a lot of debate in the case around</p> <p>18 operating expense and where we're moving and</p> <p>19 you know, when I look at this, I rely totally</p> <p>20 on my experts as I come forward with this</p> <p>21 number.</p> <p>22 MR. JOHNSON:</p> <p>23 Q. Did it surprise you at all that these two</p> <p>24 people that Newfoundland Power hired happen to</p> <p>25 pitch on the same number which would be well</p>	<p>1 Q. Mr. Johnson, we need to enter that onto the</p> <p>2 record.</p> <p>3 MR. JOHNSON:</p> <p>4 Q. Oh, I'm sorry.</p> <p>5 MS. GLYNN:</p> <p>6 Q. That's fine. So we'll enter that as</p> <p>7 Information Item No. 1, please.</p> <p>8 MR. JOHNSON:</p> <p>9 Q. Thank you. You're familiar with this</p> <p>10 document, Mr. Ludlow?</p> <p>11 MR. LUDLOW:</p> <p>12 A. Yes, I am.</p> <p>13 MR. JOHNSON:</p> <p>14 Q. Okay. What was the purpose of this document?</p> <p>15 MR. LUDLOW:</p> <p>16 A. It's a media release that we issue to all</p> <p>17 media outlets in Newfoundland and Labrador</p> <p>18 announcing that we are filing or have filed a</p> <p>19 2013 general rate application effective</p> <p>20 September the 4th as we were ordered to do by</p> <p>21 this Board, and it would lay out the various</p> <p>22 components of that.</p> <p>23 MR. JOHNSON:</p> <p>24 Q. And one thing that strikes me about your media</p> <p>25 release is that it -- you know, it talks to</p>
Page 50	Page 52
<p>1 in excess of what the highest utility in the</p> <p>2 country is getting?</p> <p>3 MR. LUDLOW:</p> <p>4 A. No, not really. I think it's a matter of</p> <p>5 consistency. How an expert looks at</p> <p>6 something, I would be greatly concerned if</p> <p>7 they were multiple basis points apart. That's</p> <p>8 the way I'd look at experts. I look for</p> <p>9 consistency in where they're going.</p> <p>10 MR. JOHNSON:</p> <p>11 Q. I think as you acknowledged in your opening</p> <p>12 that the key issue in this case is the cost of</p> <p>13 equity issue and in the letter which</p> <p>14 accompanied your application to the Board, it</p> <p>15 was described as a central issue of the</p> <p>16 application, you'd agree with that, and</p> <p>17 yesterday I sent to you two documents and</p> <p>18 you'll recall that I did the same thing last</p> <p>19 time. I sent you your company's media release</p> <p>20 and I sent you, as well, the Power Connection</p> <p>21 document that you sent to customers in the</p> <p>22 month following the filing of the general rate</p> <p>23 application and if we could bring up the media</p> <p>24 release first.</p> <p>25 MS. GLYNN:</p>	<p>1 commitment of investing in rural areas. It</p> <p>2 talks to energy supply costs. It talks to the</p> <p>3 amount of money that's been invested over the</p> <p>4 past five years of 350 million, and you</p> <p>5 indicate "establishing a fair and reasonable</p> <p>6 future return on investment is another</p> <p>7 component of the rate increase." That's</p> <p>8 what's said in the release. So that's the</p> <p>9 sentence, is it, that is supposed to tell the</p> <p>10 media and customers what the central issue is</p> <p>11 to cost of equity? Is that where they're</p> <p>12 supposed to get this information from, that</p> <p>13 sentence?</p> <p>14 MR. LUDLOW:</p> <p>15 A. This media release panel was issued on the</p> <p>16 14th to give the general public an overview of</p> <p>17 what had transpired when we filed a general</p> <p>18 rate application and as you read this</p> <p>19 application or this media release, it will</p> <p>20 show you the three key parts that are driven,</p> <p>21 and actually there's a fourth part that's</p> <p>22 highlighted very, very clearly here well about</p> <p>23 the additional increase to residential</p> <p>24 customers of this province. So it was brought</p> <p>25 down into the various areas of supply, return</p>

Page 53	Page 55
<p>1 and also the other operating costs. Those</p> <p>2 that wish to have additional detail down to</p> <p>3 the decimal point or the levels, and I'm not</p> <p>4 demeaning your point there, there's a direct</p> <p>5 link for the full application on our website</p> <p>6 which is still there, still live.</p> <p>7 MR. JOHNSON:</p> <p>8 Q. Would you not at least concede that the --</p> <p>9 there's no mention obviously of what the</p> <p>10 return on equity is and there's certainly no</p> <p>11 mention that it's going to put you at the</p> <p>12 highest in the country, correct?</p> <p>13 MR. LUDLOW:</p> <p>14 A. There is no mention of the number, but there</p> <p>15 is a mention here about establishing a fair</p> <p>16 and reasonable return, which is the central</p> <p>17 case or one of the key points of this hearing,</p> <p>18 one of the three.</p> <p>19 MR. JOHNSON:</p> <p>20 Q. Did you make it any clearer in your Power</p> <p>21 Connection? So maybe we could turn to the</p> <p>22 next document.</p> <p>23 MS. GLYNN:</p> <p>24 Q. And that would be entered as Information Item</p> <p>25 No. 2.</p>	<p>1 talking about, which is similar to the media</p> <p>2 release.</p> <p>3 MR. JOHNSON:</p> <p>4 Q. Okay. So essentially, the customer who you</p> <p>5 communicated with in October is not really</p> <p>6 told anything different than what you sent out</p> <p>7 to the media previously in relation to what</p> <p>8 the central issue is in the case?</p> <p>9 MR. LUDLOW:</p> <p>10 A. Mr. Chairman, I'm going to take a little bit</p> <p>11 of different tact here than the Consumer</p> <p>12 Advocate is putting forward because as I look</p> <p>13 at that, I would agree to the fact that the</p> <p>14 actual number is not included into the Power</p> <p>15 Connection or into the media release.</p> <p>16 However, what we did decide, and there's a lot</p> <p>17 of thought goes into this, our customers are</p> <p>18 interested in price, rate increases. Do we go</p> <p>19 with the average or do we directly point out</p> <p>20 what are the impacts on the different rate</p> <p>21 classes? And that's what we sent to our</p> <p>22 customers here. We laid out the various</p> <p>23 proposals in the case. They will be argued</p> <p>24 and that's what we're here for today. But we</p> <p>25 felt that it was essential that we put out the</p>
Page 54	Page 56
<p>1 (10:45 a.m.)</p> <p>2 MR. JOHNSON:</p> <p>3 Q. And this is a document dated October 2012 that</p> <p>4 was sent out to all your customers.</p> <p>5 MR. LUDLOW:</p> <p>6 A. Correct. This is an attachment, both</p> <p>7 electronically and paper, that we would have</p> <p>8 sent to all 250,000 customers.</p> <p>9 MR. JOHNSON:</p> <p>10 Q. And you'll confirm for me that there is no</p> <p>11 direct mention here at all to your customers</p> <p>12 of what your proposal is for the return for</p> <p>13 the company or the company's profit, right?</p> <p>14 MR. LUDLOW:</p> <p>15 A. I'm missing your point. Are you asking me if</p> <p>16 10.4 is in here?</p> <p>17 MR. JOHNSON:</p> <p>18 Q. I'm asking you -- well, I'm asking you that</p> <p>19 question. It's not in there, is it?</p> <p>20 MR. LUDLOW:</p> <p>21 A. What's not in here?</p> <p>22 MR. JOHNSON:</p> <p>23 Q. Well, the 10.4.</p> <p>24 MR. LUDLOW:</p> <p>25 A. Fair and reasonable return is what we're</p>	<p>1 impact that the bottom line on the bill of our</p> <p>2 customers will be highly clarified for them</p> <p>3 and that's what we put out here.</p> <p>4 MR. JOHNSON:</p> <p>5 Q. I'm not quibbling with the fact that you put</p> <p>6 the bottom line in there in terms of the</p> <p>7 customer impact. What I'm quibbling with is</p> <p>8 why in the world -- why in your covering</p> <p>9 letter to the Board, you say cost of equity is</p> <p>10 a central issue, but you don't say it to</p> <p>11 customers and you don't say it to the media?</p> <p>12 That's the simple question I have for you.</p> <p>13 MR. LUDLOW:</p> <p>14 A. But we have said just that, cost of equity and</p> <p>15 a fair return is a point of this and a central</p> <p>16 point of this hearing.</p> <p>17 MR. JOHNSON:</p> <p>18 Q. Now you made reference to the weather</p> <p>19 conditions of Newfoundland and Labrador and</p> <p>20 just to be clear, I understand that the events</p> <p>21 of 2010, when we had the storm -- there was</p> <p>22 two storms, was it not? There was an ice</p> <p>23 storm and then there was Igor?</p> <p>24 MR. LUDLOW:</p> <p>25 A. Correct. There was a March ice storm that</p>

Page 57

Page 59

1 impacted the Bonavista and probably the
 2 Bonavista North and as well down through
 3 Grate's Cove area and then September 21st,
 4 Hurricane Igor decided to bless us with its
 5 appearance.
 6 MR. JOHNSON:
 7 Q. Right, indeed. And the ice storm that we're
 8 talking about, that was the worst storm in 25
 9 years, I take it. I think that's what your
 10 materials disclosed.
 11 MR. LUDLOW:
 12 A. The ice storm?
 13 MR. JOHNSON:
 14 Q. Yes.
 15 MR. LUDLOW:
 16 A. It may be. Every ice storm -- I just -- I
 17 don't know where that reference is. If you
 18 can show me, I'd appreciate it.
 19 MR. JOHNSON:
 20 Q. Okay. Maybe I'll come back to it.
 21 MR. LUDLOW:
 22 A. It was a bad ice storm.
 23 MR. JOHNSON:
 24 Q. Indeed. But in any event, it didn't keep
 25 Newfoundland Power from earning its allowed

1 that, by the way, Mr. Smith will be more than
 2 happy to take you through. As we went through
 3 Igor, as I said in my chief, we were looking
 4 at a five-day period from Tuesday to Saturday
 5 and just that area alone cost an additional, I
 6 would suggest in the range of 1.8 million
 7 operating dollars.

8 So, we're now at September. What have we
 9 got left? We're running in this year, sales
 10 were in decent shape. We've also got four
 11 months to readjust and manage and bring in
 12 this company at a reasonable financial
 13 condition. So what we decided to do is rather
 14 than come before this Board for a deferral, we
 15 said: look, we're in such condition, we can
 16 try it. It means that some work will not get
 17 done because of sheer resource limitations,
 18 both capital and operating. Can we push, can
 19 we push for three or four months? So that's
 20 what we did and we pushed them over into
 21 another year. We took the 1.8 and basically
 22 took it on rather than coming before this
 23 Board. And that's the basis. It's a
 24 combination of good luck, good management --
 25 and by the way, I'd put the management of that

Page 58

Page 60

1 return, did it?
 2 MR. LUDLOW:
 3 A. Are you referring to the ice storm or both
 4 storms or the year?
 5 MR. JOHNSON:
 6 Q. Both storms. Let's say the ice storm and
 7 Igor.
 8 MR. LUDLOW:
 9 A. Okay. Take us back to 2010 for a minute.
 10 March ice storm, an ice storm by its very
 11 nature -- and again, I'm hoping this is not
 12 what's going to happen this weekend, but we'll
 13 see what happens. An ice storm by its nature
 14 has a tendency to be capital intensive, broken
 15 poles, that type of damage, whereas in a
 16 hurricane and a wind storm, combined with rain
 17 that hit with Igor -- and Igor by far was one
 18 of the worst storms we've had in multiple
 19 decades -- has a tendency to more drive
 20 towards the operating conditions of the
 21 company, trees, vegetation, response, those
 22 types of things, downed wires. So March,
 23 there was a subsequent capital adjustment made
 24 and there was some operating conditions or
 25 operating funds off that. The details of

1 storm against anyone. We were there before
 2 the military showed up, I might add, Mr.
 3 Chairman, and we were complete the day they
 4 showed up. That's what we're here for, is to
 5 keep those lights running. By the time we got
 6 past that Saturday, we then started to kick in
 7 gear and say: how do we do this without
 8 additional cost onto the customer? That's how
 9 we managed it. That's how we got through
 10 2010.

11 MR. JOHNSON:

12 Q. And so to answer my question, you made your
 13 allowed return in 2010?

14 MR. LUDLOW:

15 A. We did so.

16 MR. JOHNSON:

17 Q. Notwithstanding an event that happened late in
 18 2010 that you didn't plan for?

19 MR. LUDLOW:

20 A. It happened in September. Had that been in
 21 December, it would be a different story.

22 MR. JOHNSON:

23 Q. But you don't expect tropical storms in
 24 December, which are more operating intensive,
 25 I guess.

Page 61

Page 63

1 MR. LUDLOW:

2 A. Mr. Chair, the way the weather conditions here
3 are changing and continue to change, I don't
4 know what to expect any more, and you know,
5 like today, this has a tendency, this could
6 blow up into ice, wind, snow. I can handle
7 wind. I can handle snow. I just can't handle
8 ice and wind and that's the difference that
9 happens. September is a key in Igor. Time to
10 react.

11 MR. JOHNSON:

12 Q. And I guess, you know, the tropical storms,
13 they happen up and down the Eastern Seaboard.
14 They hit Nova Scotia. They hit PEI. They hit
15 a lot of different places, those tropical
16 storms, don't they?

17 MR. LUDLOW:

18 A. We've had ten. In 2010 we had one. We had
19 Hurricane Earl by the way. I don't take much
20 pleasure in that one, I might add, Mr.
21 Chairman, but it blew up and blew up through
22 the west coast of Newfoundland. We had
23 another one came in on the same day and time
24 and fizzled out in Trepassey. So its becoming
25 a regular occurrence these days.

Page 62

1 MR. JOHNSON:

2 Q. I hope Earl doesn't fizzle out.

3 CHAIRMAN:

4 Q. You mean more hurricanes are becoming a
5 regular -

6 MR. LUDLOW:

7 A. Seems to be moving that way. In the last five
8 years, we've had substantive weather patterns,
9 particularly in September.

10 MR. JOHNSON:

11 Q. But they're not unique to Newfoundland?

12 MR. LUDLOW:

13 A. I agree with you.

14 MR. JOHNSON:

15 Q. Right.

16 CHAIRMAN:

17 Q. But evidence worldwide, that's not the case.
18 I'm not going to argue here with you guys, but
19 -

20 MR. LUDLOW:

21 A. Certainly it seems to be what's happening in
22 this area, but I would agree it is not unique
23 to Newfoundland.

24 CHAIRMAN:

25 Q. The hurricane intensification in the United

1 States is there's been no change over the past
2 80 years.

3 MR. LUDLOW:

4 A. I can't quite go back that far, Mr. Chairman,
5 but I can go back 35 and I've seen more
6 hurricanes in the last ten than I did in the
7 previous 20.

8 CHAIRMAN:

9 Q. I'll send you an e-mail.

10 MR. JOHNSON:

11 Q. I just want to move off and perhaps we'll
12 revisit some other areas after the break, but
13 just to start a new theme for a moment. I
14 want to bring you to CA-NP-440.

15 MR. LUDLOW:

16 A. Yes.

17 MR. JOHNSON:

18 Q. And I raise this in connection with the
19 incentive targets. This obviously shows the
20 2012 salary policy and incentive targets for
21 the executives and managers, right?

22 MR. LUDLOW:

23 A. That is correct.

24 MR. JOHNSON:

25 Q. Okay. And in addition to the base salaries

Page 64

1 that we're seeing there for yourself and
2 executives and managers, there's obviously a
3 column there that allows incentive pay on top
4 of that. So in your case, it would be 50
5 percent of your base salary of 400 and so you
6 could get another 200 by incentive pay,
7 correct?

8 MR. LUDLOW:

9 A. Not 100 percent correct. Basically, the
10 incentive target is 50 percent. There is a
11 band around that that that could increase
12 above the 50 percent, but there's only 50
13 percent in rates to the customer.

14 MR. JOHNSON:

15 Q. Okay. Now these incentive target amounts for
16 executives and managers, these require, do
17 they not, the meeting of both individual
18 targets as well as corporate targets, right?

19 MR. LUDLOW:

20 A. That is correct.

21 MR. JOHNSON:

22 Q. Okay. So not only does the company have to
23 perform, but the individual executives have to
24 achieve a certain performance as well. Now,
25 by my calculation, and you can take this

Page 65

Page 67

1 subject to check, I know you don't have a
 2 calculator and I don't want you to do that,
 3 but by my calculation, just to know what we're
 4 talking about, if 100 percent of the corporate
 5 and individual targets are met, then a total
 6 of \$474,000 in incentive target payments will
 7 be paid to the executive members in 2012. Do
 8 you accept that, for argument purposes? And
 9 if I'm wrong that can be corrected on the
 10 record.
 11 MR. LUDLOW:
 12 A. I have no idea where your calculation -- show
 13 me how -- tell me how you're doing your
 14 calculation and I'll agree with your
 15 methodology.
 16 MR. JOHNSON:
 17 Q. I'm taking the base salaries and then I'm
 18 taking the incentive target percentages in the
 19 right-hand column and then I'm adding those up
 20 to come to about 474.
 21 MR. LUDLOW:
 22 A. I'll agree with the methodology.
 23 MR. JOHNSON:
 24 Q. And similar methodology is applied when I look
 25 at the managers and as a group, again subject

1 payouts to the president, the vice-presidents
 2 and the managers, we know that more than 100
 3 percent target is met, correct?
 4 MR. LUDLOW:
 5 A. Correct.
 6 MR. JOHNSON:
 7 Q. Okay. Now and we are in agreement that in
 8 forecast years 2013 and 2014 that it's
 9 reasonable to expect that at least 100 percent
 10 of the targets will be achieved and in fact,
 11 your GRA filing is premised on 100 percent
 12 being met for the company and the executives
 13 and managers. Is that correct?
 14 MR. LUDLOW:
 15 A. That's correct.
 16 (10:45 a.m.)
 17 MR. JOHNSON:
 18 Q. In terms of the revenue requirement?
 19 MR. LUDLOW:
 20 A. Okay.
 21 MR. JOHNSON:
 22 Q. And we know, we alluded to the fact that
 23 anything over 100 percent, that's non-
 24 regulated and the Board has said anything over
 25 100, that's non-regulated. We understand that

Page 66

Page 68

1 to check, when I do that, I come to \$200,970.
 2 Now if we look for a moment at 449, what we
 3 have here is a table from 2004 to 2011 which
 4 sets out the non-regulated STI payouts. Now
 5 the non-regulated, so that would mean if you -
 6 - if the company and the executives went above
 7 target, the shareholder picks up those costs
 8 and pays it, not the rate holder -- not the
 9 rate payer, right?
 10 MR. LUDLOW:
 11 A. Correct.
 12 MR. JOHNSON:
 13 Q. Okay. And if we look at that period, I guess
 14 we can deduce that over that period, the
 15 president, yourself -- well, and your
 16 predecessor, and at least some of the vice-
 17 presidents and at least some of the managers
 18 obtained STI payments in excess of 100 percent
 19 that the customer pays for, right?
 20 MR. LUDLOW:
 21 A. Make sure I've got your point. Would you
 22 repeat it, please?
 23 MR. JOHNSON:
 24 Q. Sure. By merit of the fact that we know that
 25 over those years there were non-regulated

1 from P.U. 19, right, (2003).
 2 MR. LUDLOW:
 3 A. Yes.
 4 MR. JOHNSON:
 5 Q. Not necessarily -- okay. Now if I could just
 6 go to the corporate targets for a moment by
 7 bringing you back to 443, Mr. Ludlow, and in
 8 particular, page three of four. And I just
 9 want to look at Table -- Table 5 has to do
 10 with the corporate targets for 2012, okay. So
 11 we see the category of reliability and there
 12 is a specific measure that's required to be
 13 met for SAIDI at 2.58 and that's given a 15
 14 percent weighting and we see customer
 15 satisfaction which has two measures, being
 16 percentage of customer satisfied first call
 17 resolution, that's given a weighting of 7. 5
 18 percent each, and then we have safety, the all
 19 injury frequency rate which again we have to
 20 meet 1.56 incidents for number and it's 15
 21 percent weighting, and then financial as a
 22 total is controllable operating cost per
 23 customer which is given a 20 percent weight
 24 and then earnings which is given a 35 percent
 25 weight. So out of the corporate targets for

Page 69	Page 71
<p>1 2012, the earnings get the biggest weight, 2 right? 3 MR. LUDLOW: 4 A. The earnings receives 35. Financial receive 5 55. That point I would agree. 6 MR. JOHNSON: 7 Q. Yes, the 55 includes the 20 for controllable 8 operating. 9 MR. LUDLOW: 10 A. Financial. 11 MR. JOHNSON: 12 Q. Understand, okay. And that's pretty much in 13 line with how the targets have operated over 14 the last number of years? 15 MR. LUDLOW: 16 A. Pretty much, yes. 17 MR. JOHNSON: 18 Q. Yeah, okay. So then so assuming that these 19 corporate targets are met, I'd like to look at 20 the individual targets of the executive 21 members and managers. So if we could go to 22 the personal targets at 451? And in 23 particular, we see at Table 1, this is the 24 target percentage payouts, we see for the 25 president and CEO, the previous target was 40</p>	<p>1 is I'm running a fairly tight ship right now 2 with three vice-presidents, down from numbers 3 that were much higher in the past. So, I 4 decided upon looking at incumbents, 5 contribution and impact, to take a 6 recommendation to the governance committee of 7 reducing the personal component or the 8 corporate component and raising the individual 9 and bringing it on a 50/50 split for the vice- 10 presidents and it was just a slight adjustment 11 of five percent on mine from 75 to 70, 75/25 12 to 70/30. And it was based upon where we are, 13 the basis of our operation, and the 14 contributions that three versus I guess at one 15 point in the past could be as high as six or 16 seven executive members. So it was a personal 17 thing, my professional judgment, that I 18 decided to take that forward on that basis, 19 Mr. Chairman. 20 MR. JOHNSON: 21 Q. Okay. And just - 22 MR. LUDLOW: 23 A. Would you like me to explain the top one? 24 MR. JOHNSON: 25 Q. Sure.</p>
Page 70	Page 72
<p>1 percent while the current target is 50 and 2 everybody has gone up from the previous target 3 to the current target. So we understand that. 4 And in Table 2, we see that for the president 5 and CEO, your corporate weighting was 75 6 percent and your individual was 25 and that 7 has had a slight change too. Can you explain 8 why that change took place? 9 MR. LUDLOW: 10 A. Okay. Are you asking me to explain both 11 changes or the second change? 12 MR. JOHNSON: 13 Q. The second change. 14 MR. LUDLOW: 15 A. Okay. Second change from the split between 16 corporate and personal, it was done as a 17 result -- let me explain the way it would 18 operate, first of all. For any change to be 19 made to this STI program, it's through our 20 Board of Directors upon recommendation from 21 our governance and HR committee. That would 22 go -- this one in particular would be a 23 recommendation from me to the Board, to the 24 Committee, and if they're in agreement, they 25 would take it forward. The way I look at this</p>	<p>1 MR. LUDLOW: 2 A. I shouldn't be doing this, but I did it 3 anyway. The top adjustment was made as a 4 result of recommendation of the HAY consultant 5 that we've been using now for 20 years to 6 bring us in line with the compensation policy 7 of the corporation, which is a 50th percentile 8 of the Canadian industrial commercial, and it 9 was felt that the change in targets should be 10 made and that was a recommendation from HAY 11 and he had also went through the corporate 12 governance and subsequently to the Board of 13 Directors. 14 MR. JOHNSON: 15 Q. Mr. Ludlow, if I could direct your attention 16 to 443 once more, and into the -- well into 17 the document, about 15 or 16 pages in, gives 18 the 2012 short term incentive plan performance 19 targets for yourself and the other members of 20 the executive team, and indeed the managers. 21 MR. LUDLOW: 22 A. 2012? 23 MR. JOHNSON: 24 Q. Yes, sir. And just to look at your one for a 25 moment, do we have yours up there? Yes. So</p>

Page 73	Page 75
<p>1 as I understand it, in terms of the financial</p> <p>2 results, particularly tied to the earnings,</p> <p>3 the only executives whose results are tied to</p> <p>4 earnings on a personal basis would be yours</p> <p>5 and Ms. Perry's. Is that correct?</p> <p>6 MR. LUDLOW:</p> <p>7 A. Bear with me a minute. I haven't got them all</p> <p>8 committed to memory. That is correct.</p> <p>9 MR. JOHNSON:</p> <p>10 Q. Okay. And one of the corporate targets that</p> <p>11 we saw previously was the -- that fell under a</p> <p>12 financial target was controllable costs and</p> <p>13 there's nobody personally is impacted by the</p> <p>14 controllable costs other than through the</p> <p>15 corporate target?</p> <p>16 MR. LUDLOW:</p> <p>17 A. Not directly.</p> <p>18 MR. JOHNSON:</p> <p>19 Q. Not directly.</p> <p>20 MR. LUDLOW:</p> <p>21 A. But everyone inclusively.</p> <p>22 MR. JOHNSON:</p> <p>23 Q. Everyone inclusively by virtue of it being a</p> <p>24 corporate target?</p> <p>25 MR. LUDLOW:</p>	<p>1 MR. LUDLOW:</p> <p>2 A. Not directly. That is correct.</p> <p>3 MR. JOHNSON:</p> <p>4 Q. Okay. And in terms of the managers, they have</p> <p>5 a stake as well by virtue of the corporate</p> <p>6 target in the company's earnings as well,</p> <p>7 right?</p> <p>8 MR. LUDLOW:</p> <p>9 A. Yes, they would.</p> <p>10 MR. JOHNSON:</p> <p>11 Q. Yes, okay. And I guess, Mr. Ludlow, to come</p> <p>12 to the point, when we consider the matter of</p> <p>13 earnings in the company and so for instance,</p> <p>14 for 2012, if we look at yours, to achieve the</p> <p>15 100 percent payout for financial results, it</p> <p>16 says subjective with minimum earnings of \$1.</p> <p>17 million and what does the subjective mean?</p> <p>18 MR. LUDLOW:</p> <p>19 A. The way that this would be presented to our</p> <p>20 governance committee is we would look at the</p> <p>21 year and if it was just a slam dunk that 31. 5</p> <p>22 million fell out without effort, this combines</p> <p>23 personal contribution. It involves what we've</p> <p>24 had to do. If I want to go to Igor, let's go</p> <p>25 back there on the topic. Subjected in meeting</p>
Page 74	Page 76
<p>1 A. Correct.</p> <p>2 MR. JOHNSON:</p> <p>3 Q. Okay. So you have an individual stake through</p> <p>4 the STI in the company's earnings, but you</p> <p>5 don't have an individual stake in the</p> <p>6 company's controllable costs and nor does Ms.</p> <p>7 Perry?</p> <p>8 MR. LUDLOW:</p> <p>9 A. I'm -</p> <p>10 MR. JOHNSON:</p> <p>11 Q. Let's put it this way -</p> <p>12 MR. LUDLOW:</p> <p>13 A. I'm trying to answer your question and trying</p> <p>14 to be helpful here.</p> <p>15 MR. JOHNSON:</p> <p>16 Q. And I'm not putting it properly either, so</p> <p>17 I'll just back up.</p> <p>18 MR. LUDLOW:</p> <p>19 A. So we'll agree on that.</p> <p>20 MR. JOHNSON:</p> <p>21 Q. We'll agree on that. What I'm asking you is</p> <p>22 in relation to your short term incentive plan</p> <p>23 target, your individual targets, while it</p> <p>24 includes company earnings, does not include</p> <p>25 controllable cost?</p>	<p>1 earnings means that there was a lot of work</p> <p>2 had to be done to manage the organization for</p> <p>3 four to five years to readjust, rejiggle, do</p> <p>4 what we could to make things happen. So it's</p> <p>5 not just about a number falling out. It's</p> <p>6 about a reflection on the year. It's about</p> <p>7 the effort and it's about did this group</p> <p>8 perform the way they should have been</p> <p>9 performing to get that number, not just</p> <p>10 happenstance.</p> <p>11 MR. JOHNSON:</p> <p>12 Q. But if it's expressed as a minimum, can't you</p> <p>13 say well, look, gee, I met the minimum?</p> <p>14 MR. LUDLOW:</p> <p>15 A. You can say a lot of stuff, Mr. Johnson, but</p> <p>16 I'm going to tell you something, that when</p> <p>17 this is presented and I have to debate on</p> <p>18 behalf of Ms. Perry or Mr. Alteen or Mr.</p> <p>19 Smith, I can assure you when I look at this,</p> <p>20 the fact that it's 31 don't automatically mean</p> <p>21 they get it. It means that without it they</p> <p>22 won't get it.</p> <p>23 MR. JOHNSON:</p> <p>24 Q. But in point of fact, say for 2013 and 2014,</p> <p>25 you are assuming, for the purposes of your</p>

Page 77	Page 79
<p>1 revenue requirement, that that target is met, 2 are you not? 3 MR. LUDLOW: 4 A. When we prepared the rate filing, the revenue 5 requirement, we had to have a basis and 100 6 percent is target. It's not over the target 7 or under the target. It should be reasonably 8 attainable. And that's the basis upon which 9 we decided to include in our revenue 10 requirement the 100 percent STI payment for 11 the executives and managers of Newfoundland 12 Power. So we put the 100 percent in and 13 that's the basis of it. 14 MR. JOHNSON: 15 Q. So if anybody is wondering whether their rates 16 in 2013 and 2014 would reflect, for instance, 17 yourself and Ms. Perry -- not to pick on you, 18 but you're the two individuals - 19 MR. LUDLOW: 20 A. Okay, I'm used to that. 21 MR. JOHNSON: 22 Q. - are going to achieve that target, the answer 23 would be yes, that they can assume that 24 because that's what the revenue requirement is 25 based on?</p>	<p>1 Q. I'm easy to break as well. 2 CHAIRMAN: 3 Q. Let's break. 4 MR. JOHNSON: 5 Q. Okay. 6 MS. GLYNN: 7 Q. We'll come back in? 8 CHAIRMAN: 9 Q. How long have we got? 10 MS. GLYNN: 11 Q. Half an hour. 12 CHAIRMAN: 13 Q. Half an hour. 14 (11:15 a.m.) 15 (BREAK) 16 (11:47 a.m.) 17 CHAIRMAN: 18 Q. I think we're back to you, Mr. Johnson. 19 MR. JOHNSON: 20 Q. Thank you, Mr. Chairman. Mr. Ludlow, in terms 21 of the earnings of Newfoundland Power, the 22 primary beneficiary of the earnings is the 23 shareholders of Newfoundland Power, not the 24 customer. Would you grant me that? 25 A. No, I would not agree to that statement, Mr.</p>
Page 78	Page 80
<p>1 MR. LUDLOW: 2 A. I'll take a little exception to that. I would 3 agree on the basis that it is what the revenue 4 requirement is based on. Everyone is entitled 5 to draw their own assumptions. The fact that 6 it's in there don't mean that it will be paid. 7 That I can assure you. 8 MR. JOHNSON: 9 Q. Now as between the shareholders and the 10 customers, I take it it's a truism that 11 shareholders are the ones with the primary -- 12 are the primary - 13 CHAIRMAN: 14 Q. Mr. Johnson, just -- are you going to be going 15 on much longer? 16 MR. JOHNSON: 17 Q. No, I'm wrapping up. 18 CHAIRMAN: 19 Q. Okay. 20 MR. JOHNSON: 21 Q. I'm going to be wrapping up in about five 22 minutes on this one. 23 CHAIRMAN: 24 Q. Okay. 25 MR. JOHNSON:</p>	<p>1 Chairman. I think there's a balance that 2 needs to be struck, particularly in the 3 earnings, financial integrity. If we want to 4 take that and go to the operating conditions 5 that needs a focus to be brought, so I think 6 overall there is a balance in there. 7 Q. I thought the question was very - called for a 8 very obvious reply, Mr. Ludlow, that 9 shareholder profit, that which turns into 10 dividends to go back to shareholders, while 11 there may be some aspect of benefit to 12 customer in some sense, the primary 13 beneficiary of the earnings is that of the 14 shareholder, is it not? 15 A. There's no question that the financial 16 integrity or the earnings of the company go 17 back to the - obviously, the common equity 18 shareholders, yes, but in getting that and 19 creating that earnings is a separate issue. 20 Q. Yeah, but the primary beneficiary of the 21 earnings would be the shareholders? 22 A. The dollars, yes. 23 Q. Yes, and I guess then you would have an 24 incentive, your executive team would have an 25 incentive to make the company's earnings as</p>

Page 81	Page 83
<p>1 high as possible, right?</p> <p>2 A. We would look at maximizing earnings in tandem</p> <p>3 with various other aspects of the company, and</p> <p>4 that includes customer service, reliability,</p> <p>5 safety, and all those factors and that's</p> <p>6 effectively what's built into the STI Program.</p> <p>7 To maximize earnings, I can crater either one</p> <p>8 or the two of the others, and that is</p> <p>9 unacceptable under any circumstances.</p> <p>10 Q. But your - but the incentive, nevertheless,</p> <p>11 there is an incentive to make the company's</p> <p>12 earnings higher, not lower? That's very</p> <p>13 clear, right?</p> <p>14 A. The earnings of the company as laid out in the</p> <p>15 STI is set based on the allowed earnings as</p> <p>16 laid out before this Board. The whole STI</p> <p>17 Program that we're discussing basically should</p> <p>18 ensure and will ensure earnings of a company -</p> <p>19 I'm not going to sit here and say we should</p> <p>20 not make money, we make money. We look after</p> <p>21 the customers of this company, we also do our</p> <p>22 best to keep the lights on under less than</p> <p>23 ideal circumstances. You put all that in the</p> <p>24 pot, sound financial management is core to</p> <p>25 running a solid business under any</p>	<p>1 MR. JOHNSON:</p> <p>2 Q. This witness has testified that the executives</p> <p>3 have a stake in - and the managers have a</p> <p>4 stake in the earnings of the company, and he's</p> <p>5 testifying here that the Board has got to keep</p> <p>6 in mind some sort of balance, which I'm sure</p> <p>7 the Board will, but I think it's material to</p> <p>8 know what it means to this witness and to the</p> <p>9 executives and managers of Newfoundland Power</p> <p>10 in terms of their compensation if this Board</p> <p>11 were to accede to what Newfoundland Power is</p> <p>12 telling this Board it requires by way of a</p> <p>13 return on equity, which is 10.4 percent. I</p> <p>14 think it is a perfectly legitimate question.</p> <p>15 KELLY, Q.C.:</p> <p>16 Q. And that tells me nothing more, Mr. Chairman,</p> <p>17 than all the questions which have previously</p> <p>18 been asked, and if my friend is looking for</p> <p>19 some piece of information which he has not</p> <p>20 asked, which I can't figure from the question,</p> <p>21 then he should have put it in an RFI at the</p> <p>22 appropriate time. I do not accept the</p> <p>23 undertaking.</p> <p>24 CHAIRMAN:</p> <p>25 Q. I think you're asking a what if question, is</p>
Page 82	Page 84
<p>1 circumstances.</p> <p>2 Q. And you've done all that without a 10.4</p> <p>3 percent return over the last few years,</p> <p>4 correct?</p> <p>5 A. We have not earned 10.4 percent in many years.</p> <p>6 Q. And in terms of - just to get a sense of this,</p> <p>7 Mr. Ludlow, would you be able to provide us by</p> <p>8 way of an undertaking with what it would mean</p> <p>9 to yourselves and the executives and managers</p> <p>10 in terms of extra compensation if you were to</p> <p>11 be allowed the 10.4 percent return on equity</p> <p>12 by this Board? Would you provide that in an</p> <p>13 undertaking?</p> <p>14 KELLY, Q.C.:</p> <p>15 Q. We've answered numerous requests for</p> <p>16 information on the STI Program, all of which</p> <p>17 are based upon the company's application,</p> <p>18 which is 10.4 percent built into it. So I</p> <p>19 have no idea what precisely this request would</p> <p>20 be, so I'm not agreeing to an undertaking of</p> <p>21 that, especially when that 10.4 percent has</p> <p>22 been built into it. We've been through a</p> <p>23 rigorous program of answering RFI's on what</p> <p>24 the current application is. No, I do not</p> <p>25 accept the undertaking.</p>	<p>1 that what you're saying, if the Board agrees</p> <p>2 to the 10.5 percent ROE, what does that mean</p> <p>3 to the compensation which will be paid to the</p> <p>4 executives of Newfoundland Power. That is</p> <p>5 your - that's the question?</p> <p>6 MR. JOHNSON:</p> <p>7 Q. That's the question.</p> <p>8 CHAIRMAN:</p> <p>9 Q. And you're not agreeing to answer that</p> <p>10 question?</p> <p>11 KELLY, Q.C.:</p> <p>12 Q. We have already answered a whole series of</p> <p>13 questions which effectively encompass that</p> <p>14 question, and if my friend was looking for</p> <p>15 something more -</p> <p>16 CHAIRMAN:</p> <p>17 Q. I think I'm going to turn it over to our</p> <p>18 solicitors to - do you have any insight into</p> <p>19 this?</p> <p>20 GREENE, Q.C.:</p> <p>21 Q. Yes, Mr. Chair. My name is Maureen Greene,</p> <p>22 and I am Board Hearing Counsel. I wasn't</p> <p>23 introduced before, but I believe most people</p> <p>24 in the room know who I am.</p> <p>25 CHAIRMAN:</p>

<p style="text-align: right;">Page 85</p> <p>1 Q. That was grievous omission. 2 GREENE, Q.C.: 3 Q. As I said, I'm sure most people know who I am. 4 With respect to the request, the request, and 5 the objection, as I understand the request, 6 the Chair has properly summarized what the 7 information requested by the consumer advocate 8 is. The objection, as I understand it from 9 Mr. Kelly, is that it's too late, it should 10 have been asked in an RFI process. I don't 11 believe that particular question in that was 12 asked in the RFI process, we cannot turn to 13 the record and see if that particular piece of 14 information isolated. I would point out for 15 the Commissioners that from time to time 16 during the hearing process it does arise that 17 new information is requested and undertakings 18 are given, so I don't - with respect to the 19 objection that it's simply too late in the 20 process, I would point out to the 21 Commissioners that in the past it has been a 22 common practice for undertakings to be 23 provided for answers to questions that arise 24 during cross-examination. So unless Mr. 25 Kelly had some other basis for his objection-</p>	<p style="text-align: right;">Page 87</p> <p>1 Q. And you want to know what that amount is? 2 MR. JOHNSON: 3 Q. That's right. 4 KELLY, Q.C.: 5 Q. The revenue stream that's put forward already 6 includes the 10.4 percent. That's already in 7 the revenue stream. It's there. That's the 8 problem I'm having. What is the question 9 precisely? 10 MR. JOHNSON: 11 Q. Well, we could certainly get at the difference 12 between what's currently there versus what the 13 10.4 would mean. 14 KELLY, Q.C.: 15 Q. Well, now we're asking another question. 16 That's the problem I've got with this whole 17 process. If you start giving loose 18 undertakings, then the company is off trying 19 to figure out what the heck the question 20 means. So if my friend has a specific written 21 question, he should put forward a specific 22 written question that we can then take under 23 advisement. 24 MR. JOHNSON: 25 Q. Mr. Chairman, if it will bring clarity to it,</p>
<p style="text-align: right;">Page 86</p> <p>1 KELLY, Q.C.: 2 Q. I do not agree that it is new information. 3 That's the fundamental objection. 4 GREENE, Q.C.: 5 Q. Well, if that's the case, can you point to the 6 RFI where that answer is. 7 KELLY, Q.C.: 8 Q. I can't point to the RFI because there's no 9 precision in even what this undertaking is 10 that we are being asked to answer. If my 11 friend wants to put this forward, the first 12 thing he should do is commit it to a specific 13 written request as to what the undertaking is 14 that he's looking for. 15 CHAIR: 16 Q. Presumably, Mr. Johnson is saying that if we 17 allowed it, it would be an additional revenue 18 stream, and you're saying that this revenue 19 stream would fall directly to - all other 20 considerations aside, it would fall to 21 corporate compensation, is that what you're 22 saying? 23 MR. JOHNSON: 24 Q. Yes. 25 CHAIRMAN:</p>	<p style="text-align: right;">Page 88</p> <p>1 I'd be happy to devise the question and 2 present it to the Board for the Board's 3 consideration. 4 GREENE, Q.C.: 5 Q. Mr. Chair, the consumer advocate has agreed to 6 do that, and that is fine for moving this 7 process forward, but again for the future part 8 of the hearing, as long as the question is 9 very clear, it has not been the practice in 10 the past to require written questions before 11 undertakings are given during the examination 12 of witnesses, but we have agreed for this 13 particular one to move forward in this way. 14 KELLY, Q.C.: 15 Q. I don't want to get into an argument with 16 Board Hearing Counsel, but there have always 17 been in terms of undertakings, Mr. Chairman, 18 two factors. One, clarity is required, and 19 two, necessity and reasonableness to assist 20 the Board is required. So the simple basis 21 which Ms. Greene may suggest that if a 22 question is proposed, that some undertaking 23 therefore automatically follows, I don't 24 accept that proposition because that would 25 turn hearings into endless undertakings which</p>

Page 89	Page 91
<p>1 is not appropriate, and that's never been the</p> <p>2 practice in the 15 odd years that I've been</p> <p>3 here. Now I don't wish to engage in argument</p> <p>4 on that. We can move forward.</p> <p>5 GREENE, Q.C.:</p> <p>6 Q. I don't either, and I don't want to delay the</p> <p>7 process. I do agree that obviously it has to</p> <p>8 be relevant to matters before the Board, and</p> <p>9 it also has to be a clear question. I think</p> <p>10 for the -</p> <p>11 CHAIRMAN:</p> <p>12 Q. I mean, it shouldn't be hard to generate a</p> <p>13 number with the - say, the current ROE, and</p> <p>14 assuming 10.5 or whatever it is, that number</p> <p>15 should be very - that shouldn't be hard to</p> <p>16 find that number. I think that's basically</p> <p>17 the number that Mr. Johnson is looking for.</p> <p>18 KELLY, Q.C.:</p> <p>19 Q. And is that for total executive compensation</p> <p>20 or -</p> <p>21 CHAIRMAN:</p> <p>22 Q. Well, you better ask him that. I'm just</p> <p>23 trying to -</p> <p>24 KELLY, Q.C.:</p> <p>25 Q. Well, that's my problem. That's why you got</p>	<p>1 We can get some, but not a lot. Now we're</p> <p>2 into the apprenticeship programs. So, you</p> <p>3 know, our complement is changing slightly</p> <p>4 because of workforce changes that's happened.</p> <p>5 The workload is changing as well in St.</p> <p>6 John's as it is coming down and up in other</p> <p>7 areas - up here, sorry, down in other areas.</p> <p>8 So overall our ability to look forward and to</p> <p>9 forecast, we're always at that on a regular</p> <p>10 basis.</p> <p>11 Q. In terms of the challenges of obtaining</p> <p>12 skilled workers that everybody is finding, I</p> <p>13 guess that's a reflection of the economy. How</p> <p>14 would you describe the local economy, would</p> <p>15 you consider it strong from your perspective</p> <p>16 where you sit?</p> <p>17 A. I would look at the Newfoundland economy in</p> <p>18 total as being strong in many pockets, and</p> <p>19 when I say that, I would say when I look at</p> <p>20 the developments in Labrador, Vale in Long</p> <p>21 Harbour, or Hebron, and the oil industry in</p> <p>22 general and you can see the bustle around the</p> <p>23 city here, but that's contrasted very heavily</p> <p>24 as you move into a lot of what I would call</p> <p>25 the smaller areas of this province. So the</p>
Page 90	Page 92
<p>1 to have clarity in the question. I think we</p> <p>2 should move on and have the question put into</p> <p>3 some written form.</p> <p>4 MR. JOHNSON:</p> <p>5 Q. I'll provide the clarity, Mr. Chairman.</p> <p>6 CHAIRMAN:</p> <p>7 Q. Okay.</p> <p>8 KELLY, Q.C.:</p> <p>9 Q. Thank you, Mr. Chairman.</p> <p>10 MR. JOHNSON:</p> <p>11 Q. Mr. Ludlow, in terms of getting workers,</p> <p>12 skilled workers at Newfoundland Power, I take</p> <p>13 it that you have a full complement, you're</p> <p>14 content with the complement that you have in</p> <p>15 terms of your ability to attract the skilled</p> <p>16 workers that you need?</p> <p>17 A. That's a very difficult question. It changes</p> <p>18 by the day, Mr. Chairman. Our complement, I</p> <p>19 think is changing a little bit as we go</p> <p>20 forward. Our ability to attract fully skilled</p> <p>21 workers has changed dramatically. Our</p> <p>22 approach to having future skilled workers has</p> <p>23 had to move from a hiring of, I'll use the PLT</p> <p>24 or mine person scenario, we can no longer</p> <p>25 attract Red Seal with full journeyman status.</p>	<p>1 economy of the province in total today is</p> <p>2 strong. In the foreseeable future, there will</p> <p>3 continue to be challenges.</p> <p>4 (12:00 p.m.)</p> <p>5 Q. In terms of - I guess, looking at it from the</p> <p>6 point of view of your customer growth since</p> <p>7 the last general rate application, how would</p> <p>8 you describe it?</p> <p>9 A. Again, Mr. Chairman, I'd look at our customer</p> <p>10 growth - we look at gross. We use the term,</p> <p>11 gross new connections. What does that mean?</p> <p>12 That means the number of new houses, or I</p> <p>13 don't know, garages and things that have been</p> <p>14 hooked up. We've connected record numbers</p> <p>15 particularly in the St. John's, Avalon, and</p> <p>16 the major centres. Conversely, we have seen a</p> <p>17 retraction, not of numbers, but of sales in a</p> <p>18 lot of the rural areas. So it's - again I've</p> <p>19 used the balance on a couple of pieces. We're</p> <p>20 seeing this urbanization which is not unique</p> <p>21 to Newfoundland, but it's happening. We're</p> <p>22 also seeing an impact of new workers coming</p> <p>23 in. So right now that's where we're to. The</p> <p>24 economy in this local area is pretty hot right</p> <p>25 now.</p>

Page 93	Page 95
<p>1 Q. And the workers coming in, what are you seeing 2 in that regard? You mentioned you're seeing 3 the workers coming in. On projects and 4 things?</p> <p>5 A. When I say I see them coming in, I'm reading 6 newspapers, and seeing what I see in the local 7 economy, it would be primarily the larger 8 centres again, driven around major projects is 9 what I'm hearing, and what I do envision or 10 see, it's not that I can write numbers to it 11 or quote actual details. There are some 12 coming in, but as I look to 2017 to 2030 - now 13 I rely pretty heavily again back on long haul 14 forecasters, and even short to medium term 15 forecasters. I can comment that the 16 population is forecast to decline 17 substantially by late 1920s - er, 1920s, you 18 know, 2030, and combine that with the dynamics 19 and the demographics within that population is 20 changing a lot as well, both on shift and age. 21 Huge things happening out there right now.</p> <p>22 Q. In terms of the concentration of your reach 23 for electricity into the market, it's 24 basically around 9 out of 10 new construction 25 go with electric for heat, I take it, and</p>	<p>1 that.</p> <p>2 Q. Just to clarify, that's the 90 percent?</p> <p>3 A. Yes.</p> <p>4 Q. All right. I want to ask you a question and 5 this goes back to the introduction. Because 6 cost of capital is so central here, Mr. 7 Ludlow, as I pointed out in my introduction, 8 the Board's comments from PU-43 where they 9 talked about the fact that it's not enough 10 that the chosen comparables be the best 11 available - you heard that introduction, and 12 they noted, you know, that nearly on every 13 indicator the Board noted the overwhelming 14 evidence of the lack of balance, as it was 15 clear on almost every measure Newfoundland 16 Power would have to be considered less risky 17 than the US comparables. Can I ask you, you 18 know, were you concerned, are you concerned as 19 the CEO of Newfoundland Power by the Board's 20 findings in that regard? Can you expand on 21 that?</p> <p>22 A. I don't have a whole lot that I can add to 23 that commentary. You know, we took the 24 Board's order, we look at it, we read it, and 25 we apply it. There's not a lot of explanation</p>
Page 94	Page 96
<p>1 where is the other 1 out of the 10 ending up, 2 on the oil furnace, wood stove in a new house 3 - it's harder to think that they rely fully on 4 that, but what are you - what's your sense of 5 that?</p> <p>6 A. My sense is that a lot of new homes are 7 heading towards, unless it's - I'll use the 8 term approximately 90 percent. The balance 9 are still heading towards oil, some propane, 10 still heading a little bit of wood/oil 11 combinations is happening out there, and 12 that's roughly how I would see it, Mr. 13 Johnson.</p> <p>14 Q. Your 90 percent, what are you counting as the 15 90 percent? In terms of the new customer, is 16 that the customers who's relying on you for 17 heating load?</p> <p>18 A. When I look at new customers, when I say - I 19 said earlier that we have roughly 5,000 plus 20 gross new connections. In there you've got 21 everything from garages, and there might be 22 power supplied boxes for, I don't know, 23 Rogers, Aliant, and what have you, but the 24 majority of the homes would be relying on us 25 for heating supply. There's no question about</p>	<p>1 or broadening that I can add at this point.</p> <p>2 Q. Were any steps taken for the purpose of this 3 rate application to ensure that the Board's 4 concerns were addressed in relation to that 5 key finding in its last decision?</p> <p>6 A. Can you just explain that a little further, 7 what the key finding and what your question 8 is, please?</p> <p>9 Q. Well, I view it as a pretty key finding that 10 first of all it's not enough to just - it's 11 not enough to say that the comparables are the 12 best available, and that if the data is to be 13 relied on, it must be shown to be a reasonable 14 proxy or that reasonable adjustments can be 15 made to account for the differences, and then 16 the Board noted that the evidence showed that 17 on balance the US comparables - on balance, 18 the Board noted that the overwhelming evidence 19 was of a lack of balance as it was clear on 20 almost every measure Newfoundland Power would 21 have to be considered less risky than the US 22 comparables. So that was the chief concern, 23 and my question, did you or your team take any 24 steps to ensure that the Board's concern was 25 met for the purpose of this rate application?</p>

Page 97	Page 99
<p>1 A. Mr. Chairman, the whole area of cost of 2 capital and comparators is something that once 3 we get into the details and what I would call 4 the specifics of risk, in my opinion it would 5 be much better dealt with with our expert 6 evidence, experts when they come by. 7 Similarly, Ms. Perry may be able to add some 8 basis to this, but it would be much more 9 helpful than what I can add to this discussion 10 at this time.</p> <p>11 Q. Well, are you aware of any instruction from 12 either yourself or your executive team to cost 13 of capital witnesses in terms of being 14 responsive to what the Board's concerns were 15 that I just addressed with you?</p> <p>16 A. I did not instruct our expert witnesses to 17 make change, pro or con, on any of the basis 18 of numbers. We basically engage expert 19 witnesses. They are provided with the 20 information on our business and to put forward 21 the testimony that you have seen here today.</p> <p>22 Q. Would you believe, Mr. Ludlow, from sitting in 23 the customer's perspective that it would be 24 fair for Newfoundland Power for cost of 25 capital purposes to compare itself to</p>	<p>1 reality, it's something I've got to deal with 2 and I'm trying to stay focussed on what I'm 3 doing here today while I'm wondering whether 4 Burin is going to stay on tonight. That is a 5 reality of my business. That operating 6 conditions is key. So when I look at the 7 various components of our business and a 8 business risk profile, business risk 9 regulatory and financial, yeah, I would put us 10 in the average risk category. That's how I 11 would see us.</p> <p>12 Q. Okay, now if you could answer my question, and 13 that would be do you believe it would be 14 reasonable for Newfoundland Power to ask for a 15 cost of capital in relation to companies that 16 would be on nearly every measure more risk 17 than Newfoundland Power? Would that be 18 reasonable to you?</p> <p>19 A. The premise for the question, I think would be 20 better addressed to other individuals. From 21 my perspective, I don't know all the pieces of 22 all those other businesses. When we look at 23 an average risk utility, then I would suggest 24 if we're average risk, we should be treated as 25 average risk. That's the way I would see it.</p>
Page 98	Page 100
<p>1 companies that would on nearly every measure 2 more risky than Newfoundland Power? Would 3 that be fair to you?</p> <p>4 A. Mr. Chairman, this is where I get a little 5 confused. I have worked in a lot of 6 businesses across this country, and in 7 particular as I look at the Canadian 8 environment, and I'll go there for a minute, 9 we know where Newfoundland Power - we talked 10 about business risk, regulatory risk, and we 11 look at the financial risk. You put all that 12 in a pot and I think it's been clear, clear 13 from this Board that we remain an average 14 regulatory risk - average risk utility. Now 15 we can go out and we can look at other 16 businesses, and I've work in them, and they 17 will have pros and cons. Some will have, as I 18 said earlier, a deferral account for storms. 19 They will not have an excess earnings account. 20 So it's not a matter of me sitting here and 21 saying this one is better or less or up or 22 down. What I'm saying is when we get to that 23 average point, which I think is where we are - 24 I mean, I can tell you I can pull out things 25 that - look at the weather today, this is</p>	<p>1 Q. So anything about these companies in your 2 expert sample, essentially you have to rely 3 totally on what your experts are telling you?</p> <p>4 A. Mr. Chairman, we brought in expert witnesses 5 for a reason. They are experts. I have not 6 had the privilege of working with hundreds of 7 different utilities or being around them. I 8 know five. Now I can speak to that from a CEO 9 perspective, a Senior Vice President's 10 perspective, and a Vice President of 11 Engineering and Operations. I look at the 12 markets, I rely heavily on Ms. Perry, on her 13 recommendations and where we are, and then we 14 go and get experts in the field, and that's 15 what we've done. That's what we will put 16 before this Board and are doing in this 17 hearing.</p> <p>18 Q. The five companies that you know the most 19 about are the companies that you've been 20 associated with either as a Director or an 21 Executive or worked for generally with Fortis, 22 I take it?</p> <p>23 A. Yes.</p> <p>24 Q. And those companies would be what, Mr. 25 Ludlow?</p>

Page 101	Page 103
<p>1 A. They would be BC, Alberta, Ontario, Prince 2 Edward Island. That's the four I would use. 3 Q. What BC one are you talking about? 4 A. I'm talking about the former West Kootenay 5 Power, which is now Fortis BC Electric. 6 (12:15 p.m.) 7 Q. Okay, and how about Alberta? That would be 8 Fortis Alberta? 9 A. That would be Fortis Alberta. 10 Q. And Ontario? 11 A. That would be Fortis Ontario. 12 Q. And PEI is the Maritime. Now you referred to 13 financial risk. What do you mean by that, Mr. 14 Ludlow? 15 A. Financial risk that I refer to would be the 16 structure, the financial structure, debt 17 equity structure of the business. 18 Q. And in terms of the debt equity structure of 19 the business, what is the risk that you're 20 referring to? 21 A. The risk I refer to is we currently would run 22 on a 45/55 debt equity - equity debt split. 23 So if that were to be reduced and we were to 24 dividend out substantive funds and increase 25 the debt equity ratio, now all of a sudden our</p>	<p>1 equity in your capital structure, and I take 2 it that you wouldn't disagree with me that a 3 company that has higher common equity in its 4 financial structure is seen to have less 5 financial risk than one that has lower common 6 equity in its financial structure? We don't 7 disagree on that, do we? 8 A. I'm certainly not going to disagree, but what 9 I am going to say to you is you posed the 10 question, or the question was posed, Mr. 11 Chair, that we are one of the highest in 12 Canada. 13 Q. Well, let me put it this way. Your common 14 equity component in your company's capital 15 structure is the highest certainly of all the 16 Fortis companies, is it not? 17 A. I don't know the details of all the Fortis 18 companies, Mr. Chair. I really don't. 19 Q. Could I refer you to the MDNA of Fortis, which 20 was filed as an information item, just so we 21 can be confirmed on what the capital 22 structures of the other Fortis companies are. 23 That would be - 24 KELLY, Q.C.: 25 Q. Mr. Chairman, the witness has already</p>
Page 102	Page 104
<p>1 fixed costs are implied. That basically is 2 the financial risk area that I would look at, 3 so the basis under which - the detail of that, 4 Mr. Johnson, I think I would defer beyond that 5 point to Ms. Perry. 6 Q. But generally, your understanding of financial 7 risk would be the more debt and less equity in 8 the capital structure, the more financial 9 risk? 10 A. Correct. 11 Q. So on that measure, you would have less 12 financial risk than any other Fortis company 13 in the country, would you not? 14 A. I'm not certain I would go as far as to say 15 that I have the less risk. I would suggest to 16 you - 17 Q. Less financial risk? 18 A. I have 45 percent ratio, and as such we have 19 strong regulatory support here in this 20 province, and it's been reflective of the 21 small size of our utility and that's been 22 stated multiple times. 23 Q. But, Mr. Ludlow, I'm trying to focus on 24 something. You mentioned financial risk and 25 then you tied financial risk to the amount of</p>	<p>1 indicated many of these questions would be 2 better posed to Ms. Perry, and I notice that 3 the document that the witness (sic) proposes 4 now to put to Mr. Ludlow is one which was 5 provided for Ms. Perry's examination. So I 6 think we need to be fair to the witness as 7 well. 8 MR. JOHNSON: 9 Q. The witness worked for these companies and he 10 was a Director of all of them, would that be 11 right? 12 A. My role was - that is not correct. I was the 13 Vice President of Engineering for Fortis 14 Alberta, Senior Vice President in British 15 Columbia, and Vice President of Engineering 16 and Operations for Maritime Electric. 17 Q. And you weren't a director of any of those 18 companies? 19 A. I was a director of Maritime Electric, or am a 20 director of Maritime Electric, and a director 21 of Fortis Ontario. 22 Q. You would be aware, would you not, that 23 Maritime Electric is 40 percent common equity? 24 A. I honestly don't know the number off the top. 25 If you wish, we can get it, and I'm sure it's</p>

Page 105	Page 107
<p>1 in the somewhere. I just don't know what it</p> <p>2 is.</p> <p>3 Q. Let's put it this way -</p> <p>4 A. Sorry, as a director, Mr. Chair, I don't know</p> <p>5 all the - I can tell you the details and work</p> <p>6 with it, but I just don't have it at the top</p> <p>7 of my -</p> <p>8 Q. Let's put it this way, if the record will</p> <p>9 disclose, okay, that Newfoundland Power has</p> <p>10 higher common equity in its capital structure</p> <p>11 than any other Fortis company in Canada, would</p> <p>12 that not mean that Newfoundland Power has less</p> <p>13 financial risk than any other Fortis company</p> <p>14 in Canada?</p> <p>15 A. As I look at that question, on the surface I</p> <p>16 would be inclined to say yes, but before I'm</p> <p>17 too definitive on that, I do want the input of</p> <p>18 my CFO and that would be Ms. Perry, and that</p> <p>19 question would be better directed in that</p> <p>20 direction. On the surface, I would say, yes.</p> <p>21 Q. You're saying yes to what?</p> <p>22 A. Your question.</p> <p>23 Q. So you're saying, yes, that Newfoundland Power</p> <p>24 would seem to have less financial risk than</p> <p>25 the others, correct?</p>	<p>1 risk? Is that what you're saying?</p> <p>2 A. Mr. Chairman, it sounds like I'm getting</p> <p>3 myself into an argument, and I don't mean to</p> <p>4 be, okay. I'm agreeing that we have a higher</p> <p>5 financial structure at the 45/55. If there</p> <p>6 are other implications within that financial</p> <p>7 risk, I just don't know what they are at this</p> <p>8 point in time. If it's based solely on</p> <p>9 capital structure, from where I sit, as I said</p> <p>10 earlier, we are high at 45, high being not</p> <p>11 relative to the others, but given the other</p> <p>12 parameters of us being a small utility, that I</p> <p>13 would agree. With respect to what else are in</p> <p>14 the financial risk categories, I don't know</p> <p>15 what they are and I'm not basically an expert</p> <p>16 to talk about them.</p> <p>17 Q. Now you are aware, Mr. Ludlow, that - I'll ask</p> <p>18 you the question, I won't lead it. What</p> <p>19 company does Newfoundland Power consider in</p> <p>20 Canada that it's comparable to?</p> <p>21 A. What company? Utility, I assume you're</p> <p>22 referring to.</p> <p>23 Q. Yes, for cost of capital purposes.</p> <p>24 A. That's an interesting question because as I</p> <p>25 look at it, I would have to look across all</p>
Page 106	Page 108
<p>1 A. Mr. Chairman, our equity stake is at 45</p> <p>2 percent. We said we've had strong regulatory</p> <p>3 support on that side of the financial matrix.</p> <p>4 That's been very clear. I don't know what all</p> <p>5 the details are of the equity debt structure</p> <p>6 of all the companies that I work on or have</p> <p>7 worked on, or if they've changed. If the</p> <p>8 capital structure, the credit ratings and so</p> <p>9 on - I'm sure there are other items in there</p> <p>10 that has financial risk implications, but from</p> <p>11 my perspective, I would be willing to say that</p> <p>12 the equity component that we have in</p> <p>13 Newfoundland Power of 45 percent represents a</p> <p>14 strong regulatory support in this environment.</p> <p>15 Beyond that, I think our conversation would</p> <p>16 probably be much more articulated by my CFO,</p> <p>17 Ms. Perry.</p> <p>18 Q. You cannot be - maybe you are saying this,</p> <p>19 that as the CEO of Newfoundland Power, and as</p> <p>20 a corporate director of one of the largest</p> <p>21 investor owned utility in Canada, that you</p> <p>22 cannot agree that if your company, in fact,</p> <p>23 has more common equity in its capital</p> <p>24 structure than another company, that that does</p> <p>25 not mean that your company has less financial</p>	<p>1 the variables. I would put us in, as I said</p> <p>2 earlier, an average risk category, and what</p> <p>3 other ones fall in that average risk category</p> <p>4 remains to be seen. Again that's a debate you</p> <p>5 can have. I can talk through all those</p> <p>6 various risk areas of business and so on with</p> <p>7 you. To put a peg on it, I don't think I can</p> <p>8 actually give you a company that I can compare</p> <p>9 myself to.</p> <p>10 Q. Could be bring up PUB-NP-014. In this</p> <p>11 question, Board staff asked, "How does the</p> <p>12 comparison of the allowed returns for other</p> <p>13 Canadian regulated utilities reconcile with</p> <p>14 the position that Newfoundland Power is an</p> <p>15 average risk utility", and the answer is,</p> <p>16 "Current allowed returns on equity for</p> <p>17 Canadian regulated electric utilities range</p> <p>18 from a low of 8.75 percent, Alberta Electric</p> <p>19 Utilities, to a high of 9.90 percent, Fortis</p> <p>20 BC. The utility with the current allowed</p> <p>21 return on equity of 9.9 percent is Fortis BC.</p> <p>22 Fortis BC appears to Newfoundland Power to be</p> <p>23 a comparable average risk utility". So does</p> <p>24 that refresh your thinking on the subject?</p> <p>25 A. I mean, it is what it is. I've just - if you</p>

Page 109	Page 111
<p>1 ask me directly to a question are Fortis BC</p> <p>2 utilities on an average risk basis, I would</p> <p>3 agree with that. If I didn't, I wouldn't have</p> <p>4 filed it.</p> <p>5 Q. So the Fortis BC company, that's one that you</p> <p>6 worked with?</p> <p>7 A. That is correct.</p> <p>8 Q. And Fortis BC is what sort of company, Mr.</p> <p>9 Ludlow?</p> <p>10 A. Fortis BC is a transmission, distribution,</p> <p>11 customer service, and they have some hydro</p> <p>12 production facilities. The electric utility</p> <p>13 portion of it does.</p> <p>14 Q. And do you accept the proposition that</p> <p>15 Newfoundland Power is a poles and wires</p> <p>16 company, a transmission and distribution</p> <p>17 company?</p> <p>18 A. With a small amount of generation, yes, I</p> <p>19 would agree to that.</p> <p>20 Q. But for purposes of, for instance, how Moody's</p> <p>21 characterizes you, they say, look, we treat</p> <p>22 them like a T & D, right? Are you aware of</p> <p>23 that?</p> <p>24 A. By far the majority of our assets are in</p> <p>25 distribution, roughly 9,000 kilometres,</p>	<p>1 Kelowna through to - across Boundary Country</p> <p>2 and into Creston.</p> <p>3 Q. So they're much different than Newfoundland</p> <p>4 Power?</p> <p>5 A. That was the point I was making earlier, Mr.</p> <p>6 Chairman. When we talk about average risk and</p> <p>7 we talk about business risk, working in Nelson</p> <p>8 and down through Boundary Country, white cap</p> <p>9 on the lake was seen as a windy day. They</p> <p>10 have no idea around wind or ice. So the</p> <p>11 operating conditions are different. They</p> <p>12 basically have - their pole infrastructure are</p> <p>13 nowhere near the stresses and strains we would</p> <p>14 go through. Their demographics, the mobility</p> <p>15 of their people, that's all different.</p> <p>16 Electric heating, that's different. So</p> <p>17 everything changes, and I guess that's the</p> <p>18 point I'm making.</p> <p>19 Q. So could I ask you, do you believe that the</p> <p>20 business risk for Fortis BC is higher than</p> <p>21 Newfoundland Power's, or equal, or lower?</p> <p>22 A. This whole discussion, Mr. Chairman, higher or</p> <p>23 lower is irrelevant. We have to look at the</p> <p>24 three parts.</p> <p>25 Q. No, I'm talking about business risk.</p>
Page 110	Page 112
<p>1 another couple of thousand would be</p> <p>2 transmission, and we would have roughly 28</p> <p>3 small hydro and generating plants. So on the</p> <p>4 balance, I would say, you know, the total of</p> <p>5 our assets would be small on the generation</p> <p>6 side.</p> <p>7 Q. And would you not accept that transmission and</p> <p>8 distribution are seen to have less, let's say,</p> <p>9 business risk than an integrated utility, one</p> <p>10 that's into both generation, transmission, and</p> <p>11 distribution?</p> <p>12 A. Possibly so, yeah. I think I could go there,</p> <p>13 each unique to their own, but, yeah, that's</p> <p>14 fair.</p> <p>15 Q. And in the case of Fortis BC, that would be</p> <p>16 considered a vertically integrated company,</p> <p>17 right?</p> <p>18 A. Fortis BC would also be a much different</p> <p>19 company than we are. Fortis BC would also be</p> <p>20 buying energy on the markets through an</p> <p>21 integrated market system. So they operate</p> <p>22 plants, but they don't generate all their own.</p> <p>23 So they as well have a majority of</p> <p>24 distribution and transmission out there in</p> <p>25 their service territories in the areas of</p>	<p>1 A. I understand, but what I'm saying is we have</p> <p>2 to look at it even as we look at the business</p> <p>3 risk. As I look at our business risk</p> <p>4 components, I'll just run there for a little</p> <p>5 bit and then I'll go back to BC, I talk about</p> <p>6 the demographics, decline, and aging. That is</p> <p>7 reality, that's what we're into. We talk</p> <p>8 about weather and operating conditions.</p> <p>9 That's different, it's known, and it's</p> <p>10 changing. Cost flexibility; we're less than</p> <p>11 10 percent or running about 10 percent ability</p> <p>12 to manage our operating cost now on total</p> <p>13 revenue streams. Our management ability is</p> <p>14 declining. We talk about Igor, that's</p> <p>15 continuing to decline, our ability to adjust</p> <p>16 and make short term movement. We also run on</p> <p>17 a single future supply, sole source. Now I'll</p> <p>18 go to BC. I moved out of BC about five years</p> <p>19 ago - no, it's not now, my goodness, seven</p> <p>20 years ago. So they have a plant, a utility</p> <p>21 that was designed by a mining company, Teck</p> <p>22 Cominco. It had large blocks of customers</p> <p>23 that were in areas of Kelowna, Osoyoos, and</p> <p>24 down through the Okanagan. The plant, much</p> <p>25 older. They have some generating plants.</p>

Page 113	Page 115
<p>1 Population, increasing, not decreasing. 2 Workforce, not an issue. So there's a whole 3 lot of parameters. I'm not really in a 4 position to say, yes or no, higher or lower. 5 I mean, if I look at all those factors, I know 6 I'm facing a lot of challenges in the next 7 four to five years. BC, as I speak to them 8 from time to time, anecdotally, their ability 9 to attract workers don't appear to be a big 10 issue at this point. Their ability - their 11 load, median load, buying on the market and 12 multiple sourcing, they don't seem to have 13 those issues, and that's all I can say, Mr. 14 Johnson. Maybe there are things, but I don't 15 know them. 16 (12:30 p.m.) 17 Q. Do you have a sense as between - well, no, 18 I'll pass on this, actually. Mr. Ludlow, 19 there's reference made to Fortis Alberta 20 earning a return of 8.75 percent, and Fortis 21 Alberta, they're under service quality 22 standards, I take it? Are you aware of that? 23 A. I'm not familiar with the details, but I do 24 believe they are. There are some service - 25 Mr. Smith might be able to help you with those</p>	<p>1 would we say. I've already laid out the 2 operating conditions or the business risk. I 3 would look at market out there, pro and con, 4 whether they've got multiple suppliers. 5 That's not necessarily a good thing, not 6 necessarily a bad thing, but it's a different 7 place to work. I do know that they have also 8 worked in a PBR regime that didn't work so 9 well and they're rebuilding that company back 10 from where it was in the mid 90s, early 2000s. 11 I look at the people, the dynamics, I see the 12 heating load different because of gas. So I 13 guess the point that was being made as I look 14 here, there are so many variables that are 15 changing. There's no such thing as you take 16 Newfoundland Power and say line it up 17 perfectly against Fortis BC or Fortis Alberta, 18 but on a whole, when you bring all the factors 19 together, the regulatory environment in 20 British Columbia with the BCUC - it's again 21 fairly supportive, and when I look at where 22 the average risk from my perspective back 23 against BC, those are the factors, I think, 24 that I would take in, Mr. Johnson. 25 Q. Mr. Ludlow, I asked a recent RFI #682, having</p>
Page 114	Page 116
<p>1 later on. 2 Q. Okay. In terms of PBR, for instance, do you 3 know whether or not that would be expected to 4 subject you to at least a greater risk than a 5 pure cost of service regime? 6 A. I read the risk document out of Alberta, and 7 when I was finished, I have no idea what the 8 answer was, whether it's riskier or not, to be 9 quite honest with you in Alberta. They've 10 just embarked on the PBR process, and the 11 details I don't know, and I honestly do not 12 know the pieces of it. 13 CHAIRMAN: 14 Q. What's PBR? 15 A. It's Performance Based Regulation. 16 MR. JOHNSON: 17 Q. I guess, if I could ask you, would you be able 18 to encapsulate for me why it is you believe 19 that it's appropriate to compare Newfoundland 20 Power with Fortis BC, just put a bow around 21 that question for me. 22 A. Can I assume you're referring to the document 23 we had here earlier? 24 Q. Right. 25 A. Okay. When we look at average risk, what</p>	<p>1 to do with your company's in depth workforce 2 assessment. If we could bring that up. 3 A. The number again, please? 4 Q. 682. 5 A. I'm sorry, I don't have the paper copy which I 6 prefer to read by because - 7 Q. Yes, I understand. 8 A. Thank you. 9 Q. Mr. Ludlow, I guess the question came from a 10 reference in the annual report of Newfoundland 11 Power, where it stated that, "In early 2011 12 the company conducted an in depth workforce 13 assessment in which we projected retirements 14 for the next five years, reviewed workload 15 plans, and identified human resource 16 strategies to guide the company in the 17 future", and just tell us about how that 18 exercise came out, what spurred it on? 19 A. I think we looked at the exercise as one step 20 in multiples of exercises. I'm going to go 21 back a little bit here and, you know, when 22 this - we have a large number of our employees 23 that are coming through - were hired in the 24 60s, the 70s, and the early 80s, and we've got 25 - the demographic bubble, without getting into</p>

Page 117	Page 119
<p>1 specifics, is coming at us. We've seen it, 2 we're looking at it, and how do we get ready 3 as we go to the future. I would suggest that 4 it's pretty much a regular event that I would 5 have, look, where are we now, where were we, 6 where are we going, what are the skills we 7 will require, and these aren't global, these 8 aren't down to a unit or a position in Port 9 Aux Basques, it's what are - like, the impact 10 of technology, it's the impact of location, 11 it's the rural versus urban, do we need more 12 in St. John's or not, and those types of 13 thinking. That's one way we look at this. So 14 typically that type of an exercise would be 15 driven through HR, our Human Resources area, 16 and also through our Operations group, which 17 basically makes up for most of the bodies, as 18 it were, within the organization. Likewise to 19 that, what is it we're doing that we don't 20 need to continue doing. Now I'm back to how 21 can we continue to improve, operating cost 22 reductions, cost per customer, and I won't go 23 back into that, but that's the type of 24 thinking that comes to bear. That can happen 25 on a fairly regular basis. The reference here</p>	<p>1 look at age, demographics, I'd look at 2 locations, and that would be the type of 3 thinking that's going on all the time 4 throughout the HR of my business. 5 Q. Okay, and I understand that, but this got 6 special highlight in the company's annual 7 report, that the company conducted this in 8 depth workforce assessment, and one part of my 9 question was if any reports were produced from 10 the assessment, if you could provide a copy, 11 and there must have been reports or memos or 12 something generated from a process that would 13 merit the attention of specific mention in the 14 annual report, Mr. Ludlow, was there? 15 A. I do believe there's a feeling that everything 16 we do has to have long meetings and 17 bureaucracy wrapped around it. This whole 18 process, having HR involved, having my VP 19 Operations or his designate involved, no, we 20 will not create multi-bound documents. It 21 just don't happen. I'm not a tendency to sit 22 down and write emails and memos. I just don't 23 do it. I do know, though, that I will need 24 "x" number of individuals at this location, 25 are we ready, when are they leaving, what are</p>
Page 118	Page 120
<p>1 was done in early 2011, and we looked across 2 the organization and those are the types of 3 things that we then in turn build back in, pro 4 and con, into a proceeding like we're doing 5 here today as we build our costs. 6 Q. How long did the process take? 7 A. I have no idea. This could be running for 8 days, weeks - it could be weeks, and it's not 9 a group of people sitting in a boardroom 10 pontificating with things. It is about an 11 actual work in process leading into budgetary 12 allowance and budgetary discussions is the way 13 we would go at this. 14 Q. But there would have to be some - I don't know 15 about pontificating about things, but at least 16 meeting and figuring out, okay, what's our 17 objectives here, how are we going to go about 18 it. There must have been that type of 19 approach taken. 20 A. Those are what I just gave you, panel, it's 21 how do I ensure that this company is in good 22 hands from a human resource standpoint in five 23 and ten years time. I mean, I'd look at 24 engineering staff, I'd look at P & C, 25 Protection and Control, civil, mechanical, I'd</p>	<p>1 the criteria for thinking about this, and 2 that's all laid out and I'm not avoiding your 3 question. If there was a report, we would 4 have filed it. That's the basis. When this 5 request came in - and I talk to my Board on a 6 regular basis with this, Mr. Chairman, 7 regular, every Board meeting I'm talking about 8 are we ready, what's the impact of Muskrat, 9 what's the impact of Vale, are you able to 10 retain, are you losing, and, yes, we're 11 losing, but that's the balance that's fluid, 12 Mr. Johnson, throughout this process. 13 Q. But surely the Board would have said, Mr. 14 Ludlow, you've embarked on this in depth 15 workforce assessment, do you have the results 16 of that assessment that you could share with 17 us. It wouldn't work like that? 18 A. I do not have a management board, Mr. 19 Chairman. I have a governance board. 20 Q. Okay. Well, surely - didn't you have to have 21 some sense of - because you didn't conduct 22 this assessment yourself, correct? 23 A. Correct. 24 Q. And didn't you have to find out, okay, ladies 25 and gentlemen, what did you come up with? How</p>

Page 121	Page 123
<p>1 would you have known?</p> <p>2 A. How I would know would be through regular</p> <p>3 ongoing discussions, debates, with my</p> <p>4 executive team, and that's the reason I have a</p> <p>5 VP Operations. It's not about whether I need</p> <p>6 three line personnel in Stephenville or in</p> <p>7 Port Aux Basques, or whatever. It's about</p> <p>8 where are we going, what's our hot spots, how</p> <p>9 is it working, and that's the basis upon which</p> <p>10 we do, and we run that company on a regular</p> <p>11 basis like that, and, no, it's no more than</p> <p>12 that. I do not take a multi-bound report and</p> <p>13 go through it or even a small report. It's</p> <p>14 not the way it works.</p> <p>15 Q. You don't mean to tell me that when you're</p> <p>16 having these debates and discussions, that</p> <p>17 there would be no paper in terms of what the</p> <p>18 analysis showed or where the numbers are? I</p> <p>19 mean, that can't be, is it, Mr. Ludlow?</p> <p>20 A. I don't like the insinuation of that question,</p> <p>21 Mr. Chairman.</p> <p>22 Q. But it just strikes me as odd that - I mean,</p> <p>23 if you're going to have a meeting and talk</p> <p>24 about results and that sort of thing, I don't</p> <p>25 mean to insinuate, but it just strikes me as</p>	<p>1 and your introduction materials that you</p> <p>2 sponsored spoke of the operating efficiency of</p> <p>3 Newfoundland Power, and we asked the question</p> <p>4 whether you had information on the operating</p> <p>5 efficiency of other Canadian utilities, and in</p> <p>6 reply to CA-NP-143, we were advised that you</p> <p>7 do not have information on the operating</p> <p>8 efficiency of other Canadian utilities. Would</p> <p>9 that be correct?</p> <p>10 (12:45 p.m.)</p> <p>11 A. Let me just check what we're saying here.</p> <p>12 143?</p> <p>13 Q. Yes, sir. The very first line says,</p> <p>14 "Newfoundland Power does not have information</p> <p>15 on the operating efficiency of other Canadian</p> <p>16 utilities".</p> <p>17 A. I agree with that.</p> <p>18 Q. Okay. So, I guess, it's - you can't say then,</p> <p>19 obviously, whether Newfoundland Power is doing</p> <p>20 a good job or not relative to other utilities</p> <p>21 when it comes to operating efficiency. That</p> <p>22 would have to be correct, I take it?</p> <p>23 A. That is correct.</p> <p>24 Q. And at page 224 of your Application at line 12</p> <p>25 and 13, the statement is made that overall</p>
Page 122	Page 124
<p>1 unnatural that there wouldn't be something to</p> <p>2 discuss and say, you know, here's what we came</p> <p>3 up with, but if -</p> <p>4 A. When you asked whether or not there's a memo</p> <p>5 or an email from Gary and I talking back and</p> <p>6 forth, back then there may have been, but that</p> <p>7 does not constitute a report for filing. I</p> <p>8 mean, that's the way we operate. I mean, a</p> <p>9 lot of it is talking, discussion, working. I</p> <p>10 mean, that's the basis upon which we run and</p> <p>11 we always have. Out of that process, we filed</p> <p>12 with our capital budget the whole AMR</p> <p>13 strategy. That AMR strategy removes a fair</p> <p>14 number of positions out of our company by</p> <p>15 2017. That's a formal document, formal report</p> <p>16 filed with this Board, and that's the basis</p> <p>17 upon which we go forward.</p> <p>18 Q. So to sum it up, if you went looking for a</p> <p>19 report in your organization, you would not be</p> <p>20 able to find one arising out of this in depth</p> <p>21 workforce assessment?</p> <p>22 A. We were asked to provide reports that were</p> <p>23 produced from this assessment. If we had</p> <p>24 them, we would have produced them.</p> <p>25 Q. Mr. Ludlow, you spoke of operating efficiency</p>	<p>1 Newfoundland Power's operating costs reflect</p> <p>2 improved labour productivity of approximately</p> <p>3 1 percent per year, and so when we saw that,</p> <p>4 we asked a question in CA-NP-142 referring to</p> <p>5 this line and asking - CA-NP-142. We asked,</p> <p>6 "How do Newfoundland Power's labour cost and</p> <p>7 improved labour productivity compare to</p> <p>8 electric distribution companies elsewhere in</p> <p>9 Canada", and again you indicated Newfoundland</p> <p>10 Power does not have data with which to make</p> <p>11 the comparison requested, right?</p> <p>12 A. Correct.</p> <p>13 Q. And so again we logically then don't know - we</p> <p>14 don't have a relative basis to look at your</p> <p>15 efficiency at Newfoundland Power. That's the</p> <p>16 bottom line, right?</p> <p>17 A. I think the statement on 12 and 13 is very</p> <p>18 clear, Mr. Chairman, and says that our</p> <p>19 improved labour productivity of approximately</p> <p>20 1 percent per year is not a relative or a</p> <p>21 comparator, and I don't know if that's your</p> <p>22 point.</p> <p>23 Q. Yeah.</p> <p>24 A. It's more about the way we look at it and</p> <p>25 benchmark, and what we've been trying to do to</p>

Page 125	Page 127
<p>1 continuously improve on our operating expense</p> <p>2 lines.</p> <p>3 Q. And even - is there no effort to compare</p> <p>4 baselines, for instance, with your other</p> <p>5 sister utilities, for instance, if you're all</p> <p>6 part of the one family?</p> <p>7 A. Some time back we looked at some of these</p> <p>8 comparators. My goodness - unless it's me as</p> <p>9 an individual who's working on utilities, it</p> <p>10 gets so convoluted as to where things are</p> <p>11 charged, how is it charged, how things are</p> <p>12 actually run, that they become meaningless.</p> <p>13 One of the RFIs, I think it's 243 here, we</p> <p>14 talk about some of the matrix we look at like</p> <p>15 SAIFI and SAIDI, we'll look at a safety</p> <p>16 statistics, but they're driven on a national</p> <p>17 basis and we will look at those, but we won't</p> <p>18 draw specifically on those. So, you know, if</p> <p>19 I were to compare myself to Newfoundland and</p> <p>20 Labrador Hydro, two different businesses, two</p> <p>21 different environments. I can look at</p> <p>22 Maritime Electric, two different businesses,</p> <p>23 and that becomes, I think - I'm trying to lay</p> <p>24 out the differentials between companies, and</p> <p>25 that's the reason that - I don't know if there</p>	<p>1 A. Good afternoon.</p> <p>2 Q. I'm sure that you and everybody will be happy</p> <p>3 to hear that my questions are reduced from</p> <p>4 what they were when I started this morning</p> <p>5 because Mr. Johnson did pursue a couple of</p> <p>6 areas where we did have some questions, but I</p> <p>7 still have two or three areas I'd like to</p> <p>8 cover with you. The first one does relate to</p> <p>9 risk, and the risk of Newfoundland Power, and</p> <p>10 that's been covered in detail, I'm not going</p> <p>11 to repeat it at this point, but I did have a</p> <p>12 couple of follow-up questions with respect to</p> <p>13 your discussion with Mr. Johnson about risk.</p> <p>14 I believe that you have confirmed that in</p> <p>15 Newfoundland Power's view, you are an average</p> <p>16 risk Canadian utility as found by the Board in</p> <p>17 the last rate case, is that correct?</p> <p>18 A. That is correct.</p> <p>19 Q. And in your opinion, there's been no material</p> <p>20 change in the risk that Newfoundland Power</p> <p>21 faces since the last rate case?</p> <p>22 A. That is correct.</p> <p>23 Q. In terms of stating that Newfoundland Power is</p> <p>24 an average risk utility, it does imply that</p> <p>25 usually there would be somebody higher and</p>
Page 126	Page 128
<p>1 out there. We haven't got them and we don't</p> <p>2 use them, or I do not compare myself to BC.</p> <p>3 Example, BC runs a fully defined - full</p> <p>4 fledged defined benefit pension plan. We do</p> <p>5 not. It closed in 2003/2004. So what's our</p> <p>6 comparators. There's a million anomalies in</p> <p>7 all these little companies that you get into,</p> <p>8 and that's the reason, Mr. Johnson, we don't</p> <p>9 do it.</p> <p>10 Q. But you compare yourselves to them for return</p> <p>11 on equity?</p> <p>12 A. Because when we look at risk, risk is much</p> <p>13 more global, and we look at the three</p> <p>14 components of that risk, and as I explained -</p> <p>15 you very correctly pointed out the BC piece,</p> <p>16 and we could look at it on that basis, but if</p> <p>17 I get down to operating expense lines, no,</p> <p>18 can't do it.</p> <p>19 MR. JOHNSON:</p> <p>20 Q. I think those are my questions for Mr.</p> <p>21 Ludlow.</p> <p>22 CHAIRMAN:</p> <p>23 Q. Okay.</p> <p>24 MR. EARL LUDLOW - EXAMINATION BY MAUREEN GREENE, Q.C.:</p> <p>25 Q. Good afternoon, Mr. Ludlow.</p>	<p>1 somebody lower if you are average, and I</p> <p>2 wanted to explore that a little bit with you.</p> <p>3 In response to questions from the Consumer</p> <p>4 Advocate with respect to how Fortis BC, for</p> <p>5 example, I believe in your answer you said</p> <p>6 it's the total risk that should be looked at,</p> <p>7 which is the business risk, the financial</p> <p>8 risk, and the regulatory risk. So I do agree</p> <p>9 you do consider all of those, and I did want</p> <p>10 to talk to you about that in terms of the</p> <p>11 total risk and I'm talking about all of those</p> <p>12 as the total package. So Newfoundland Power</p> <p>13 is an average risk utility, I believe, is the</p> <p>14 position of Newfoundland Power, and I'm only</p> <p>15 talking Canadian utilities for this</p> <p>16 discussion, and I believe you agreed that</p> <p>17 Fortis BC could also be considered to be an</p> <p>18 average risk Canadian utility, is that</p> <p>19 correct?</p> <p>20 A. That's correct.</p> <p>21 Q. I want to explore from your perspective as</p> <p>22 CEO, and with your experience as you've</p> <p>23 already outlined for us in four other</p> <p>24 provinces, from your perspective looking at</p> <p>25 that total risk package, what Canadian utility</p>

Page 129	Page 131
<p>1 would you consider to be higher than average</p> <p>2 risk?</p> <p>3 A. I've thought about that question and that's</p> <p>4 the one I struggled with because I'm</p> <p>5 struggling to find one that's lower or above</p> <p>6 as well, Mr. Chair, and at the risk of</p> <p>7 sounding evasive, I looked at each of them</p> <p>8 individually and the various risk categories</p> <p>9 and instead of trying to weight them and bring</p> <p>10 them up, which I couldn't do, I found it very</p> <p>11 difficult to do it, I found myself pro and con</p> <p>12 on all of them. I look at Nova Scotia Power</p> <p>13 and I look at where their regulatory is and</p> <p>14 their reliability and how it sits. I look at</p> <p>15 Maritime Electric and their dependence upon</p> <p>16 everything from shale gas to nuclear in their</p> <p>17 supply mix, and how that factors in. So to</p> <p>18 say that I would have a specific question of</p> <p>19 one that would be higher and one that would be</p> <p>20 lower, I don't have an answer for your</p> <p>21 question, I'm sorry.</p> <p>22 Q. Is this the type of discussion that's ever</p> <p>23 occurred with the Executive, between yourself</p> <p>24 and your Chief Financial Officer as to who</p> <p>25 your comparators are and who would be</p>	<p>1 Bell to avoid multiple calls, multiple calls.</p> <p>2 I mean, they're responding on their pole</p> <p>3 setting. We're maintaining the 60/40 split.</p> <p>4 The costings and the financial that we put</p> <p>5 forward were within - there's no material</p> <p>6 differences from what was anticipated to where</p> <p>7 we are at this stage. One thing has happened</p> <p>8 in the middle of all this is Aliant has</p> <p>9 embarked on a massive fibre op program, and</p> <p>10 we've taken on a fair amount of third party</p> <p>11 work, and it's obviously billable out to them,</p> <p>12 and that's assisted. So things have gone, I</p> <p>13 would suggest, pretty much as we had</p> <p>14 forecasted in the filings and on the approval</p> <p>15 basis of what we had anticipated.</p> <p>16 Q. With respect to maintenance, and the fact that</p> <p>17 Newfoundland Power performs maintenance for</p> <p>18 the joint use support structures, about a year</p> <p>19 ago it wasn't clear as to how long that</p> <p>20 practice would continue. Has there been any</p> <p>21 further discussions with respect to ongoing</p> <p>22 maintenance beyond the initial period that had</p> <p>23 initially been agreed upon?</p> <p>24 A. I am not - I don't have the detail of where we</p> <p>25 are on it. I know there was a discussion that</p>
Page 130	Page 132
<p>1 considered to be riskier than you?</p> <p>2 A. I have not had that discussion with Ms.</p> <p>3 Perry, but maybe she's had them with different</p> <p>4 agencies. I'm not certain.</p> <p>5 Q. So we can defer that question to Ms. Perry.</p> <p>6 A. Please.</p> <p>7 Q. Turning to an operating question, recently the</p> <p>8 agreement between Newfoundland Power and Bell</p> <p>9 Aliant was approved by the Board for the sale</p> <p>10 of the joint use support structures about a</p> <p>11 year ago, so Newfoundland Power now has more</p> <p>12 than a years experience with the new</p> <p>13 arrangement with respect to the ownership of</p> <p>14 the support structures and the maintenance,</p> <p>15 and what has your experience been since the</p> <p>16 new arrangements became effective?</p> <p>17 A. Well, I guess we're early days, we're into it</p> <p>18 is what I would suggest, a year in now. So</p> <p>19 far, so good. I would suggest a lot of things</p> <p>20 have, I think, gone very well. For example,</p> <p>21 calls that would come in during - I keep going</p> <p>22 back to weather, but normal day to day</p> <p>23 circumstances which come through our call</p> <p>24 centre, we automatically are - our set systems</p> <p>25 in now that they're diverted directly over to</p>	<p>1 we'd keep doing it if we could strike the deal</p> <p>2 with them. Mr. Smith would be more than</p> <p>3 capable of addressing where we are on that at</p> <p>4 this point in time, Ms. Greene.</p> <p>5 GREENE, Q.C.:</p> <p>6 Q. Thank you. Those are all the questions that I</p> <p>7 have.</p> <p>8 (1:00 p.m.)</p> <p>9 MR. EARL LUDLOW - EXAMINATION BY THE CHAIRMAN</p> <p>10 Q. Just a couple of questions on demographics,</p> <p>11 Mr. Ludlow. You said the company projects</p> <p>12 population declines for the next 20 years or</p> <p>13 so.</p> <p>14 A. Yes.</p> <p>15 Q. Is that right?</p> <p>16 A. That is correct, Mr. Chair, yes.</p> <p>17 Q. How do you - what sources do you use for</p> <p>18 making your demographic projections?</p> <p>19 A. We use the Conference Board of Canada as the</p> <p>20 prime source, as we would with any of our -</p> <p>21 pretty much our forecasting, and we temper</p> <p>22 that with anything we can see, but the prime</p> <p>23 is the Conference Board.</p> <p>24 Q. And would you do your own calculations on</p> <p>25 demographics?</p>

Page 133	Page 135
<p>1 A. We have a forecaster, and forecasters by their 2 very nature will do calculations on 3 everything, but we wouldn't go out and be 4 serving customer bases on average ages or 5 anything of that type. I guess the answer 6 would be, no.</p> <p>7 Q. How would you calculate population decline 8 then or growth, what number do you use there, 9 do you know?</p> <p>10 A. The same - population growth - I'm sorry?</p> <p>11 Q. Well, like, I've read on demographics, you 12 know, to keep your population stable, you need 13 a reproductive ratio of 2.1.</p> <p>14 A. 2.1.</p> <p>15 Q. Newfoundland, I think now is at -</p> <p>16 A. 1.4, I do believe, Mr. Chair.</p> <p>17 Q. 1.4 or 1.3, I read. So what number are you 18 using? Are you using 1.4, for instance?</p> <p>19 A. Again I don't know, but we would be using 20 probably a much higher level number than that, 21 looking at what's being said and forecasted by 22 the forecasters, you know, on total base, and 23 if they're using 1.4, and whether that's going 24 to increase, I don't know, but again the 25 average age is increasing as well, so - I</p>	<p>1 Q. Which means we've got approximately one 2 service for every two people in the province, 3 say, 500,000?</p> <p>4 A. Pretty much.</p> <p>5 Q. How's that likely to change with the 6 demographics? Do you have any information on 7 that?</p> <p>8 A. Well, anecdotally, Mr. Chair, I think the way 9 I would look at that is a lot of these homes 10 in a lot of the smaller communities are older 11 homes, and I'm going to be a pessimist, I'm 12 from rural Newfoundland, proud of it, and I 13 will say that as I look out and look at the 14 future of rural Newfoundland, unless something 15 happens, a lot of those older houses are not 16 going to be maintained. I'm looking 20 years. 17 I don't want to be a fear-monger. I'm being 18 very careful of that because, you know, I look 19 at the place I come from, they've registered 20 something like a 12 percent decline in 21 population since the last census. Not the 22 community, but the general area.</p> <p>23 Q. Because I understand that one of the things, I 24 mean, in this forecasting business is - if you 25 know anything about forecasting, it's pretty</p>
Page 134	Page 136
<p>1 would think that would come right from the 2 Conference Board, Mr. Chairman.</p> <p>3 Q. Have you filed any numbers about what you 4 expect with the Board over the next 20 years?</p> <p>5 A. I think we have given an indication of what we 6 would expect to see regarding percentage drop 7 in population of Newfoundland and Labrador. 8 It's a - tangle is an awful word, but we're 9 seeing an average increase and a decline in 10 some areas, and a growth in others, and I 11 referenced the urbanization earlier. So what 12 we've got going on is we've got a contraction 13 in some areas. A lot of people still keeping 14 the houses as summer residences. Now pulling 15 into the urban centres of Mount Pearl, St. 16 John's, and I've got to mention my namesake, 17 Paradise, that you're growing the system and 18 pushing a force on the system here; at the 19 same time, trying to maintain that service 20 level in -</p> <p>21 Q. But there's two aspects. There's service 22 levels and there's population. Like, right 23 now, I think you said there's 250,000 24 customers?</p> <p>25 A. Correct, approximately.</p>	<p>1 unreliable after three or four years on 2 anything, but demographics because of the 3 nature of - I mean, demographics you can 4 predict with some accuracy.</p> <p>5 A. One of the scariest things we look at is the 6 age. Even the age cohorts and how things are 7 moving through, there's a graph here that 8 shows the average age and how much it's 9 increasing, and that's probably more 10 concerning or at least equally as concerning 11 because as - let me put it another way. As I 12 get older, and if I live in rural 13 Newfoundland, my call for service and 14 reliability will increase. It's almost like 15 the medical system when you look at it in some 16 way, right, and, you know, as we see that 17 happening - we're trying to keep an eye on it. 18 There's not a lot you can do about it, I 19 guess.</p> <p>20 Q. That's your -</p> <p>21 A. We structure around that, by the way.</p> <p>22 Q. The reproductive ratio would capture that, 23 wouldn't it?</p> <p>24 A. You would think.</p> <p>25 Q. I think Ms. Greene covered off this business</p>

Page 137	Page 139
<p>1 of average risk. You say we got a generally</p> <p>2 supportive regulatory environment. Generally</p> <p>3 means that it's okay, it's not great. I mean,</p> <p>4 generally I'm a pretty nice guy, but some</p> <p>5 people, you know - generally doesn't mean a</p> <p>6 heck of a lot. I mean, what else would you</p> <p>7 think we could do to make the regulatory</p> <p>8 environment more than generally supportive?</p> <p>9 Tell us where we're inadequate. We're not</p> <p>10 sensitive.</p> <p>11 A. I thought we were very positive with generally</p> <p>12 supportive.</p> <p>13 Q. I don't know what generally means there, you</p> <p>14 know.</p> <p>15 A. I guess the point, Mr. Chair, with that is</p> <p>16 compared to other areas, there's differences</p> <p>17 between regulatory regimes.</p> <p>18 Q. Uh-hm.</p> <p>19 A. You know, like - to be quite honest, we've</p> <p>20 structured our business and if you look at the</p> <p>21 Executive structure of my business, you will</p> <p>22 see that I have a Vice President Regulatory</p> <p>23 and he handles IT, and that's seen as an area</p> <p>24 that we bring focus to. We look at it on that</p> <p>25 basis. So our ability to be responsive and</p>	<p>1 today but there's something wrong or there's</p> <p>2 something going on in Europe and its impact</p> <p>3 here. What does that all translate to? We</p> <p>4 talk about infrastructure and governments</p> <p>5 injecting money to markets, I don't believe,</p> <p>6 and this is me as an uninformed engineer</p> <p>7 looking at it, would say the markets haven't</p> <p>8 been able to be a market, there's a lot of</p> <p>9 influences out there, all over. The</p> <p>10 volatility is all over the place. Bond yields</p> <p>11 are down to 2.39. I think the last time we</p> <p>12 were here they were 4, and we said they'll</p> <p>13 never go to 2.</p> <p>14 Q. You've given no indication, sir, that you're</p> <p>15 uninformed, but how do you think capital</p> <p>16 markets are going to get back to normal?</p> <p>17 A. That's going to be the big question.</p> <p>18 Q. Because you could make a pile of money if you</p> <p>19 knew that one.</p> <p>20 A. I wouldn't be here.</p> <p>21 Q. We could all retire.</p> <p>22 A. Yes.</p> <p>23 Q. Maybe we'll leave it for Mr. Booth. The only</p> <p>24 other question I had is on this recurrent</p> <p>25 issue of Executive compensation. You quoted</p>
Page 138	Page 140
<p>1 meet deadlines and work with the Board, that's</p> <p>2 something we take very seriously. Now in</p> <p>3 there, there are rulings that are different</p> <p>4 here than they would be out west. Am I</p> <p>5 looking for something else; no, I'm just</p> <p>6 saying they're different. Like, the excess</p> <p>7 earnings account, we're hearing numbers here</p> <p>8 of Alberta earning 8.75. That's their</p> <p>9 allowed. We don't know what they're going to</p> <p>10 earn because they might earn nine and a</p> <p>11 quarter or nine and a half. I know that I've</p> <p>12 got a 40 basis point spread on my allowed ROE.</p> <p>13 If I go above that, it goes into an excess</p> <p>14 earnings account. Now am I knocking that;</p> <p>15 it's just the basis under which I run.</p> <p>16 Q. Uh-hm. I guess, on this business of capital</p> <p>17 markets, we can leave that to your CFO, but</p> <p>18 you said capital markets have not been normal</p> <p>19 and I was wondering when is the last time you</p> <p>20 thought they were normal?</p> <p>21 A. I would go back to 2007, early 2008.</p> <p>22 Q. Before the bailouts?</p> <p>23 A. Yeah, and, you know, I thought long and hard</p> <p>24 about that, not anticipating your question,</p> <p>25 but, you know, you can't pick up the paper</p>	<p>1 HAY. HAY is pretty well accepted across the</p> <p>2 country as one of the major companies with</p> <p>3 respect to this whole compensation issue. I</p> <p>4 think you said that you're at the 50</p> <p>5 percentile. So in the survey that HAY did for</p> <p>6 your company, half the company's paid more,</p> <p>7 half paid less. Is that the way that would</p> <p>8 work?</p> <p>9 A. There's a policy line set and where the policy</p> <p>10 line, Mr. Chairman, is set to is a group of</p> <p>11 companies called the Canadian Commercial</p> <p>12 Industrial, and there's been a policy line set</p> <p>13 by our Board that we would target 50 percent</p> <p>14 of that grouping, and that was the basis, not</p> <p>15 of all companies, but of that particular group</p> <p>16 of companies. So that was the adjustment that</p> <p>17 was made to the STI portion for the Executive</p> <p>18 members to bring that a little closer in line.</p> <p>19 Q. Uh-hm.</p> <p>20 A. And that's the basis. Like, that policy may</p> <p>21 move by the markets moving a bit, but the</p> <p>22 policy line was set on that grouping.</p> <p>23 Q. That would be total compensation, would it?</p> <p>24 It wouldn't be compensation paid for by rate</p> <p>25 payers, it would be total compensation?</p>

<p style="text-align: right;">Page 141</p> <p>1 A. It would look at total compensation, that is</p> <p>2 correct, and it would look at cash and</p> <p>3 indirect -</p> <p>4 Q. And in that calculation, would there be a</p> <p>5 comparison between total compensation and</p> <p>6 compensation paid by rate payers? Is there a</p> <p>7 ratio there that - in other words, I guess I'm</p> <p>8 asking you in your total compensation compared</p> <p>9 to your study group or the control group, are</p> <p>10 you - are the rate payers in Newfoundland</p> <p>11 paying more than, say, the average in the</p> <p>12 group? Are we at 50 percent in terms of</p> <p>13 contributions from rate payers to your</p> <p>14 Executive compensation?</p> <p>15 A. That would not be in or part of this study,</p> <p>16 and again this could range, Mr. Chairman, from</p> <p>17 - just any kind of a company is what's in</p> <p>18 there. You know, it's not just electricians, it</p> <p>19 could be - I don't think retailers. Retailers</p> <p>20 might be in there - there's other companies in</p> <p>21 that mix. So your answer is, I do not have</p> <p>22 that visibility from HAY at all.</p> <p>23 Q. Uh-hm. I think what would concern the Board</p> <p>24 is what percentage of your compensation is</p> <p>25 paid for through rates, and what the</p>	<p style="text-align: right;">Page 143</p> <p>1 on or adjourn? I mean, what do you think.</p> <p>2 MS. GLYNN:</p> <p>3 Q. Can we just go off the record?</p> <p>4 CHAIRMAN:</p> <p>5 Q. Yes, go off the record.</p> <p>6 (OFF RECORD)</p> <p>7 (1:23 p.m.)</p> <p>8 CHAIRMAN:</p> <p>9 Q. I understand we're going to deal with our next</p> <p>10 witness.</p> <p>11 KELLY, Q.C.:</p> <p>12 Q. Press ahead, Mr. Chairman.</p> <p>13 CHAIRMAN:</p> <p>14 Q. Press ahead. Generally forecasts are</p> <p>15 reliable, but we don't know.</p> <p>16 KELLY, Q.C.:</p> <p>17 Q. The consensus forecast is we'll go through Ms.</p> <p>18 Perry's evidence in chief.</p> <p>19 THE CHAIRMAN:</p> <p>20 Q. And I also understand that if the weather</p> <p>21 doesn't materialize, we will convene tomorrow.</p> <p>22 Has everybody agreed to that?</p> <p>23 KELLY, Q.C.:</p> <p>24 Q. I'm agreeable.</p> <p>25 MR. JOHNSON:</p>
<p style="text-align: right;">Page 142</p> <p>1 shareholders decide to do for you people is</p> <p>2 entirely up to them, I would presume.</p> <p>3 A. Well that's -</p> <p>4 CHAIRMAN:</p> <p>5 Q. Okay, let me just--I think that is all that I</p> <p>6 have. So we're finishing up a little bit</p> <p>7 early. Do you want to adjourn for the day, or</p> <p>8 do you want to try and get our CFO going.</p> <p>9 What do you want to do?</p> <p>10 KELLY, Q.C.:</p> <p>11 Q. Perhaps if we're finished with the witness,</p> <p>12 the witness can -</p> <p>13 CHAIRMAN:</p> <p>14 Q. Oh, yeah, I'm going to dismiss him. I mean,</p> <p>15 we're finished with you. I don't think</p> <p>16 there's anything else.</p> <p>17 KELLY, Q.C.:</p> <p>18 Q. Then we could perhaps have a quick</p> <p>19 conversation as to the timing. I take it the</p> <p>20 Board only intends to sit until 1:30, in any</p> <p>21 event, Mr. Chairman. It wouldn't make sense</p> <p>22 to start on that basis.</p> <p>23 CHAIRMAN:</p> <p>24 Q. Look, I'm - I mean, I'm easy. I don't know -</p> <p>25 what do you want to do, do you want to carry</p>	<p style="text-align: right;">Page 144</p> <p>1 Q. Yes.</p> <p>2 CHAIRMAN:</p> <p>3 Q. So we'll see what it's like at, say, 8 o'clock</p> <p>4 in the morning, something like that, is that</p> <p>5 all right?</p> <p>6 MR. JOHNSON:</p> <p>7 Q. It's kind of like calling the Regatta, Mr.</p> <p>8 Chair.</p> <p>9 CHAIRMAN:</p> <p>10 Q. It's like calling the Regatta. So tomorrow it</p> <p>11 depends on the wind, boy. Madame, do you</p> <p>12 swear to tell the truth, the whole truth, and</p> <p>13 nothing but the truth, so help you God.</p> <p>14 MS. PERRY:</p> <p>15 Q. I do.</p> <p>16 MS. JOCELYN PERRY (SWORN) EXAMINATION-IN-CHIEF BY KELLY,</p> <p>17 Q.C.:</p> <p>18 Q. Thank you, Mr. Chairman. Ms. Perry, you are</p> <p>19 the Vice President of Finance and Chief</p> <p>20 Financial Officer of Newfoundland Power?</p> <p>21 A. Yes, that's correct. I've held this position</p> <p>22 since 2005.</p> <p>23 Q. And do you adopt Section 3 of the Finance</p> <p>24 testimony and the company's rebuttal evidence</p> <p>25 as your testimony in this matter?</p>

Page 145	Page 147
<p>1 A. Yes.</p> <p>2 Q. Are there any changes you wish to make to any</p> <p>3 of the pre-filed testimony and exhibits?</p> <p>4 A. No, not at this time.</p> <p>5 Q. Now Ms. Perry, we'll go through four matters.</p> <p>6 One is financial performance and financial</p> <p>7 integrity. Two is cost of capital and capital</p> <p>8 structure. Three is the automatic adjustment</p> <p>9 formula, and four is depreciation. We'll talk</p> <p>10 about those four. Let's start with the</p> <p>11 company's financial performance and financial</p> <p>12 integrity. Can you start with that?</p> <p>13 A. Certainly. I'd like to start with a brief</p> <p>14 overview of the financial performance since</p> <p>15 the last rate case. If we could please go to</p> <p>16 page 1 of Exhibit 3. This exhibit includes</p> <p>17 the company's actual financial results for</p> <p>18 2011 - 2010 and 2011, and the most current</p> <p>19 financial forecast for 2012, 2013, and 2014.</p> <p>20 Let's look at the first two columns which are</p> <p>21 the actual results for 2010 and 2011. On line</p> <p>22 35, you'll see that our rate of return on</p> <p>23 equity was 9.21 percent for 2010, and 9</p> <p>24 percent for 2011. In both those years, we</p> <p>25 were within our allowed range of return. So</p>	<p>1 will not have an opportunity to earn a</p> <p>2 reasonable return in either year. Lines 37</p> <p>3 through 39, they contain the key credit matrix</p> <p>4 that flow out of these returns. You'll note</p> <p>5 that all key matrix are forecast to erode from</p> <p>6 where they are today, and these financial</p> <p>7 results are not consistent with the</p> <p>8 maintenance of the company's financial</p> <p>9 integrity.</p> <p>10 Q. Next can you please comment on Newfoundland</p> <p>11 Power's creditworthiness?</p> <p>12 A. Newfoundland Power continues to be</p> <p>13 creditworthy. Our first mortgage bonds are</p> <p>14 rated A by DBRS, and A2 by Moody's Investor</p> <p>15 Services. These ratings have not changed</p> <p>16 since our last general rate order. Both DBRS</p> <p>17 and Moody's recognize that Newfoundland</p> <p>18 Power's creditworthiness is dependent upon</p> <p>19 decision making by this Board. Moody's latest</p> <p>20 exhibit, latest report, I believe Chris is</p> <p>21 going to bring up on the screen - last page.</p> <p>22 Okay, right here, Moody's latest report</p> <p>23 indicates that the company's rating would</p> <p>24 likely be downgraded if we perceived a</p> <p>25 meaningful reduction in the level of</p>
Page 146	Page 148
<p>1 now moving on to the third column, this is our</p> <p>2 2012 forecast. Newfoundland Power's 2012 rate</p> <p>3 of return on rate base is set based on a</p> <p>4 return on equity of 8.8 percent. As you can</p> <p>5 see from line 35 again, we are forecasting a</p> <p>6 return on equity of 8.81 percent. At line 37,</p> <p>7 our interest coverage is 2.3 times. At line</p> <p>8 38, our cash flow interest coverage is 3. 2</p> <p>9 times, and on line 39, our cash flow to debt</p> <p>10 is 15.7 percent. While our 2012 matrix are</p> <p>11 consistent with maintaining Newfoundland</p> <p>12 Power's financial integrity, as you can see</p> <p>13 they have deteriorated since 2010.</p> <p>14 Q. Next would you provide the Board with an</p> <p>15 overview of Newfoundland Power's financial</p> <p>16 outlook for 2013 and 2014?</p> <p>17 A. Yes. The 2013 and 2014 forecast are shown in</p> <p>18 the last two columns on this exhibit. The</p> <p>19 2013 and 2014 forecasts excludes the proposals</p> <p>20 in this Application, and is based on the 8. 38</p> <p>21 percent cost of equity currently in customer</p> <p>22 rates. So moving down to line 35 again, the</p> <p>23 forecasted return on equity is 7.57 in 2013,</p> <p>24 and 6.89 percent in 2014. So based on the</p> <p>25 current financial outlook, Newfoundland Power</p>	<p>1 regulatory support combined with weaker</p> <p>2 liquidity and a sustained deterioration in the</p> <p>3 company's financial matrix.</p> <p>4 (1:30 p.m.)</p> <p>5 KELLY, Q.C.:</p> <p>6 Q. What do credit rating agencies consider as</p> <p>7 regulatory support?</p> <p>8 A. Credit rating agencies typically look to</p> <p>9 predictability and Board decision making, and</p> <p>10 Newfoundland Power's opportunity to recover</p> <p>11 its cost in a timely manner, and earn its</p> <p>12 return as the key components of regulatory</p> <p>13 support. As an example, the company's 45</p> <p>14 percent common equity ratio has consistently</p> <p>15 been singled out by credit rating agencies as</p> <p>16 a financial strength. The maintenance of this</p> <p>17 ratio is a prominent feature of this Board's</p> <p>18 regulatory support of the company's financial</p> <p>19 integrity.</p> <p>20 Q. Could this Application have implications for</p> <p>21 the company's future creditworthiness?</p> <p>22 A. Yes, it could. When I consider the combined</p> <p>23 proposals as put forward by the consumer</p> <p>24 advocate, which include; one, a reduction in</p> <p>25 the equity capital structure from 45 percent</p>

Page 149	Page 151
<p>1 to 40 percent; two, a reduction in the return</p> <p>2 on equity to 7.5 percent; three, a decrease in</p> <p>3 accrued depreciation recovery of approximately</p> <p>4 10 million per year, I do have serious</p> <p>5 concerns about a downgrade in the company's</p> <p>6 credit rating.</p> <p>7 Q. Let's discuss capital structure first. Can</p> <p>8 you explain to the Board the practical effects</p> <p>9 of changing the capital structure for</p> <p>10 Newfoundland Power?</p> <p>11 A. Yes. Well, a reduction in the common equity</p> <p>12 by 5 percent would have significant</p> <p>13 consequences for the company. First of all,</p> <p>14 it would prompt a capital divided payout of</p> <p>15 approximately 42 million dollars. That amount</p> <p>16 would have to be borrowed and Newfoundland</p> <p>17 Power's financial risk would increase, and its</p> <p>18 matrix would again decrease. Second, and</p> <p>19 equally important, such a change could lead to</p> <p>20 a reevaluation of the regulatory support as</p> <p>21 perceived by the credit rating agencies. This</p> <p>22 could lead to a reduction in Newfoundland</p> <p>23 Power's current credit ratings in these</p> <p>24 circumstances.</p> <p>25 Q. Now I want to take you to a piece of Dr.</p>	<p>1 to respect that the determination of whether</p> <p>2 returns are fair or not rests with the utility</p> <p>3 regulators, but the returns allowed by</p> <p>4 regulators affect the financial matrix. So</p> <p>5 allowed returns are, therefore, relevant to</p> <p>6 the credit rating agencies assessment of our</p> <p>7 creditworthiness. The return provides a</p> <p>8 margin of safety for debt holders that</p> <p>9 interest will be paid in the future. So for</p> <p>10 this very reason, a reduced return could very</p> <p>11 well impact the company's creditworthiness.</p> <p>12 Q. I want to take you next to Dr. Booth's</p> <p>13 evidence at page 90, lines 20 and 21, and Dr.</p> <p>14 Booth has indicated that Moody's has implied</p> <p>15 that a lower allowed ROE is warranted for</p> <p>16 Newfoundland Power because of its 45 percent</p> <p>17 common equity ratio. Has Moody's ever</p> <p>18 indicated that to you?</p> <p>19 A. No. I speak or meet with each credit rating</p> <p>20 agency two or three times each year. Neither</p> <p>21 Moody's nor DBRS has ever indicated that</p> <p>22 Newfoundland Power's allowed ROE should be</p> <p>23 lower because of its capital structure. I</p> <p>24 would be surprised if Moody's or DBRS were to</p> <p>25 indicate an appropriate level of ROE for</p>
Page 150	Page 152
<p>1 Booth's evidence. He's proposed, if we go to</p> <p>2 page 80, at lines 11 to 12, that Newfoundland</p> <p>3 Power's 45 percent common equity ratio be</p> <p>4 reduced to 40 percent, and the 5 percent be</p> <p>5 replaced with retractable preferred shares.</p> <p>6 Do you agree with that proposal?</p> <p>7 A. No, I do not.</p> <p>8 Q. Could you explain to the Board why not?</p> <p>9 A. Well, Newfoundland Power is a small issuer in</p> <p>10 the financial markets. I seriously doubt that</p> <p>11 we could issue retractable preference shares,</p> <p>12 and if we could, what the cost might be.</p> <p>13 Second, retractable preference shares would</p> <p>14 likely be considered debt by the credit rating</p> <p>15 agencies. The preference shares would not be</p> <p>16 assigned any equity value for the purpose of</p> <p>17 assessing Newfoundland Power's credit rating.</p> <p>18 So from a credit rating perspective, issuing</p> <p>19 42 million in retractable preference shares</p> <p>20 would be the same as issuing 42 million in</p> <p>21 additional debt.</p> <p>22 Q. Let's turn next to the return on equity. Do</p> <p>23 credit rating agencies typically assess</p> <p>24 whether the allowed utility returns are fair?</p> <p>25 A. Not directly. Credit rating agencies appear</p>	<p>1 Newfoundland Power one way or the other. What</p> <p>2 Moody's has indicated quite clearly is that</p> <p>3 Newfoundland Power's financial matrix are</p> <p>4 somewhat weaker than those of its peers, which</p> <p>5 they state are Fortis Alberta, Connecticut</p> <p>6 Light and Power, Orange and Rockland Utilities</p> <p>7 in New York, and Public Service Electric and</p> <p>8 Gas in New Jersey, and as I mentioned earlier,</p> <p>9 Moody's has quite clearly indicated that</p> <p>10 sustained deterioration in the company's</p> <p>11 financial matrix could result in a ratings</p> <p>12 downgrade.</p> <p>13 Q. Does the 2013 return on equity of 7.5 percent</p> <p>14 as recommended by Dr. Booth appear fair to</p> <p>15 you?</p> <p>16 A. No.</p> <p>17 Q. Explain to the Board why not?</p> <p>18 A. The 7.5 percent return on equity recommended</p> <p>19 by Dr. Booth is significantly below the return</p> <p>20 of any investor owned electric utility in</p> <p>21 North America. It is less than the 7.85</p> <p>22 percent return on equity indicated by the</p> <p>23 formula for 2012, which led to the suspension</p> <p>24 of the formula, and it's also not materially</p> <p>25 different than the 7.53 percent return on</p>

Page 153	Page 155
<p>1 equity indicated by the formula for 2013. A</p> <p>2 7.5 percent return on equity is simply not</p> <p>3 fair to Newfoundland Power. We have filed</p> <p>4 expert reports from Ms. McShane and Dr.</p> <p>5 Vanderweide that consider an appropriate</p> <p>6 return on equity for Newfoundland Power.</p> <p>7 Q. Now I want to turn a little bit to the</p> <p>8 automatic adjustment formula. Can you explain</p> <p>9 to the Board the effect on Newfoundland Power</p> <p>10 of the continuation of the automatic</p> <p>11 adjustment formula since the 2009 hearing?</p> <p>12 A. Yes. I understand the purpose of the formula</p> <p>13 was to set a fair return on equity between</p> <p>14 test years. This was intended to provide for</p> <p>15 regulatory efficiencies, which in turn would</p> <p>16 reduce cost associated with these proceedings.</p> <p>17 Since 2009, this has not been the result. As</p> <p>18 previously stated by Mr. Ludlow, the</p> <p>19 experience has been that the formula has</p> <p>20 produced unfair returns and increased</p> <p>21 regulatory process, taking considerable time</p> <p>22 and resources away from the daily operations</p> <p>23 of Newfoundland Power.</p> <p>24 Q. In 2011, the formula indicated an estimated</p> <p>25 return on equity of 8.38 percent. Why didn't</p>	<p>1 capital so soon after the last examination</p> <p>2 factored into the company's mind set.</p> <p>3 Finally, the 8.38 percent was the result of</p> <p>4 financial market conditions reducing forecast</p> <p>5 long Canada Bond yields. Given the degree of</p> <p>6 volatility in the financial markets at that</p> <p>7 time, Newfoundland Power was mindful that long</p> <p>8 Canada Bond yields could increase by the time</p> <p>9 the formula operated again. So all of these</p> <p>10 considerations influenced the company's</p> <p>11 decision in November, 2010, not to apply to</p> <p>12 suspend the operation of the formula in 2011.</p> <p>13 Q. Now in this hearing, Newfoundland Power is</p> <p>14 proposing that operation of the automatic</p> <p>15 adjustment formula be discontinued. Would you</p> <p>16 please explain why?</p> <p>17 A. Well, I think we all agree the existing</p> <p>18 formula is not working in current financial</p> <p>19 market conditions. The formula has not</p> <p>20 produced fair returns and has increased the</p> <p>21 regulatory process. The modified formulas</p> <p>22 which currently exist in Canada take into</p> <p>23 account both the change in long Canada Bond</p> <p>24 yields and the change in spreads between</p> <p>25 utility and long Canada Bond yields. The</p>
Page 154	Page 156
<p>1 Newfoundland Power seek to suspend the</p> <p>2 operation of the formula for 2011?</p> <p>3 A. Well, first of all, Newfoundland Power did not</p> <p>4 think the 8.38 percent return on equity in</p> <p>5 2011 was a fair return. It was significantly</p> <p>6 lower than the returns of other investor owned</p> <p>7 utilities. Newfoundland Power chose, however,</p> <p>8 not to seek to suspend operation of the</p> <p>9 formula for 2011 for a number of reasons.</p> <p>10 Most notably, in late 2010, Newfoundland Power</p> <p>11 was negotiating the terms of the Bell Aliant</p> <p>12 repurchase of the joint use support structures</p> <p>13 pursuant to a 2001 agreement. The negotiated</p> <p>14 terms of the repurchase would have affected</p> <p>15 the company's rate base and future cash flows.</p> <p>16 So this created a significant degree of</p> <p>17 uncertainty in the company's financial</p> <p>18 outlook. Newfoundland Power chose instead to</p> <p>19 focus on managing this project and the</p> <p>20 financial uncertainty associated with it. The</p> <p>21 company also considered the fact that a</p> <p>22 November 2010 Application would have been</p> <p>23 filed approximately 11 months after the</p> <p>24 Board's decision in 2009. The expense</p> <p>25 associated with a full review of the cost of</p>	<p>1 addition of the spread is an attempt to limit</p> <p>2 the exposure to changes in long Canada Bond</p> <p>3 yields. So generally speaking, I simply have</p> <p>4 no confidence that the formula or either of</p> <p>5 the modified formulas would result in a fair</p> <p>6 return for Newfoundland Power in current</p> <p>7 financial market conditions.</p> <p>8 Q. We have two proposals that have been put</p> <p>9 forward here; Mr. MacDonald's and Dr.</p> <p>10 Booth's. So would you please comment on the</p> <p>11 operation of modified formulas as proposed by</p> <p>12 each of Mr. MacDonald and Dr. Booth, please?</p> <p>13 A. Yes. While neither Mr. MacDonald nor Dr.</p> <p>14 Booth has provided full details on a proposed</p> <p>15 formula, I did attempt a pro forma analysis of</p> <p>16 how these formulas might operate. Let me say</p> <p>17 to you first that as a fundamental principle,</p> <p>18 a formula should produce a change in the ROE</p> <p>19 if there has been a change in circumstance.</p> <p>20 If conditions haven't changed, the ROE should</p> <p>21 remain the same. So now let's take a look at</p> <p>22 Mr. MacDonald's proposed formula first. If we</p> <p>23 could display Exhibit JP #1, please.</p> <p>24 Q. We pre-filed that as marked.</p> <p>25 MS. GLYNN:</p>

Page 157	Page 159
<p>1 Q. And we'll enter that into the record. Thank</p> <p>2 you.</p> <p>3 KELLY, Q.C.:</p> <p>4 Q. Thank you.</p> <p>5 A. So for this pro forma analysis, I have assumed</p> <p>6 the financial markets remain the same. This</p> <p>7 exhibit simply shows the pro forma operation</p> <p>8 of the formula to estimate the 2014 return on</p> <p>9 equity based on that assumption. So first</p> <p>10 we'll start on line 4 with the 2013 return on</p> <p>11 common equity of 8.91 percent as proposed by</p> <p>12 Mr. MacDonald, and this return assumes a risk</p> <p>13 free rate of 3.04. Next Mr. MacDonald proposes</p> <p>14 the return on equity be adjusted by 50 percent</p> <p>15 of the change in long Canada Bond yields, and</p> <p>16 this starts on line 6. Assuming the financial</p> <p>17 markets remain unchanged, the long Canada Bond</p> <p>18 consensus forecast is 2.59 percent, and this</p> <p>19 was based on the November, 2012 consensus</p> <p>20 formula and - that consensus forecast, and</p> <p>21 that's essentially the same as what it is</p> <p>22 today, and this can be found on line 7. On</p> <p>23 line 8, the base forecast for long Canada Bond</p> <p>24 yield proposed by Mr. MacDonald again is</p> <p>25 3.04. So the 0.23 percent reduction on line</p>	<p>1 in forecast long Canada Bond yields would not</p> <p>2 result in an increase in Newfoundland Power's</p> <p>3 return on equity. We would still be under Mr.</p> <p>4 MacDonald's deadband. So the formula appears</p> <p>5 unbalanced. Based on the pro forma analysis,</p> <p>6 the difficulties we've just discussed are a</p> <p>7 direct result of the parameters used in the</p> <p>8 formula.</p> <p>9 Q. Thank you. Can you go next to Dr. Booth's</p> <p>10 proposed formula and take us through that one?</p> <p>11 A. Yes. Despite apparent similarities between</p> <p>12 Dr. Booth's proposed formula and Mr.</p> <p>13 MacDonald's, the operation of the two formulas</p> <p>14 is quite different. If we could go to Exhibit</p> <p>15 JP #2, and we can discuss Dr. Booth's</p> <p>16 proposed formula.</p> <p>17 MS. GLYNN:</p> <p>18 Q. And we'll enter that one into the record as</p> <p>19 well. Thank you.</p> <p>20 (1:45 p.m.)</p> <p>21 KELLY, Q.C.:</p> <p>22 Q. Thank you. So again starting on line 4, we</p> <p>23 start with the return on equity of 7.5 percent</p> <p>24 as proposed by Dr. Booth. This proposed</p> <p>25 return on equity assumes a 3.8 percent risk</p>
Page 158	Page 160
<p>1 11 is the difference between the 2.59 percent</p> <p>2 and the 3.04 percent multiplied by 50 percent.</p> <p>3 Next the proposed formula adjusts the return</p> <p>4 on equity by 50 percent of the change in the</p> <p>5 utility bond spread, and as I mentioned</p> <p>6 earlier, the utility bond spread is the</p> <p>7 difference between utility bond yields on 30</p> <p>8 year A rated utility bonds, and long Canada</p> <p>9 Bond yields. Mr. MacDonald does not specify</p> <p>10 the base or the starting utility bond spread</p> <p>11 to incorporate in the formula. So I've made</p> <p>12 the assumption that the base utility bond</p> <p>13 spread is the current spread of 1.45 percent.</p> <p>14 With no change in utility bond spread, no</p> <p>15 adjustment is required to the return on equity</p> <p>16 for this component. So moving down to line</p> <p>17 21, the 2014 estimated return on equity is</p> <p>18 8.68 percent. This would be the 8.91 percent,</p> <p>19 less the .23 percent as indicated on line 11.</p> <p>20 The .23 percent reduction would technically</p> <p>21 fall within Mr. MacDonald's proposed 25 basis</p> <p>22 point deadband, but you'll note that if long</p> <p>23 Canada Bond yields fell by 6 basis points, our</p> <p>24 return would drop by more than .25 percent.</p> <p>25 On the other hand, a 75 basis point increase</p>	<p>1 free rate. On line 6, Dr. Booth proposes the</p> <p>2 return on equity be adjusted by 75 percent of</p> <p>3 the change in long Canada Bond yields above</p> <p>4 the 3.8 percent. My understanding of Dr.</p> <p>5 Booth's evidence is the 3.8 percent is viewed</p> <p>6 as a floor to be applied in this formula. So</p> <p>7 assuming the financial markets remain</p> <p>8 unchanged, the long Canada Bond forecast is</p> <p>9 2.59 percent, and that's the same as Mr.</p> <p>10 MacDonald's formula, and this can be found on</p> <p>11 line 7. Given the current long Canada Bond</p> <p>12 forecast is below the 3.8 percent indicated by</p> <p>13 Dr. Booth, no adjustment is required to the</p> <p>14 return on equity for this component. Next the</p> <p>15 proposed formula adjust the return on equity</p> <p>16 by 50 percent of the change in the utility</p> <p>17 bond spread. This is the same as Mr.</p> <p>18 MacDonald's proposed formula as well.</p> <p>19 However, in Dr. Booth's evidence, the base or</p> <p>20 the starting utility bond spread to</p> <p>21 incorporate in the formula was based on the</p> <p>22 Scotia Capital Bond Index, and the base</p> <p>23 utility bond spread referenced by Dr. Booth</p> <p>24 was 1.8 percent. However, when I looked at a</p> <p>25 number of answers to requests for information,</p>

Page 161	Page 163
<p>1 my understanding is Dr. Booth agrees with 2 using the Bloomberg 30 year A rated utility 3 index, and this again is consistent with Mr. 4 MacDonald's formula. So going to lines 15 and 5 16, the current and base utility bond spread 6 is 1.45 percent. With no change in the 7 utility bond spread, no adjustment is required 8 for this component. So moving down to line 9 21, the 2014 estimated return on equity is 7.5 10 percent. So based on how I interpret Dr. 11 Booth's formula, there will be no change in 12 Newfoundland Power's 2014 return on equity if 13 financial markets remain the same. However, 14 given Dr. Booth applies a 3.8 percent floor on 15 the long Canada Bond yields at a time when the 16 forecast is 2.59 percent, the yield forecast 17 would have to increase by more than 1.2 18 percent before the formula would signal an 19 increase in the company's cost of equity for 20 changes in long Canada Bond yields, and it 21 would be reasonable to assume that the utility 22 bond spread would decline if long Canada Bond 23 yields were to increase by that amount. So, 24 therefore, the operation of the formula could 25 signal a reduction in Newfoundland Power's</p>	<p>1 advocate's depreciation proposals include the 2 transfer of approximately 70 million dollars 3 net of tax that has been collected from 4 customers in the past to the customers in the 5 future. Transferring such a large cost to 6 future customers causes me concern. This 7 amount will have to collected from customers 8 at some point in the future as Newfoundland 9 Power's costs are not changing. The proposals 10 have the short effect of reducing annual 11 depreciation expense and the revenue 12 requirement by approximately 10 million 13 dollars. Newfoundland Power's rate base and 14 its return on rate base will increase as a 15 result of these proposals, again costing 16 future customers more. So effectively, this 17 becomes a current rate reduction at the 18 expense of higher cost for customers in the 19 future.</p> <p>20 Q. What are the financial effects of that for the 21 company?</p> <p>22 A. From a financial perspective, if the consumer 23 advocate's depreciation proposals are 24 approved, in the short term the company's cash 25 flow from operations and financial matrix</p>
Page 162	Page 164
<p>1 2014 cost of equity at a time when bond yields 2 are rising. Given this, I'm not clear how the 3 proposed formula is logically reflecting 4 changes to Newfoundland Power's cost of equity 5 for changes in financial market conditions.</p> <p>6 Q. Ms. Perry, what is your overall assessment of 7 the formulas proposed in this proceeding?</p> <p>8 A. Simply speaking, Newfoundland Power did not 9 propose a formula, given the lack of consensus 10 on the relationship between long Canada Bond 11 yields in current financial market conditions 12 and the utility's cost of capital. I believe 13 the proposed formulas demonstrate that lack of 14 consensus. The 1.2 percent increase in long 15 Canada Bond yields in Mr. MacDonald's proposed 16 formula would almost certainly increase 17 Newfoundland Power's forecast cost of equity. 18 However, a 1.2 percent increase in Dr. Booth's 19 proposed formula would either leave 20 Newfoundland Power's forecast cost of equity 21 unchanged or could potentially reduce it.</p> <p>22 Q. Now let's turn next to depreciation. What 23 financial impact will the consumer advocate's 24 proposals have on customers?</p> <p>25 A. Well, a prominent feature of the consumer</p>	<p>1 would be reduced. I do not believe that this 2 is in the long term interest of either our 3 customers or Newfoundland Power.</p> <p>4 Q. Ms. Perry, have you assessed the impact on the 5 company's financial integrity if the Board 6 implemented both the depreciation 7 recommendations of Mr. Pous, and the ROE and 8 capital structure recommendations of Dr. 9 Booth?</p> <p>10 A. Yes, I have, and when you combine the impact 11 of both recommendations, the financial impact 12 to Newfoundland Power is very serious. If we 13 could go to Exhibit JP #3, please.</p> <p>14 MS. GLYNN:</p> <p>15 Q. And the same, that will be entered onto the 16 record.</p> <p>17 KELLY, Q.C.:</p> <p>18 Q. Thank you. This exhibit shows the company's 19 forecasted key financial matrix for 2014. The 20 first column shows the matrix based on 21 existing rates prior to any proposals in this 22 Application, and this was shown on Exhibit 3 23 in the evidence. Now as I said earlier, the 24 matrix shown here are not consistent with the 25 maintenance of Newfoundland Power's</p>

Page 165

Page 167

1 creditworthiness. The middle column shows the
 2 forecasted matrix proposed by Newfoundland
 3 Power in this Application. Finally, the last
 4 column is showing the impact of the consumer
 5 advocate's recommendations, particularly the
 6 reduction in the capital structure, the
 7 reduction in the return on equity to 7.5
 8 percent, and the depreciation recommendations.
 9 So simply looking at the financial matrix
 10 alone, based on the consumer advocate's
 11 recommendations, if you go to line 6, our
 12 interest coverage would be 2.1 times; on line
 13 8, our cash flow to interest would drop to 2.7
 14 times; and then on line 11, our cash flow to
 15 debt ratio would be 11 percent. These matrix
 16 are at or lower than our existing matrix under
 17 column 1, and are also at or below the bottom
 18 of the range indicated by Moody's that may
 19 warrant a credit downgrade. Moody's has
 20 indicated that Newfoundland Power would likely
 21 be downgraded if they were to perceive a
 22 meaningful reduction in the level of
 23 regulatory support combined with the sustained
 24 deterioration in financial matrix. These
 25 proposals disregard the requirement that the

1 CERTIFICATE
 2 I, Judy Moss, hereby certify that the foregoing is a true
 3 and correct transcript in the matter of Newfoundland
 4 Power's Inc.s General Rate Application, heard on the 10th
 5 day of January, A.D., 2013 at the Board of Commissioners
 6 of Public Utilities, 120 Torbay Road, St. John's,
 7 Newfoundland and Labrador and was transcribed by me to
 8 the best of my ability by means of a sound apparatus.
 9 Dated at St. John's, Newfoundland and Labrador
 10 this 11th day of January, A.D., 2013
 11 Judy Moss

Page 166

1 company maintain a sound credit rating in the
 2 financial markets. As CFO, I believe that
 3 these proposals would negatively impact our
 4 credit ratings.
 5 Q. Does that conclude your testimony?
 6 A. Yes, it does.
 7 KELLY, Q.C.:
 8 Q. Thank you.
 9 CHAIRMAN:
 10 Q. I think we'll adjourn and we'll make a
 11 decision as to proceeding tomorrow early in
 12 the morning, and the parties will be advised
 13 of the Board's decision.
 14 MS. GLYNN:
 15 Q. We received emails and phone numbers for all
 16 the parties, but just for the record to make
 17 sure that we'll be putting out a media
 18 advisory as well as the public will be
 19 advised.
 20 CHAIRMAN:
 21 Q. Okay, we're adjourned.
 22 KELLY, Q.C.:
 23 Q. Thank you, Mr. Chairman.
 24 (1:53 p.m.)
 25 (UPON CONCLUDING)

<div>#-</div> <div>#1 [1] 156:23</div> <div>#2 [1] 159:15</div> <div>#3 [1] 164:13</div> <div>#682 [1] 115:25</div> <div>-\$-</div> <div>\$100,000 [1] 32:2</div> <div>\$200,970 [1] 66:1</div> <div>\$474,000 [1] 65:6</div> <div>-&-</div> <div>& [2] 109:22 118:24</div> <div>-.-</div> <div>.23 [2] 158:19,20</div> <div>.25 [1] 158:24</div> <div>-0-</div> <div>0.23 [1] 157:25</div> <div>0.6 [2] 2:17 25:23</div> <div>-1-</div> <div>1 [11] 3:14 6:12 10:3 23:12 51:7 69:23 94:1 124:3,20 145:16 165:17</div> <div>1.2 [3] 161:17 162:14,18</div> <div>1.3 [2] 10:2 133:17</div> <div>1.4 [4] 133:16,17,18,23</div> <div>1.45 [2] 158:13 161:6</div> <div>1.56 [1] 68:20</div> <div>1.6 [3] 7:24 25:9 46:1</div> <div>1.8 [7] 7:6,17 25:7 32:5 59:6,21 160:24</div> <div>10 [7] 1:1 93:24 94:1 112:11,11 149:4 163:12</div> <div>10.4 [17] 7:18 13:11 25:4 34:8 43:18 46:24 47:3 54:16,23 82:2,5,11,18 82:21 83:13 87:6,13</div> <div>10.5 [3] 34:8 84:2 89:14</div> <div>100 [12] 64:9 65:4 66:18 67:2,9,11,23,25 75:15 77:5,10,12</div> <div>10.00 [1] 18:20</div> <div>10.15 [1] 28:12</div> <div>10.30 [1] 41:3</div> <div>10.45 [2] 54:1 67:16</div> <div>10th [1] 167:4</div> <div>11 [8] 1:12 5:17 150:2 154:23 158:1,19 165:14 165:15</div> <div>11.15 [1] 79:14</div> <div>11.30 [1] 1:12</div> <div>11.47 [1] 79:16</div> <div>11th [3] 2:22 4:24 167:10</div> <div>12 [4] 123:24 124:17 135:20 150:2</div> <div>120 [1] 167:6</div>	<div>12:00 [1] 92:4</div> <div>12:15 [1] 101:6</div> <div>12:30 [1] 113:16</div> <div>12:45 [1] 123:10</div> <div>13 [2] 123:25 124:17</div> <div>143 [1] 123:12</div> <div>14th [2] 2:9 52:16</div> <div>15 [5] 68:13,20 72:17 89:2 161:4</div> <div>15.7 [1] 146:10</div> <div>15th [1] 4:20</div> <div>16 [2] 72:17 161:5</div> <div>17th [1] 3:10</div> <div>18th [1] 5:1</div> <div>19 [1] 68:1</div> <div>1920s [2] 93:17,17</div> <div>1977 [1] 10:17</div> <div>1983 [1] 10:18</div> <div>1990s [2] 35:14 36:5</div> <div>1998 [1] 35:25</div> <div>1999 [1] 20:18</div> <div>1:00 [1] 132:8</div> <div>1:23 [1] 143:7</div> <div>1:30 [4] 1:11 5:16 142:20 148:4</div> <div>1:45 [1] 159:20</div> <div>1:53 [1] 166:24</div> <div>1st [1] 2:16</div> <div>-2-</div> <div>2 [7] 5:10 42:8 44:7,19 53:25 70:4 139:13</div> <div>2.1 [3] 133:13,14 165:12</div> <div>2.3 [1] 146:7</div> <div>2.39 [1] 139:11</div> <div>2.58 [1] 68:13</div> <div>2.59 [4] 157:18 158:1 160:9 161:16</div> <div>2.6 [2] 6:22 24:22</div> <div>2.7 [1] 165:13</div> <div>20 [8] 63:7 68:23 69:7 72:5 132:12 134:4 135:16 151:13</div> <div>200 [1] 64:6</div> <div>2000s [1] 115:10</div> <div>2001 [1] 154:13</div> <div>2003 [1] 68:1</div> <div>2003/2004 [1] 126:5</div> <div>2004 [1] 66:3</div> <div>2005 [1] 144:22</div> <div>2007 [3] 24:1,3 138:21</div> <div>2008 [3] 38:14,15 138:21</div> <div>2009 [10] 8:22 13:18 14:6 14:11 16:21 27:24 29:5 153:11,17 154:24</div> <div>2010 [20] 8:1,23,24 10:22 21:7 22:2 32:6 56:21 58:9 60:10,13,18 61:18 145:18,21,23 146:13 154:10,22 155:11</div> <div>2011 [21] 7:8 8:23 14:14</div>	<div>28:5,13 44:12 45:10,13 45:16 66:3 116:11 118:1 145:18,18,21,24 153:24 154:2,5,9 155:12</div> <div>2012 [36] 2:22 3:19 4:20 5:4 7:11,13 8:23 13:5 28:9,14,16 38:20 41:16 41:25,25 42:12,19 44:12 44:14,23 45:6,12 54:3 63:20 65:7 68:10 69:1 72:18,22 75:14 145:19 146:2,2,10 152:23 157:19</div> <div>2013 [33] 1:1,4 2:16 4:7 4:8 6:23 8:23 13:5,8,11 28:20 38:18 43:4,5,7 44:13,14,23 45:25 51:19 67:8 76:24 77:16 145:19 146:16,17,19,23 152:13 153:1 157:10 167:5,10</div> <div>2013-2014 [1] 24:21</div> <div>2014 [25] 4:8 6:24 13:8 13:11 28:20 43:4,8,10 44:13 45:24 46:1 67:8 76:24 77:16 145:19 146:16,17,19,24 157:8 158:17 161:9,12 162:1 164:19</div> <div>2017 [2] 93:12 122:15</div> <div>2030 [2] 93:12,18</div> <div>21 [3] 151:13 158:17 161:9</div> <div>21st [2] 3:12 57:3</div> <div>224 [1] 123:24</div> <div>24.1 [1] 45:4</div> <div>243 [1] 125:13</div> <div>25 [4] 43:5 57:8 70:6 158:21</div> <div>250,000 [2] 54:8 134:23</div> <div>28 [2] 42:9 110:2</div> <div>2:30 [1] 5:19</div> <div>-3-</div> <div>3 [4] 42:8 144:23 145:16 164:22</div> <div>3.04 [3] 157:13,25 158:2</div> <div>3.2 [1] 146:8</div> <div>3.4 [1] 7:3</div> <div>3.7 [2] 11:4 40:13</div> <div>3.8 [5] 159:25 160:4,5,12 161:14</div> <div>30 [2] 158:7 161:2</div> <div>31 [1] 76:20</div> <div>31.5 [2] 75:16,21</div> <div>32 [1] 43:15</div> <div>35 [7] 42:17 63:5 68:24 69:4 145:22 146:5,22</div> <div>350 [1] 52:4</div> <div>36 [2] 13:4 42:12</div> <div>37 [2] 146:6 147:2</div> <div>38 [1] 146:8</div> <div>39 [2] 146:9 147:3</div> <div>-4-</div>	<div>4 [3] 139:12 157:10 159:22</div> <div>40 [5] 69:25 104:23 138:12 149:1 150:4</div> <div>400 [2] 21:16 64:5</div> <div>401 [1] 44:4</div> <div>42 [4] 13:7 149:15 150:19 150:20</div> <div>42.5 [1] 43:7</div> <div>44 [2] 13:9 43:9</div> <div>443 [2] 68:7 72:16</div> <div>449 [1] 66:2</div> <div>45 [11] 8:8,11 46:2 102:18 106:1,13 107:10 148:13 148:25 150:3 151:16</div> <div>45/55 [2] 101:22 107:5</div> <div>451 [1] 69:22</div> <div>474 [1] 65:20</div> <div>4th [1] 51:20</div> <div>-5-</div> <div>5 [3] 68:9 149:12 150:4</div> <div>5,000 [1] 94:19</div> <div>50 [12] 64:4,10,12,12 70:1 140:4,13 141:12 157:14 158:2,4 160:16</div> <div>50/50 [1] 71:9</div> <div>500,000 [1] 135:3</div> <div>50th [1] 72:7</div> <div>55 [2] 69:5,7</div> <div>-6-</div> <div>6 [10] 2:18 6:20,20 24:9 24:13 43:5 157:16 158:23 160:1 165:11</div> <div>6.89 [1] 146:24</div> <div>60/40 [1] 131:3</div> <div>60s [1] 116:24</div> <div>682 [1] 116:4</div> <div>-7-</div> <div>7 [2] 157:22 160:11</div> <div>7.2 [2] 2:19 25:21</div> <div>7.5 [9] 28:1 68:17 149:2 152:13,18 153:2 159:23 161:9 165:7</div> <div>7.53 [1] 152:25</div> <div>7.57 [1] 146:23</div> <div>7.85 [2] 28:11 152:21</div> <div>70 [2] 71:11 163:2</div> <div>70/30 [1] 71:12</div> <div>70s [1] 116:24</div> <div>75 [4] 70:5 71:11 158:25 160:2</div> <div>75/25 [1] 71:11</div> <div>-8-</div> <div>8 [3] 144:3 157:23 165:13</div> <div>8.38 [9] 7:9,16,18 25:6 28:6 146:20 153:25 154:4</div>	<div>155:3</div> <div>8.4 [1] 44:17</div> <div>8.68 [1] 158:18</div> <div>8.7 [2] 47:15,17</div> <div>8.75 [3] 108:18 113:20 138:8</div> <div>8.8 [3] 7:12 28:16 146:4</div> <div>8.81 [2] 42:19 146:6</div> <div>8.91 [2] 157:11 158:18</div> <div>80 [2] 63:2 150:2</div> <div>80s [1] 116:24</div> <div>-9-</div> <div>9 [6] 5:16 7:9 28:3 47:19 93:24 145:23</div> <div>9,000 [1] 109:25</div> <div>9.21 [1] 145:23</div> <div>9.9 [2] 47:10 108:21</div> <div>9.90 [1] 108:19</div> <div>90 [5] 94:8,14,15 95:2 151:13</div> <div>90s [1] 115:10</div> <div>9th [1] 5:3</div> <div>-A-</div> <div>A.D [2] 167:5,10</div> <div>a.m [7] 18:20 28:12 41:3 54:1 67:16 79:14,16</div> <div>A2 [1] 147:14</div> <div>ability [12] 27:11 32:19 90:15,20 91:8 112:11,13 112:15 113:8,10 137:25 167:8</div> <div>able [7] 82:7 97:7 113:25 114:17 120:9 122:20 139:8</div> <div>abnormal [1] 8:21</div> <div>above [5] 64:12 66:6 129:5 138:13 160:3</div> <div>absolutely [1] 41:17</div> <div>accede [1] 83:11</div> <div>accept [7] 5:4 65:8 82:25 83:22 88:24 109:14 110:7</div> <div>accepted [2] 49:1 140:1</div> <div>accompanied [1] 50:14</div> <div>according [5] 43:12 44:19,25 46:6,11</div> <div>Accordingly [1] 18:1</div> <div>account [8] 4:4 15:16 96:15 98:18,19 138:7,14 155:23</div> <div>accounts [4] 4:6 14:12 24:21 25:7</div> <div>accrued [1] 149:3</div> <div>accuracy [1] 136:4</div> <div>achieve [7] 18:4 20:4 34:19,23 64:24 75:14 77:22</div> <div>achieved [2] 8:20 67:10</div> <div>achieving [1] 10:6</div> <div>acknowledged [1] 50:11</div>
---	---	--	--	---

Act [1] 37:15 actual [6] 4:2 55:14 93:11 118:11 145:17,21 adapt [1] 26:18 add [7] 30:3 60:2 61:20 95:22 96:1 97:7,9 added [2] 9:1 38:19 adding [1] 65:19 addition [6] 29:25 30:19 37:18 45:25 63:25 156:1 additional [7] 5:20 52:23 53:2 59:5 60:8 86:17 150:21 address [4] 10:8 21:24 36:17 39:4 addressed [3] 96:4 97:15 99:20 addressing [1] 132:3 adds [2] 11:3 39:24 adjourn [4] 18:16 142:7 143:1 166:10 adjourned [1] 166:21 adjust [2] 112:15 160:15 adjusted [2] 157:14 160:2 adjustment [18] 7:10 8:5,16 17:2,12 21:10 38:8 58:23 71:10 72:3 140:16 145:8 153:8,11 155:15 158:15 160:13 161:7 adjustments [4] 4:10 15:16 16:18 96:14 adjusts [1] 158:3 admitted [1] 42:23 admonitions [1] 16:8 adopt [5] 5:7 10:24 11:6 23:12 144:23 adopted [2] 38:9 40:6 adopting [1] 40:16 adverse [1] 14:8 advised [3] 123:6 166:12 166:19 advisement [1] 87:23 advisory [1] 166:18 advocate [13] 4:1 10:11 11:1,22 19:4 20:11 21:24 39:16 55:12 85:7 88:5 128:4 148:24 advocate's [5] 162:23 163:1,23 165:5,10 affect [2] 37:9 151:4 affected [1] 154:14 affects [1] 12:10 afternoon [2] 126:25 127:1 again [35] 5:8,21 8:15 15:1 16:7,13 19:11 28:19 38:7 41:6 47:24 58:11 65:25 68:19 88:7 92:9 92:18 93:8,13 108:4 115:20 116:3 124:9,13 133:19,24 141:16 146:5 146:22 149:18 155:9	157:24 159:22 161:3 163:15 against [3] 60:1 115:17 115:23 age [6] 93:20 119:1 133:25 136:6,8 agencies [9] 130:4 148:6 148:8,15 149:21 150:15 150:23,25 151:6 agency [1] 151:20 ages [1] 133:4 aging [3] 30:21 31:1 112:6 ago [5] 40:6 112:19,20 130:11 131:19 agree [24] 38:15,17 41:20 50:16 55:13 62:13,22 65:14,22 69:5 74:19,21 78:3 79:25 86:2 89:7 106:22 107:13 109:3,19 123:17 128:8 150:6 155:17 agreeable [1] 143:24 agreed [16] 3:16,17,22 3:25 4:3,5,13,15 5:4,18 13:20 88:5,12 128:16 131:23 143:22 agreeing [3] 82:20 84:9 107:4 agreement [8] 3:11,13 6:8,11 67:7 70:24 130:8 154:13 agrees [2] 84:1 161:1 ahead [2] 143:12,14 aimed [1] 36:18 Alberta [15] 24:5 32:1 101:1,7,8,9 104:14 108:18 113:19,21 114:6 114:9 115:17 138:8 152:5 ALG [1] 40:12 Aliant [4] 94:23 130:9 131:8 154:11 allowance [1] 118:12 allowed [27] 3:1,3 7:8 7:12 13:12 18:13 28:7 34:11,25 46:20 47:6 57:25 60:13 81:15 82:11 86:17 108:12,16,20 138:9 138:12 145:25 150:24 151:3,5,15,22 allowing [1] 43:16 allows [1] 64:3 alluded [2] 21:5 67:22 almost [5] 16:2 95:15 96:20 136:14 162:16 alone [2] 59:5 165:10 Alteen [1] 76:18 always [3] 88:16 91:9 122:11 America [2] 28:9 152:21 among [3] 2:14 33:21 39:9 amongst [2] 21:20 47:5 amortization [3] 3:21 3:23 9:13	amount [10] 14:3 17:19 52:3 87:1 102:25 109:18 131:10 149:15 161:23 163:7 amounts [2] 7:6 64:15 AMR [2] 122:12,13 analysis [6] 9:19 15:12 121:18 156:15 157:5 159:5 Andy [1] 1:5 anecdotally [2] 113:8 135:8 announcing [1] 51:18 annual [6] 33:2 35:17 116:10 119:6,14 163:10 anomalies [1] 126:6 answer [15] 6:16 12:18 60:12 74:13 77:22 84:9 86:6,10 99:12 108:15 114:8 128:5 129:20 133:5 141:21 answered [2] 82:15 84:12 answering [1] 82:23 answers [2] 85:23 160:25 anticipated [2] 131:6 131:15 anticipating [1] 138:24 anyway [1] 72:3 apart [1] 50:7 apparatus [1] 167:8 apparent [1] 159:11 Appeal [1] 11:17 appear [3] 113:9 150:25 152:14 appearance [1] 57:5 appearing [1] 5:6 application [43] 1:5 2:10 3:8,20 4:16 5:23 6:10 7:2 10:13 13:19 15:9 18:25 19:3 22:3 23:11 24:7 25:1,3 27:21,24 28:15 28:18 32:7 41:16 50:14 50:16,23 51:19 52:18,19 53:5 82:17,24 92:7 96:3 96:25 123:24 146:20 148:20 154:22 164:22 165:3 167:4 applications [1] 17:9 applied [4] 11:16 28:13 65:24 160:6 applies [2] 11:20 161:14 apply [3] 36:13 95:25 155:11 appreciate [1] 57:18 apprenticeship [1] 91:2 approach [7] 9:3 16:9 16:13 39:7 40:9 90:22 118:19 appropriate [10] 5:24 7:23 10:14 25:18 34:24 83:22 89:1 114:19 151:25 153:5 approval [1] 131:14 approve [1] 2:14	approved [4] 8:7 10:22 130:9 163:24 area [10] 20:21 57:3 59:5 62:22 92:24 97:1 102:2 117:15 135:22 137:23 areas [15] 52:1,25 63:12 91:7,7,25 92:18 108:6 110:25 112:23 127:6,7 134:10,13 137:16 argue [1] 62:18 argued [2] 15:23 55:23 89:3 107:3 argument [4] 65:8 88:15 89:3 107:3 arise [2] 85:16,23 arising [1] 122:20 arrangement [1] 130:13 arrangements [1] 130:16 articulated [1] 106:16 aside [1] 86:20 aspect [4] 19:21 27:21 32:23 80:11 aspects [2] 81:3 134:21 assemble [1] 19:8 assess [1] 150:23 assessed [1] 164:4 assessing [1] 150:17 assessment [11] 116:2 116:13 119:8,10 120:15 120:16,22 122:21,23 151:6 162:6 asset [1] 40:10 assets [7] 10:14 22:7 26:11 32:21 33:17 109:24 110:5 assigned [1] 150:16 assist [1] 88:19 assisted [1] 131:12 assisting [2] 1:8,21 associated [7] 14:15 18:2 20:2 100:20 153:16 154:20,25 assume [4] 77:23 107:21 114:22 161:21 assumed [1] 157:5 assumes [2] 157:12 159:25 assuming [5] 69:18 76:25 89:14 157:16 160:7 assumption [2] 157:9 158:12 assumptions [3] 10:1,5 78:5 assure [3] 48:20 76:19 78:7 attachment [1] 54:6 attainable [1] 77:8 attempt [2] 156:1,15 attention [2] 72:15 119:13 attract [4] 90:15,20,25 113:9 August [1] 3:19	Austin [1] 21:14 automatic [11] 7:10 8:5 8:16 17:2,12 21:9 38:8 145:8 153:8,10 155:14 automatically [4] 32:2 76:20 88:23 130:24 Aux [2] 117:9 121:7 available [3] 15:13 95:11 96:12 Avalon [1] 92:15 average [40] 2:15,19 4:7 6:19 8:14 22:5,10 24:8 24:13 28:25 29:17 32:11 55:19 98:13,14,23 99:10 99:23,24,25 108:2,3,15 108:23 109:2 111:6 114:25 115:22 127:15,24 128:1,13,18 129:1 133:4 133:25 134:9 136:8 137:1 141:11 avoid [1] 131:1 avoiding [1] 120:2 aware [6] 6:1 97:11 104:22 107:17 109:22 113:22 away [2] 38:24 153:22 awful [1] 134:8
-B-				
bad [2] 57:22 115:6 bailouts [1] 138:22 balance [18] 16:1 29:17 37:8,10,20,22 48:19 80:1 80:6 83:6 92:19 94:8 95:14 96:17,17,19 110:4 120:11 balanced [1] 15:24 band [2] 46:21 64:11 base [22] 4:8 9:14 11:2,4 39:22,23,24 40:11 63:25 64:5 65:17 133:22 146:3 154:15 157:23 158:10,12 160:19,22 161:5 163:13 163:14 based [22] 7:19 10:19 15:2 22:1 47:20 71:12 77:25 78:4 81:15 82:17 107:8 114:15 146:3,20 146:24 157:9,19 159:5 160:21 161:10 164:20 165:10 baselines [1] 125:4 bases [1] 133:4 basis [39] 9:16 32:11 48:3 50:7 59:23 71:13,18 73:4 77:5,8,13 78:3 85:25 88:20 91:10 97:8,17 102:3 109:2 117:25 120:4 120:6 121:9,11 122:10 122:16 124:14 125:17 126:16 131:15 137:25 138:12,15 140:14,20 142:22 158:21,23,25 Basques [2] 117:9 121:7 BC [26] 101:1,3,5 108:20 108:21,22 109:1,5,8,10				

110:15,18,19 111:20 112:5,18,18 113:7 114:20 115:17,23 126:2,3,15 128:4,17 BCUC [1] 115:20 bear [4] 26:1 44:3 73:7 117:24 bearing [1] 25:12 became [1] 130:16 become [1] 125:12 becomes [2] 125:23 163:17 becoming [2] 61:24 62:4 begs [1] 16:23 behalf [4] 1:25 21:21 23:11 76:18 believes [2] 15:11 41:14 Bell [3] 130:8 131:1 154:11 below [3] 152:19 160:12 165:17 benchmark [1] 124:25 beneficiary [5] 17:23 19:24 79:22 80:13,20 benefit [5] 3:22 14:19 31:22 80:11 126:4 benefits [2] 10:4 14:17 Berra [1] 16:6 best [10] 9:3 15:13 40:5 40:9,9 48:21 81:22 95:10 96:12 167:8 better [8] 39:2,7 89:22 97:5 98:21 99:20 104:2 105:19 between [21] 1:12 7:18 37:20,25 44:13,14 70:15 78:9 87:12 113:17 125:24 129:23 130:8 137:17 141:5 153:13 155:24 158:1,7 159:11 162:10 beyond [3] 102:4 106:15 131:22 big [2] 113:9 139:17 biggest [1] 69:1 bill [1] 56:1 billable [1] 131:11 bills [2] 26:23,24 bit [9] 55:10 90:19 94:10 112:5 116:21 128:2 140:21 142:6 153:7 bless [1] 57:4 blew [2] 61:21,21 blocks [1] 112:22 Bloomberg [1] 161:2 blow [1] 61:6 Blundon [1] 1:9 board [88] 2:9,14,21 3:5 3:6,11,17 6:17 7:22 8:7 8:10 9:18 10:14,18 11:14 12:25 13:6 14:11 15:9 15:11,25 16:9,14,16 17:11 21:6 24:10 28:3 28:19,24,24 29:12 39:10 40:5,16 43:16 50:14 51:21 56:9 59:14,23 67:24 70:20,23 72:12 81:16 82:12 83:5,7,10 83:12 84:1,22 88:2,16 88:20 89:8 95:13 96:16 96:18 98:13 100:16 108:11 120:5,7,13,18,19 122:16 127:16 130:9 132:19,23 134:2,4 138:1 140:13 141:23 142:20 146:14 147:19 148:9 149:8 150:8 152:17 153:9 164:5 167:5 Board's [15] 4:10 5:2 10:24 11:6 36:2 88:2 95:8,19,24 96:3,24 97:14 148:17 154:24 166:13 boardroom [1] 118:9 bodies [1] 117:17 Bonavista [2] 57:1,2 bond [34] 139:10 155:5,8 155:23,25 156:2 157:15 157:17,23 158:5,6,7,9 158:10,12,14,23 159:1 160:3,8,11,17,20,22,23 161:5,7,15,20,22,22 162:1,10,15 bonds [3] 21:3 147:13 158:8 book [1] 42:18 books [1] 42:3 Booth [19] 2:1 20:14,14 20:23 21:4,7 139:23 151:14 152:14,19 156:12 156:14 159:24 160:1,13 160:23 161:1,14 164:9 Booth's [10] 150:1 151:12 156:10 159:9,12 159:15 160:5,19 161:11 162:18 borrowed [1] 149:16 bottom [4] 56:1,6 124:16 165:17 Boundary [2] 111:1,8 bow [1] 114:20 boxes [1] 94:22 boy [1] 144:11 break [7] 1:12 5:17,20 63:12 79:1,3,15 breaks [1] 6:21 brief [2] 26:4 145:13 bring [14] 17:5 46:2 50:23 59:11 63:14 72:6 87:25 108:10 115:18 116:2 129:9 137:24 140:18 147:21 bringing [2] 68:7 71:9 brings [1] 21:1 British [6] 24:5 33:23 34:3 47:11 104:14 115:20 broadening [1] 96:1 broken [1] 58:14 brought [3] 52:24 80:5 100:4 bubble [1] 116:25 budget [1] 122:12 budgetary [2] 118:11 118:12 build [2] 118:3,5 built [4] 9:25 81:6 82:18 82:22 bunch [1] 48:17 burden [2] 8:18 11:21 bureaucracy [1] 119:17 Burin [1] 99:4 business [29] 15:20 19:9 19:15 46:16 47:22 81:25 97:20 98:10 99:5,7,8,8 101:17,19 108:6 110:9 111:7,20,25 112:2,3 115:2 119:4 128:7 135:24 136:25 137:20,21 138:16 businesses [5] 98:6,16 99:22 125:20,22 bustle [1] 91:22 buying [2] 110:20 113:11 -C- C [1] 118:24 CA-NP-142 [2] 124:4,5 CA-NP-143 [1] 123:6 CA-NP-401 [1] 44:1 CA-NP-440 [1] 63:14 calculate [1] 133:7 calculation [7] 3:21 22:9 64:25 65:3,12,14 141:4 calculations [2] 132:24 133:2 calculator [1] 65:2 calls [3] 130:21 131:1,1 Canada [34] 13:13 21:4 21:17 22:11 29:16 30:7 30:21 47:6 103:12 105:11 105:14 106:21 107:20 132:19 155:5,8,22,23,25 156:2 157:15,17,23 158:8 158:23 159:1 160:3,8,11 161:15,20,22 162:10,15 Canada" [1] 124:9 Canadian [18] 21:23 29:1,11 30:15,17 47:9 72:8 98:7 108:13,17 123:5,8,15 127:16 128:15 128:18,25 140:11 cannot [3] 85:12 106:18 106:22 cap [1] 111:8 capable [1] 132:3 capital [66] 5:12,18 7:20 8:3,4,6,7,9,21 12:11 15:3 16:11,25 20:19,20 29:14 31:8 32:10,13,22 33:1,3 33:5,17,19,25 34:2,3 35:17,20 38:16 46:23 48:20 58:14,23 59:18 95:6 97:2,13,25 99:15 102:8 103:1,14,21 105:10 106:8,23 107:9,23 122:12 138:16,18 139:15 145:7 145:7 148:25 149:7,9,14 151:23 155:1 160:22 162:12 164:8 165:6 captive [1] 33:19 capture [1] 136:22 careful [1] 135:18 carry [1] 142:25 case [19] 8:3 15:2 16:23 41:12 48:16 49:6,16,17 50:12 53:17 55:8,23 62:17 64:4 86:5 110:15 127:17,21 145:15 cash [7] 141:2 146:8,9 154:15 163:24 165:13,14 casting [1] 48:24 categories [3] 22:7 107:14 129:8 category [4] 68:11 99:10 108:2,3 causes [1] 163:6 census [1] 135:21 central [7] 50:15 52:10 53:16 55:8 56:10,15 95:6 centre [2] 20:19 130:24 centres [4] 30:23 92:16 93:8 134:15 CEO [9] 23:24 34:21 48:10 69:25 70:5 95:19 100:8 106:19 128:22 certain [4] 9:25 64:24 102:14 130:4 certainly [10] 26:7 30:1 37:2 53:10 62:21 87:11 103:8,15 145:13 162:16 CERTIFICATE [1] 167:1 certify [1] 167:2 CFO [5] 105:18 106:16 138:17 142:8 166:2 chair [22] 1:18,25 2:7 3:9 5:15,23 20:17,17 61:2 84:21 85:6 86:15 88:5 103:11,18 105:4 129:6 132:16 133:16 135:8 137:15 144:8 Chairman [94] 1:2,22 2:3 6:4,7 11:12,25 12:20 12:24 16:5,20 18:5,12 18:21 19:19 22:14,19,22 22:25 23:4 24:16 30:4 40:25 41:1,20 42:4 46:7 48:15 55:10 60:3 61:21 62:3,16,24 63:4,8 71:19 78:13,18,23 79:2,8,12 79:17,20 80:1 83:16,24 84:8,16,25 86:25 87:25 88:17 89:11,21 90:5,6,9 90:18 92:9 97:1 98:4 100:4 103:25 106:1 107:2 111:6,22 114:13 120:6 120:19 121:21 124:18 126:22 132:9 134:2 140:10 141:16 142:4,13 142:21,23 143:4,8,12,13 143:19 144:2,9,18 166:9 166:20,23 challenge [1] 22:4 challenges [9] 10:11 22:8 29:6,10,13 31:10 91:11 92:3 113:6 challenging [1] 30:13 change [25] 16:9 61:3 63:1 70:7,8,11,13,15,18 72:9 97:17 127:20 135:5 149:19 155:23,24 156:18 156:19 157:15 158:4,14 160:3,16 161:6,11 changed [5] 42:11 90:21 106:7 147:15 156:20 changes [20] 3:20 4:3,12 4:13 5:22 23:17 25:10 25:24 26:18 31:9 40:4 70:11 90:17 91:4 111:17 145:2 156:2 161:20 162:4 162:5 changing [10] 29:10 61:3 90:19 91:3,5 93:20 112:10 115:15 149:9 163:9 characteristics [2] 47:21,23 characterizes [1] 109:21 charged [2] 125:11,11 check [3] 65:1 66:1 123:11 Cheryl [1] 1:8 chief [8] 12:4,7 23:5 59:3 96:22 129:24 143:18 144:19 choice [1] 38:2 choose [1] 37:25 chose [2] 154:7,18 chosen [2] 15:12 95:10 Chris [2] 1:20 147:20 circumstance [1] 156:19 circumstances [5] 81:9 81:23 82:1 130:23 149:24 CIT [1] 20:17 city [1] 91:23 civil [1] 118:25 clarified [1] 56:2 clarify [1] 95:2 clarity [4] 87:25 88:18 90:1,5 classes [1] 55:21 clause [1] 4:14 clear [17] 16:1,8 19:23 40:15 45:10 56:20 81:13 88:9 89:9 95:15 96:19 98:12,12 106:4 124:18 131:19 162:2 clearer [1] 53:20 clearly [4] 36:10 52:22 152:2,9 closed [2] 42:3 126:5 closer [1] 140:18 coast [1] 61:22 cohorts [1] 136:6 colleagues [1] 1:6 collected [2] 163:3,7 Columbia [6] 24:5 33:23
--

34:3 47:11 104:15 115:20 column [9] 43:6,9 64:3 65:19 146:1 164:20 165:1 165:4,17 columns [2] 145:20 146:18 combination [1] 59:24 combinations [1] 94:11 combine [2] 93:18 164:10 combined [4] 58:16 148:1,22 165:23 combines [1] 75:22 comfort [1] 9:19 Cominco [1] 112:22 coming [11] 20:7 31:4 59:22 91:6 92:22 93:1,3 93:5,12 116:23 117:1 commensurate [1] 14:24 comment [5] 29:20 31:12 93:15 147:10 156:10 commentary [1] 95:23 comments [4] 4:25 12:21 24:23 95:8 commercial [3] 2:18 72:8 140:11 Commissioners [9] 12:24 16:5,20 19:19 21:6 22:15 85:15,21 167:5 commissions [1] 21:22 commit [2] 33:16 86:12 commitment [1] 52:1 committed [1] 73:8 committee [5] 20:25 70:21,24 71:6 75:20 common [17] 31:21 34:20 43:24 46:3 80:17 85:22 103:3,5,13 104:23 105:10 106:23 148:14 149:11 150:3 151:17 157:11 communicated [1] 55:5 communities [2] 30:24 135:10 community [1] 135:22 companies [26] 16:14 16:18,21 47:16,19,20 98:1 99:15 100:1,18,19 100:24 103:16,18,22 104:9,18 106:6 124:8 125:24 126:7 140:2,11 140:15,16 141:20 company [71] 5:12 8:15 10:6,21 11:19 12:8 13:25 14:15,23 17:24,25 19:24 23:11 24:2 28:2,13 32:17 36:4 38:9,21,25 41:23 45:10,14 48:13 54:13 58:21 59:12 64:22 66:6 67:12 74:24 75:13 80:16 81:3,14,18,21 83:4 87:18 102:12 103:3 105:11,13 106:22,24,25 107:19,21 108:8 109:5,8,16,17	110:16,19 112:21 115:9 116:12,16 118:21 119:7 121:10 122:14 132:11 140:6 141:17 149:13 154:21 163:21 166:1 company's [50] 6:9,13 7:20 9:21 11:14 19:22 20:3,6 22:5,9 27:23 28:10 34:14 35:25 36:11 36:20,23 41:17 50:19 54:13 74:4,6 75:6 80:25 81:11 82:17 103:14 116:1 119:6 140:6 144:24 145:11,17 147:8,23 148:3 148:13,18,21 149:5 151:11 152:10 154:15,17 155:2,10 161:19 163:24 164:5,18 comparable [6] 15:5 16:15,21,22 107:20 108:23 comparables [9] 15:13 15:19,24 16:4 95:10,17 96:11,17,22 comparator [1] 124:21 comparators [4] 97:2 125:8 126:6 129:25 compare [8] 97:25 108:8 114:19 124:7 125:3,19 126:2,10 compared [2] 137:16 141:8 comparison [4] 32:3 108:12 124:11 141:5 compensation [18] 19:23 72:6 82:10 83:10 84:3 86:21 89:19 139:25 140:3,23,24,25 141:1,5 141:6,8,14,24 competing [2] 37:20,23 competition [2] 14:2 15:22 complement [4] 90:13 90:14,18 91:3 complete [1] 60:3 completed [2] 10:21 21:18 complexity [1] 38:20 component [13] 6:22 7:5 25:9 27:19 33:3 52:7 71:7,8 103:14 106:12 158:16 160:14 161:8 components [8] 6:22 24:20 26:8 51:22 99:7 112:4 126:14 148:12 comprehensive [1] 9:15 con [4] 97:17 115:3 118:4 129:11 concede [1] 53:8 concentration [1] 93:22 concern [6] 19:6 30:9 96:22,24 141:23 163:6 concerned [3] 50:6 95:18,18 concerning [3] 39:17 136:10,10 concerns [3] 96:4 97:14	149:5 conclude [5] 9:16 15:9 22:14 40:21 166:5 concluded [2] 15:10 28:24 CONCLUDING [1] 166:25 conclusions [1] 9:20 condition [3] 26:13 59:13,15 conditions [24] 8:21 9:6 30:2,7,9 35:15,20 39:4 39:12 56:19 58:20,24 61:2 80:4 99:6 111:11 112:8 115:2 155:4,19 156:7,20 162:5,11 conduct [1] 120:21 conducted [3] 9:11 116:12 119:7 conference [5] 2:21 3:1 132:19,23 134:2 confidence [2] 39:1 156:4 confirm [3] 5:23 41:13 54:10 confirmed [2] 103:21 127:14 confused [1] 98:5 connected [1] 92:14 Connecticut [1] 152:5 connection [4] 50:20 53:21 55:15 63:18 connections [2] 92:11 94:20 cons [1] 98:17 consensus [9] 9:6 39:9 39:13 143:17 157:18,19 157:20 162:9,14 Consent [3] 3:14 5:10 6:12 consequences [1] 149:13 conservation [2] 3:24 26:21 conservative [1] 13:23 consider [10] 29:17 35:3 75:12 91:15 107:19 128:9 129:1 148:6,22 153:5 considerable [2] 16:12 153:21 consideration [1] 88:3 considerations [2] 86:20 155:10 considered [8] 16:3 95:16 96:21 110:16 128:17 130:1 150:14 154:21 consistency [2] 50:5,9 consistent [7] 34:15 41:17 42:25 146:11 147:7 161:3 164:24 consistently [2] 8:7 148:14 Consolidated [1] 16:14 constitute [1] 122:7	construction [1] 93:24 constructive [1] 17:5 consultant [2] 36:2 72:4 consultants [2] 5:2 21:14 consumed [1] 26:25 consumer [19] 2:1 4:1 10:11 11:1,22 19:4 20:11 21:24 39:16 55:11 85:7 88:5 128:3 148:23 162:23 162:25 163:22 165:4,10 contain [1] 147:3 contained [2] 3:7 6:10 content [1] 90:14 contention [2] 19:19 48:9 context [3] 13:4 22:13 27:21 continuation [1] 153:10 continue [10] 1:11 13:22 26:18 28:5 49:5 61:3 92:3 117:20,21 131:20 continued [3] 8:22 32:20 35:18 continues [3] 9:3 28:25 147:12 continuing [3] 8:23 32:23 112:15 continuously [1] 125:1 contraction [1] 134:12 contrasted [1] 91:23 contribute [1] 32:10 contribution [2] 71:5 75:23 contributions [2] 71:14 141:13 control [2] 118:25 141:9 controllable [6] 68:22 69:7 73:12,14 74:6,25 convene [1] 143:21 conversation [2] 106:15 142:19 Conversely [1] 92:16 convoluted [1] 125:10 copy [4] 3:12 5:9 116:5 119:10 core [1] 81:24 corporate [17] 20:20 64:18 65:4 68:6,10,25 69:19 70:5,16 71:8 72:11 73:10,15,24 75:5 86:21 106:20 corporation [1] 72:7 correct [56] 10:25 23:8 25:24 41:18 42:13,15,21 43:10,12,19,21 44:20 45:8 46:4,6,12 47:7,12 49:11 53:12 54:6 56:25 63:23 64:7,9,20 66:11 67:3,5,13,15 73:5,8 74:1 75:2 82:4 102:10 104:12 105:25 109:7 120:22,23 123:9,22,23 124:12 127:17,18,22 128:19,20 132:16 134:25 141:2	144:21 167:3 corrected [1] 65:9 correctly [1] 126:15 cost [67] 4:5 5:12,18 7:1 7:20 8:3 9:1 12:11 15:2 16:11,24 20:19 24:24 25:13,25 26:1 27:15 31:9 31:19 32:13,18 33:2,5 34:15 35:21,23 36:6,9 37:1 39:23 46:16,23 48:20 50:12 52:11 56:9 56:14 59:5 60:8 68:22 74:25 95:6 97:1,12,24 99:15 107:23 112:10,12 114:5 117:21,22 124:6 145:7 146:21 148:11 150:12 153:16 154:25 161:19 162:1,4,12,17,20 163:5,18 costing [1] 163:15 costings [1] 131:4 costs [42] 3:24 4:2,6 6:24 8:2,19 9:9,12,22,24 10:3 11:15 12:19 14:16 18:2 20:2,6 24:21,23 25:10 25:11,19 26:24 31:5,22 32:4 35:3,4 36:21 37:19 38:13 39:25 52:2 53:1 66:7 73:12,14 74:6 102:1 118:5 124:1 163:9 council [2] 20:24,25 counsel [3] 2:2 84:22 88:16 counting [1] 94:14 country [8] 31:17 50:2 53:12 98:6 102:13 111:1 111:8 140:2 couple [6] 18:16 92:19 110:1 127:5,12 132:10 course [4] 5:21 6:16 7:21 20:5 Court [1] 11:17 Cove [1] 57:3 cover [1] 127:8 coverage [3] 146:7,8 165:12 covered [2] 127:10 136:25 covering [1] 56:8 covers [1] 7:17 crater [1] 81:7 create [1] 119:20 created [1] 154:16 creating [1] 80:19 credit [18] 106:8 147:3 148:6,8,15 149:6,21,23 150:14,17,18,23,25 151:6 151:19 165:19 166:1,4 creditworthiness [6] 147:11,18 148:21 151:7 151:11 165:1 creditworthy [1] 147:13 Creston [1] 111:2 criteria [1] 120:1 critical [1] 38:25
---	--	---	--	--

cross [1] 5:7 cross-examination [2] 41:4 85:24 cross-examine [1] 4:2 current [23] 2:15 10:13 11:7 25:5 26:5 29:2 39:3 40:7 70:1,3 82:24 89:13 108:20 145:18 146:25 149:23 155:18 156:6 158:13 160:11 161:5 162:11 163:17 curtail [1] 36:21 customer [37] 3:18 6:19 7:7,16 11:4 12:17 14:1 17:18 19:25 24:14 25:8 26:9,17,19,20 27:5 30:13 36:19 39:23 55:4 56:7 60:8 64:13 66:19 68:14 68:16,23 79:24 80:12 81:4 92:6,9 94:15 109:11 117:22 133:4 146:21 customer's [1] 97:23 customers [64] 2:12,18 2:20 6:25 10:3,4 11:11 14:10,19,25 22:16 25:20 25:23 26:1,15,21 27:13 27:16 30:10 31:4 32:14 32:19,20,25 33:4,6,11 34:17,22 35:8,23 36:8 36:11 37:1,3,7,21 40:13 40:19 43:4 50:21 52:10 52:24 54:4,8,11 55:17 55:22 56:2,11 78:10 81:21 94:16,18 112:22 134:24 162:24 163:4,4,6 163:7,16,18 164:3 customers' [4] 26:24 27:2 39:25 40:5 cutting [1] 35:16 <hr/> -D- <hr/> D [1] 109:22 daily [1] 153:22 damage [2] 32:1 58:15 data [3] 15:14 96:12 124:10 date [1] 4:18 dated [3] 3:19 54:3 167:9 days [5] 5:21 20:7 61:25 118:8 130:17 DBRS [4] 147:14,16 151:21,24 deadband [2] 158:22 159:4 deadlines [2] 4:21 138:1 deal [7] 12:8 18:25 19:12 19:13 99:1 132:1 143:9 dealt [2] 46:15 97:5 debate [4] 49:5,17 76:17 108:4 debates [2] 121:3,16 debt [13] 33:2 101:16,18 101:22,22,25 102:7 106:5 146:9 150:14,21 151:8 165:15 decades [4] 30:16,19	33:18 58:19 December [5] 3:10,11 4:20 60:21,24 decent [1] 59:10 decide [2] 55:16 142:1 decided [5] 57:4 59:13 71:4,18 77:9 decimal [1] 53:3 decision [11] 10:24 11:6 15:10 40:16 96:5 147:19 148:9 154:24 155:11 166:11,13 decline [8] 30:18 93:16 112:6,15 133:7 134:9 135:20 161:22 declined [1] 30:16 declines [1] 132:12 declining [1] 112:14 decrease [2] 149:2,18 decreasing [1] 113:1 deduce [1] 66:14 deeply [1] 19:7 defer [2] 102:4 130:5 deferral [6] 3:23 4:5 14:12 32:7 59:14 98:18 deferred [3] 7:15 9:13 32:2 defined [3] 3:21 126:3,4 definitive [1] 105:17 degree [2] 154:16 155:5 deja [1] 16:6 delay [1] 89:6 delivery [1] 34:16 demand [4] 3:18 9:14 27:9 31:2 demeaning [1] 53:4 demographic [2] 116:25 132:18 demographics [13] 29:9 30:13 36:18 93:19 111:14 112:6 119:1 132:10,25 133:11 135:6 136:2,3 demonstrate [2] 11:23 162:13 demonstrated [1] 10:23 demonstrates [1] 25:14 deniable [1] 17:25 depart [1] 40:17 depend [1] 7:22 dependence [1] 129:15 dependent [1] 147:18 depreciation [30] 5:13 10:9,12,19,24 11:1,21 11:23 12:9,15 21:11,19 21:20,25 22:2,5 39:16 39:17,19,22 40:2,7 145:9 149:3 162:22 163:1,11 163:23 164:6 165:8 depth [5] 116:1,12 119:8 120:14 122:20 describe [2] 91:14 92:8 described [1] 50:15 design [1] 4:12	designate [1] 119:19 designed [1] 112:21 Despite [1] 159:11 detail [4] 53:2 102:3 127:10 131:24 detailed [1] 9:11 details [10] 31:24 58:25 93:11 97:3 103:17 105:5 106:5 113:23 114:11 156:14 deteriorated [1] 146:13 deterioration [4] 35:7 148:2 152:10 165:24 determination [3] 4:10 7:22 151:1 determined [1] 10:14 determining [2] 11:20 16:19 developments [1] 91:20 devise [1] 88:1 difference [7] 7:18 25:7 44:14 61:8 87:11 158:1 158:7 differences [7] 15:17,18 31:23 33:21 96:15 131:6 137:16 different [25] 33:24 39:5 47:21 55:6,11,20 60:21 61:15 100:7 110:18 111:3 111:11,15,16 112:9 115:6 115:12 125:20,21,22 130:3 138:3,6 152:25 159:14 differentials [1] 125:24 difficult [5] 30:2 35:2 35:20 90:17 129:11 difficulties [1] 159:6 direct [5] 41:10 53:4 54:11 72:15 159:7 directed [1] 105:19 direction [1] 105:20 directly [8] 55:19 73:17 73:19 75:2 86:19 109:1 130:25 150:25 director [10] 24:1 29:24 100:20 104:10,17,19,20 104:20 105:4 106:20 Directors [2] 70:20 72:13 disagree [3] 103:2,7,8 disclose [1] 105:9 disclosed [1] 57:10 discontinuance [1] 8:16 discontinue [2] 9:4 28:21 discontinued [1] 155:15 discontinuing [1] 38:7 Discoveries [1] 1:8 discuss [4] 3:7 122:2 149:7 159:15 discussed [1] 159:6 discussing [1] 81:17 discussion [9] 39:21 97:9 111:22 122:9 127:13	128:16 129:22 130:2 131:25 discussions [4] 118:12 121:3,16 131:21 dismiss [1] 142:14 display [1] 156:23 disregard [1] 165:25 disrespectful [1] 19:7 disruptions [1] 18:24 distribution [8] 31:18 109:10,16,25 110:8,11 110:24 124:8 Diversified [1] 21:13 diverted [1] 130:25 divided [1] 149:14 dividend [1] 101:24 dividends [1] 80:10 document [10] 50:21 51:10,14 53:22 54:3 72:17 104:3 114:6,22 122:15 documents [3] 1:21 50:17 119:20 doesn't [4] 17:4 62:2 137:5 143:21 dollars [17] 11:5 13:5,7 13:9 32:5 40:14 42:12 43:8,9 44:16,17 46:1 59:7 80:22 149:15 163:2 163:13 domestic [1] 20:22 done [9] 35:18 46:22 47:23 59:17 70:16 76:2 82:2 100:15 118:1 doubled [1] 16:10 doubling [1] 16:24 doubt [1] 150:10 down [24] 6:21 7:8 15:7 16:10,24 17:1 18:15 52:25 53:2 57:2 61:13 71:2 91:6,7 98:22 111:8 112:24 117:8 119:22 126:17 139:11 146:22 158:16 161:8 downed [1] 58:22 downgrade [3] 149:5 152:12 165:19 downgraded [2] 147:24 165:21 Dr [31] 2:1 20:14,14,23 21:4,7 34:6 48:7 149:25 151:12,13 152:14,19 153:4 156:9,12,13 159:9 159:12,15,24 160:1,4,13 160:19,23 161:1,10,14 162:18 164:8 dramatically [1] 90:21 draw [2] 78:5 125:18 drive [1] 58:19 driven [5] 13:2 52:20 93:8 117:15 125:16 drivers [1] 24:10 drop [3] 134:6 158:24 165:13 due [2] 20:5 31:5	dunk [1] 75:21 during [8] 5:17 12:11 20:7 46:13 85:16,24 88:11 130:21 Dwanda [1] 1:6 dynamics [2] 93:18 115:11 <hr/> -E- <hr/> e-mail [1] 63:9 EAL-1 [1] 24:14 Earl [8] 12:3 22:23 23:1 41:4 61:19 62:2 126:24 132:9 early [10] 35:14 36:5 115:10 116:11,24 118:1 130:17 138:21 142:7 166:11 earn [13] 13:4,7,9 34:21 34:25 35:5,11 37:17 46:21 138:10,10 147:1 148:11 earned [1] 82:5 earning [4] 37:7 57:25 113:20 138:8 earnings [31] 15:21 46:13 68:24 69:1,4 73:2 73:4 74:4,24 75:6,13,16 76:1 79:21,22 80:3,13 80:16,19,21,25 81:2,7 81:12,14,15,18 83:4 98:19 138:7,14 Eastern [1] 61:13 easy [2] 79:1 142:24 economic [3] 9:8 35:15 35:20 economy [9] 25:14 27:9 31:3 91:13,14,17 92:1 92:24 93:7 Edison [1] 16:15 Edward [2] 24:4 101:2 effect [2] 153:9 163:10 effective [2] 51:19 130:16 effectively [3] 81:6 84:13 163:16 effects [2] 149:8 163:20 efficiencies [2] 10:7 153:15 efficiency [13] 8:19 9:2 10:1 26:9 27:4 38:12 122:25 123:2,5,8,15,21 124:15 efficient [3] 25:15 26:11 27:12 effort [3] 75:22 76:7 125:3 efforts [2] 36:18,22 either [11] 38:1,2 74:16 81:7 89:6 97:12 100:20 147:2 156:4 162:19 164:2 electric [19] 13:14 24:2 30:10 33:21 93:25 101:5 104:16,19,20,23 108:17 108:18 109:12 111:16
--	---	---	--	---

124:8 125:22 129:15 152:7,20 electrical [2] 26:12,14 electricity [6] 2:15 25:5 26:23 33:22 40:14 93:23 electrics [1] 141:18 electronically [1] 54:7 ELG [5] 10:16,24 11:6 40:7,16 elsewhere [2] 30:25 124:8 email [1] 122:5 emails [2] 119:22 166:15 embarked [3] 114:10 120:14 131:9 embedded [1] 7:16 emerges [2] 9:6 39:13 employees [1] 116:22 employment [1] 14:17 encapsulate [1] 114:18 encompass [1] 84:13 encountered [1] 30:14 end [2] 5:14 17:22 ending [1] 94:1 endless [1] 88:25 energy [9] 3:18 6:24 7:1 24:21,24 26:20,22 52:2 110:20 engage [2] 89:3 97:18 engaged [2] 47:24 48:4 engineer [2] 21:15 139:6 engineering [6] 12:18 36:2 100:11 104:13,15 118:24 enjoys [1] 13:25 ensure [9] 27:6,11 35:18 36:6 81:18,18 96:3,24 118:21 ensures [1] 25:25 enter [4] 51:1,6 157:1 159:18 entered [5] 3:13 5:9 6:12 53:24 164:15 entirely [1] 142:2 entitled [4] 11:18,19 37:16 78:4 entitlement [1] 37:19 environment [9] 13:25 14:20 29:8,15 98:8 106:14 115:19 137:2,8 environments [1] 125:21 envision [1] 93:9 equal [3] 10:16 22:9 111:21 equally [2] 136:10 149:19 equitable [1] 26:1 equities [1] 21:3 equity [10] 7:6,23 8:4,9 8:12 13:3,10 14:21 16:20 25:3,6 27:19 28:4,6,11 28:16,20 33:2,10,15,16	34:7,11,20,20,23 35:1 42:18 43:19,24 46:3 47:7 50:13 52:11 53:10 56:9 56:14 80:17 82:11 83:13 101:17,18,22,22,25 102:7 103:1,3,6,14 104:23 105:10 106:1,5,12,23 108:16,21 126:11 145:23 146:4,6,21,23 148:14,25 149:2,11 150:3,16,22 151:17 152:13,18,22 153:1,2,6,13,25 154:4 157:9,11,14 158:4,15,17 159:3,23,25 160:2,14,15 161:9,12,19 162:1,4,17 162:20 165:7 er [1] 93:17 erode [1] 147:5 especially [2] 25:12 82:21 essence [3] 14:4 15:4,6 essential [2] 37:20 55:25 essentially [5] 6:21 33:19 55:4 100:2 157:21 establish [2] 2:11 28:19 establishing [3] 37:8 52:5 53:15 estimate [1] 157:8 estimated [3] 153:24 158:17 161:9 estimates [1] 9:25 estimating [2] 42:7,7 Europe [1] 139:2 evasive [1] 129:7 event [5] 7:1 57:24 60:17 117:4 142:21 events [1] 56:20 eventually [1] 35:6 everybody [6] 1:3 2:8 70:2 91:12 127:2 143:22 evidence [20] 1:10 5:11 5:14,18 7:19 12:9 15:17 16:1 62:17 95:14 96:16 96:18 97:6 143:18 144:24 150:1 151:13 160:5,19 164:23 examination [6] 20:6 88:11 104:5 126:24 132:9 155:1 EXAMINATION-IN-CHIEF [2] 23:1 144:16 examine [2] 5:8 43:2 examined [2] 4:16 40:6 examines [1] 11:14 example [8] 26:19 31:25 33:22 35:10 126:3 128:5 130:20 148:13 exceeding [1] 32:2 exception [2] 30:3 78:2 excess [5] 50:1 66:18 98:19 138:6,13 excludes [1] 146:19 execute [1] 46:17 executive [16] 12:4 23:6 65:7 69:20 71:16 72:20	80:24 89:19 97:12 100:21 121:4 129:23 137:21 139:25 140:17 141:14 executives [16] 17:17 18:3 19:22 20:3 63:21 64:2,16,23 66:6 67:12 73:3 77:11 82:9 83:2,9 84:4 exercise [4] 11:18 116:18 116:19 117:14 exercises [1] 116:20 exhibit [15] 3:14 5:10 24:14 42:8 43:5 145:16 145:16 146:18 147:20 156:23 157:7 159:14 164:13,18,22 exhibits [2] 23:18 145:3 exist [1] 155:22 existed [1] 8:22 existing [4] 4:5 155:17 164:21 165:16 expand [1] 95:20 expanded [1] 26:20 expect [7] 33:15 34:21 60:23 61:4 67:9 134:4,6 expectations [2] 26:19 27:2 expected [1] 114:3 expects [1] 13:3 expenditures [1] 31:9 expense [15] 3:22 11:8 11:21,23 12:10 14:14 16:12 21:25 31:6 49:18 125:1 126:17 154:24 163:11,18 expenses [1] 40:10 experience [8] 10:23 25:20 31:25 33:20 128:22 130:12,15 153:19 expert [16] 12:12 20:12 20:13 34:5 47:24 48:1 48:20 49:2 50:5 97:5,16 97:18 100:2,4 107:15 153:4 experts [10] 3:4 34:6 46:24 48:4 49:20 50:8 97:6 100:3,5,14 explain [11] 24:9 70:7 70:10,17 71:23 96:6 149:8 150:8 152:17 153:8 155:16 explained [2] 6:8 126:14 explanation [1] 95:25 explore [2] 128:2,21 exposed [1] 14:24 exposure [1] 156:2 expressed [1] 76:12 extensively [1] 21:19 extra [1] 82:10 eye [1] 136:17	faces [1] 127:21 facilitated [1] 3:6 facilities [1] 109:12 facing [1] 113:6 fact [15] 14:7 16:10 47:3 55:13 56:5 66:24 67:10 67:22 76:20,24 78:5 95:9 106:22 131:16 154:21 factor [2] 8:12 27:3 factored [1] 155:2 factors [8] 48:15,18 81:5 88:18 113:5 115:18,23 129:17 fair [31] 13:16 16:19 21:8 28:20 33:10,16 34:7,10 34:19,21 35:6,11 45:12 52:5 53:15 54:25 56:15 97:24 98:3 104:6 110:14 122:13 131:10 150:24 151:2 152:14 153:3,13 154:5 155:20 156:5 fairly [4] 14:1 71:1 115:21 117:25 fairness [1] 33:13 faith [1] 11:20 fall [4] 86:19,20 108:3 158:21 falling [1] 76:5 familiar [2] 51:9 113:23 family [1] 125:6 far [5] 58:17 63:4 102:14 109:24 130:19 favour [1] 22:10 fear-monger [1] 135:17 feature [2] 148:17 162:25 features [1] 17:7 feeling [1] 119:15 fell [3] 73:11 75:22 158:23 felt [2] 55:25 72:9 few [3] 33:20 41:11 82:3 fibre [1] 131:9 field [1] 100:14 figure [2] 83:20 87:19 figuring [1] 118:16 filed [17] 3:3,11 5:24 9:15 22:2 34:4 49:3 51:18 52:17 103:20 109:4 120:4 122:11,16 134:3 153:3 154:23 filing [5] 50:22 51:18 67:11 77:4 122:7 filings [1] 131:14 final [2] 7:21,24 finally [3] 12:16 155:3 165:3 finance [7] 12:7 20:15 20:17,20,22 144:19,23 financial [99] 5:2 9:5 12:7,9,10 16:17 34:14 34:18 35:19 36:7,23 38:2 39:11 41:15,18,23 42:23 43:1 45:13 47:22 59:12	68:21 69:4,10 73:1,12 75:15 80:3,15 81:24 98:11 99:9 101:13,15,16 102:2,6,8,12,17,24,25 103:4,5,6 105:13,24 106:3,10,25 107:5,6,14 128:7 129:24 131:4 144:20 145:6,6,11,11,14 145:17,19 146:12,15,25 147:6,8 148:3,16,18 149:17 150:10 151:4 152:3,11 154:17,20 155:4 155:6,18 156:7 157:6,16 160:7 161:13 162:5,11 162:23 163:20,22,25 164:5,11,19 165:9,24 166:2 finding [4] 91:12 96:5,7 96:9 findings [1] 95:20 fine [2] 51:6 88:6 finished [3] 114:7 142:11 142:15 finishing [1] 142:6 firm [1] 21:13 first [22] 12:4 20:13 22:4 22:23 23:23 32:16 50:24 68:16 70:18 86:11 96:10 123:13 127:8 145:20 147:13 149:7,13 154:3 156:17,22 157:9 164:20 fisheries [1] 35:15 five [15] 10:20 21:22 30:4 36:9 52:4 62:7 71:11 76:3 78:21 100:8,18 112:18 113:7 116:14 118:22 five-day [1] 59:4 five-year [1] 10:17 fixed [1] 102:1 fizzle [1] 62:2 fizzled [1] 61:24 fledged [1] 126:4 Fleming [2] 12:14 22:2 flexibility [1] 112:10 floor [2] 160:6 161:14 flow [6] 146:8,9 147:4 163:25 165:13,14 flow-through [1] 31:19 flowed [1] 6:25 flows [1] 154:15 fluid [1] 120:11 focus [5] 26:7 80:5 102:23 137:24 154:19 focused [2] 27:14 37:5 focuses [1] 44:11 focussed [1] 99:2 follow [1] 39:5 follow-up [1] 127:12 following [5] 2:25 5:14 28:15 35:14 50:22 follows [2] 15:10 88:23 force [2] 10:1 134:18 forecast [30] 3:19 4:7 9:14 30:18 42:15,21
---	--	--	--	--

-F-

face [4] 14:25 16:8 29:6
31:5

44:12,12,14,15 45:25 67:8 91:9 93:16 143:17 145:19 146:2,17 147:5 155:4 157:18,20,23 159:1 160:8,12 161:16,16 162:17,20 forecasted [6] 21:3 131:14 133:21 146:23 164:19 165:2 forecaster [1] 133:1 forecasters [4] 93:14,15 133:1,22 forecasting [9] 14:13 14:16 42:10,11,17 132:21 135:24,25 146:5 forecasts [2] 143:14 146:19 foregoing [1] 167:2 foremost [1] 32:16 foreseeable [1] 92:2 form [1] 90:3 forma [4] 156:15 157:5 157:7 159:5 formal [2] 122:15,15 former [1] 101:4 formula [68] 7:11 8:5 8:15,17,17,24 9:4,7 17:2 17:4,12 21:10 28:1,2,4,5 28:9,14,21 38:8,11,19 38:22 39:2,8,10 145:9 152:23,24 153:1,8,11,12 153:19,24 154:2,9 155:9 155:12,15,18,19 156:4 156:15,18,22 157:8,20 158:3,11 159:4,8,10,12 159:16 160:6,10,15,18 160:21 161:4,11,18,24 162:3,9,16,19 formulas [7] 155:21 156:5,11,16 159:13 162:7 162:13 forth [1] 122:6 Fortis [38] 24:2,4 29:24 32:1 47:16 100:21 101:5 101:8,9,11 102:12 103:16 103:17,19,22 104:13,21 105:11,13 108:19,21,22 109:1,5,8,10 110:15,18 110:19 111:20 113:19,20 114:20 115:17,17 128:4 128:17 152:5 forward [22] 17:5 20:5 22:15 46:23 48:8 49:20 55:12 70:25 71:18 86:11 87:5,21 88:7,13 89:4 90:20 91:8 97:20 122:17 131:5 148:23 156:9 found [6] 9:16 127:16 129:10,11 157:22 160:10 four [13] 10:20 29:25 59:10,19 68:8 76:3 101:2 113:7 128:23 136:1 145:5 145:9,10 fourth [1] 52:21 free [3] 14:1 157:13 160:1 frequency [2] 17:8 68:19 Friday [2] 4:24,25	friend [4] 83:18 84:14 86:11 87:20 fulfilled [1] 38:13 full [7] 31:19 53:5 90:13 90:25 126:3 154:25 156:14 fully [3] 90:20 94:3 126:3 function [1] 38:14 fund [3] 32:22 33:1,17 fundamental [4] 17:13 33:7 86:3 156:17 funded [1] 17:18 funds [2] 58:25 101:24 furnace [1] 94:2 future [22] 11:9 27:8 31:22 32:3 37:4 39:11 40:4 52:6 88:7 90:22 92:2 112:17 117:3 135:14 148:21 151:9 154:15 163:5,6,8,16,19 future" [1] 116:17 <hr/> -G- <hr/> gains [1] 17:10 Gannett [2] 12:14 22:2 garages [2] 92:13 94:21 Gary [2] 12:16 122:5 gas [4] 13:14 115:12 129:16 152:8 gear [1] 60:7 gee [1] 76:13 general [20] 1:4 2:10 13:19 15:8 17:8 22:3 23:10 25:1,23 27:23 41:16 50:22 51:19 52:16 52:17 91:22 92:7 135:22 147:16 167:4 generally [12] 29:15 100:21 102:6 137:1,2,4 137:5,8,11,13 143:14 156:3 generate [2] 89:12 110:22 generated [1] 119:12 generating [2] 110:3 112:25 generation [5] 14:3 15:21 109:18 110:5,10 gentlemen [2] 18:23 120:25 Gerard [1] 1:20 Gibbons [1] 1:7 given [14] 68:13,17,23 68:24 85:18 88:11 107:11 134:5 139:14 155:5 160:11 161:14 162:2,9 giving [2] 46:20 87:17 Glenda [1] 1:7 global [2] 117:7 126:13 Glynn [14] 2:5,6 6:7 9:10 50:25 51:5 53:23 79:6 79:10 143:2 156:25 159:17 164:14 166:14 God [1] 144:13	goes [3] 55:17 95:5 138:13 gone [3] 70:2 130:20 131:12 good [21] 1:3,14,23 2:7 11:20 17:16 23:4 26:13 26:16,19 41:6,8,25 59:24 59:24 115:5 118:21 123:20 126:25 127:1 130:19 goodness [2] 112:19 125:8 governance [5] 70:21 71:6 72:12 75:20 120:19 governing [2] 20:24,25 governments [1] 139:4 GRA [5] 11:13 17:11 21:7 42:25 67:11 grant [6] 5:2,6 9:10,15 9:19 79:24 graph [1] 136:7 Grate's [1] 57:3 great [2] 16:6 137:3 greater [4] 29:11 44:23 45:6 114:4 greatly [1] 50:6 Greene [12] 9:10 84:20 84:21 85:2 86:4 88:4,21 89:5 126:24 132:4,5 136:25 Greg [1] 2:2 grievous [1] 85:1 gross [4] 13:15 92:10,11 94:20 group [12] 10:16 22:9,10 65:25 76:7 117:16 118:9 140:10,15 141:9,9,12 grouping [2] 140:14,22 growing [1] 134:17 grows [1] 39:22 growth [7] 14:1 30:25 92:6,10 133:8,10 134:10 guess [19] 60:25 61:12 66:13 71:14 75:11 80:23 91:13 92:5 111:17 114:17 115:13 116:9 123:18 130:17 133:5 136:19 137:15 138:16 141:7 guide [1] 116:16 guy [1] 137:4 guys [1] 62:18 <hr/> -H- <hr/> half [9] 13:4,7 35:17 42:12 79:11,13 138:11 140:6,7 half-hour [2] 1:12 5:17 hand [1] 158:25 handle [3] 61:6,7,7 handles [1] 137:23 hands [1] 118:22 happening [5] 62:21 92:21 93:21 94:11 136:17 happenstance [1] 76:10	happy [4] 6:16 59:2 88:1 127:2 harassment [1] 19:10 Harbour [1] 91:21 hard [3] 89:12,15 138:23 harder [1] 94:3 harsh [1] 29:8 haul [1] 93:13 HAY [6] 72:4,10 140:1,1 140:5 141:22 Hayes [1] 1:20 heading [3] 94:7,9,10 hear [5] 12:1,12 48:1 49:13 127:3 heard [2] 95:11 167:4 hearing [23] 1:5 2:25 4:6 4:17,18 6:18 14:10 17:23 19:20 20:8 22:18 38:18 53:17 56:16 84:22 85:16 88:8,16 93:9 100:17 138:7 153:11 155:13 hearings [4] 1:10 8:25 38:12 88:25 heat [3] 30:10,11 93:25 heating [4] 94:17,25 111:16 115:12 heavily [3] 91:23 93:13 100:12 Hebron [1] 91:21 heck [2] 87:19 137:6 held [6] 2:21 3:9 17:11 20:18 24:3 144:21 help [2] 113:25 144:13 helpful [2] 74:14 97:9 hereby [1] 167:2 high [10] 13:6,8 26:17 27:9 31:2 71:15 81:1 107:10,10 108:19 higher [21] 11:8 14:24 15:2 27:25 31:5 40:3,11 40:14 71:3 81:12 103:3 105:10 107:4 111:20,22 113:4 127:25 129:1,19 133:20 163:18 highest [10] 13:12 47:5 47:11,14 48:8,11 50:1 53:12 103:11,15 highlight [1] 119:6 highlighted [1] 52:22 highly [1] 56:2 hired [2] 49:24 116:23 hiring [2] 16:10 90:23 hit [5] 48:19 58:17 61:14 61:14,14 holder [1] 66:8 holders [1] 151:8 holds [1] 20:16 Holyrood [2] 26:25 31:8 homes [5] 30:11 94:6,24 135:9,11 honest [2] 114:9 137:19 honestly [2] 104:24 114:11	hooked [1] 92:14 hope [1] 62:2 hopefully [1] 48:2 hoping [1] 58:11 hot [2] 92:24 121:8 hour [3] 5:19 79:11,13 house [1] 94:2 houses [3] 92:12 134:14 135:15 HR [4] 70:21 117:15 119:4,18 Huge [1] 93:21 human [3] 116:15 117:15 118:22 hundreds [1] 100:6 hurricane [5] 32:6 57:4 58:16 61:19 62:25 hurricanes [2] 62:4 63:6 hydro [4] 31:9 109:11 110:3 125:20 <hr/> -I- <hr/> Ian [2] 1:18 23:1 ice [15] 30:6 56:22,25 57:7,12,16,22 58:3,6,10 58:10,13 61:6,8 111:10 idea [5] 65:12 82:19 111:10 114:7 118:7 ideal [1] 81:23 identified [1] 116:15 identify [1] 2:22 Igor [10] 32:6 56:23 57:4 58:7,17,17 59:3 61:9 75:24 112:14 immediate [3] 35:4,21 36:24 immediately [1] 36:8 impact [22] 35:4,12,22 36:7,25 41:22 56:1,7 71:5 92:22 117:9,10 120:8,9 139:2 151:11 162:23 164:4,10,11 165:4 166:3 impacted [3] 36:10 57:1 73:13 impacts [3] 35:24 37:2 55:20 implementation [1] 10:15 implemented [1] 164:6 implications [4] 34:10 106:10 107:6 148:20 implied [2] 102:1 151:14 imply [1] 127:24 important [6] 7:7 8:12 32:13 33:6 36:3 149:19 improve [3] 36:4 117:21 125:1 improved [3] 124:2,7 124:19 improvement [1] 37:6 inadequate [1] 137:9 Inc.s [1] 167:4
--	---	---	--	--

<p>incenting [2] 18:3 20:3 incentive [18] 17:9,16 17:19 19:21 63:19,20 64:3,6,10,15 65:6,18 72:18 74:22 80:24,25 81:10,11 Incidentally [1] 20:23 incidents [1] 68:20 inclined [1] 105:16 include [5] 37:23 74:24 77:9 148:24 163:1 included [1] 55:14 includes [6] 2:17 69:7 74:24 81:4 87:6 145:16 including [3] 12:9 15:19 32:9 inclusively [2] 73:21,23 income [5] 13:4,10 42:11 43:7 46:3 inconsistent [1] 38:3 incorporate [2] 158:11 160:21 increase [41] 2:15 6:19 6:24 7:4,15,17 8:1 13:1 24:8,10,13,20 25:2,8,12 25:19,21,22 26:23 27:20 36:20 38:12 43:17 52:7 52:23 64:11 101:24 133:24 134:9 136:14 149:17 155:8 158:25 159:2 161:17,19,23 162:14,16,18 163:14 increased [8] 7:12 8:25 27:10 32:4 36:16,22 153:20 155:20 increases [5] 2:17,19 11:2 31:5 55:18 increasing [4] 39:24 113:1 133:25 136:9 incremental [1] 44:16 incumbents [1] 71:4 indeed [4] 14:10 57:7,24 72:20 index [2] 160:22 161:3 indicate [3] 34:6 52:5 151:25 indicated [23] 3:9 5:15 24:12,22 27:18 28:1,9 29:23 36:3 104:1 124:9 151:14,18,21 152:2,9,22 153:1,24 158:19 160:12 165:18,20 indicates [1] 147:23 indication [2] 134:5 139:14 indicator [1] 95:13 indirect [1] 141:3 individual [10] 64:17,23 65:5 69:20 70:6 71:8 74:3,5,23 125:9 individually [1] 129:8 individuals [3] 77:18 99:20 119:24 industrial [2] 72:8 140:12</p>	<p>industry [1] 91:21 infeed [1] 31:7 influenced [1] 155:10 influences [1] 139:9 information [17] 3:2 51:7 52:12 53:24 82:16 83:19 85:7,14,17 86:2 97:20 103:20 123:4,7,14 135:6 160:25 infrastructure [2] 111:12 139:4 initial [1] 131:22 injecting [1] 139:5 injury [1] 68:19 input [1] 105:17 insight [1] 84:18 insinuate [1] 121:25 insinuation [1] 121:20 insofar [1] 12:10 installed [2] 33:23,24 instance [7] 75:13 77:16 109:20 114:2 125:4,5 133:18 instead [3] 48:23 129:9 154:18 instruct [1] 97:16 instruction [1] 97:11 integrated [3] 110:9,16 110:21 integrity [18] 34:15,18 35:19 36:7,23 38:2 41:18 41:23 43:1 45:14 80:3 80:16 145:7,12 146:12 147:9 148:19 164:5 intended [1] 153:14 intends [2] 12:2 142:20 intensification [1] 62:25 intensive [2] 58:14 60:24 interest [8] 40:5,18 146:7,8 151:9 164:2 165:12,13 interested [1] 55:18 interesting [1] 107:24 interests [5] 11:9,10 20:19 37:21,23 international [2] 20:20 20:22 interpret [1] 161:10 interruption [1] 19:10 interruptions [1] 19:14 intervenor [1] 2:23 introduce [2] 1:16 23:10 introduced [1] 84:23 introduction [5] 23:12 95:5,7,11 123:1 invested [1] 52:3 investing [1] 52:1 investment [5] 32:21,23 33:1 35:17 52:6 investor [5] 28:8 106:21 147:14 152:20 154:6 investors [5] 33:15,16</p>	<p>34:20,23 37:21 involved [2] 119:18,19 involves [1] 75:23 irrelevant [1] 111:23 Island [2] 24:5 101:2 isolated [2] 29:7 85:14 issue [19] 10:9,10 19:5 39:11,15 40:6 50:12,13 50:15 51:16 52:10 55:8 56:10 80:19 113:2,10 139:25 140:3 150:11 issued [1] 52:15 issuer [1] 150:9 issues [12] 3:7,15 4:11 4:15 6:11,15 8:2,3 21:21 25:25 39:17 113:13 issuing [2] 150:18,20 item [4] 10:8 51:7 53:24 103:20 items [3] 9:18,22 106:9 itself [2] 41:14 97:25</p> <hr/> <p style="text-align: center;">-J-</p> <hr/> <p>Jacob [1] 21:12 Jacqueline [1] 2:4 James [3] 1:7 12:13 34:6 January [5] 1:1 4:24,25 167:5,10 Jersey [1] 152:8 job [3] 27:1 38:25 123:20 Jocelyn [2] 12:6 144:16 John [1] 12:14 John's [6] 91:6 92:15 117:12 134:16 167:6,9 Johnson [125] 1:24,25 12:23 18:6 19:16,18 41:2 41:4,5,9,24 42:5,16,22 43:14,22 44:5,10,21 45:1 45:5,9,17,23 46:8 47:1,2 47:13 48:5 49:8,12,22 50:10 51:1,3,8,13,23 53:7,19 54:2,9,17,22 55:3 56:4,17 57:6,13,19 57:23 58:5 60:11,16,22 61:11 62:1,10,14 63:10 63:17,24 64:14,21 65:16 65:23 66:12,23 67:6,17 67:21 68:4 69:6,11,17 70:12 71:20,24 72:14,23 73:9,18,22 74:2,10,15 74:20 75:3,10 76:11,15 76:23 77:14,21 78:8,14 78:16,20,25 79:4,18,19 83:1 84:6 86:16,23 87:2 87:10,24 89:17 90:4,10 94:13 102:4 104:8 113:14 114:16 115:24 120:12 126:8,19 127:5,13 143:25 144:6 joined [2] 1:6 2:8 Joining [1] 1:19 joint [3] 130:10 131:18 154:12 journeyman [1] 90:25 JP [3] 156:23 159:15</p>	<p>164:13 judgment [2] 11:18 71:17 Judy [2] 167:2,11 June [1] 7:13 jurisdiction [2] 17:14 31:13</p> <hr/> <p style="text-align: center;">-K-</p> <hr/> <p>Kathleen [2] 12:13 34:5 keep [8] 57:24 60:5 81:22 83:5 130:21 132:1 133:12 136:17 keeping [1] 134:13 Kelly [53] 1:17,18 6:6 22:21 23:2,3,9,16,22 24:6,15 26:3 27:17 28:22 29:19 31:11 32:12 33:12 34:9 35:9 36:12 37:11 38:5 39:14 40:20,24 41:10 82:14 83:15 84:11 85:9,25 86:1,7 87:4,14 88:14 89:18,24 90:8 103:24 142:10,17 143:11 143:16,23 144:16 148:5 157:3 159:21 164:17 166:7,22 Kelowna [2] 111:1 112:23 key [17] 24:10 27:3 32:23 46:20 48:19 50:12 52:20 53:17 61:9 96:5,7,9 99:6 147:3,5 148:12 164:19 kick [1] 60:6 kicked [1] 14:12 kilometres [1] 109:25 kind [4] 19:10 37:13 141:17 144:7 Kirby [1] 2:2 knew [1] 139:19 knocking [1] 138:14 known [3] 47:14 112:9 121:1 Kootenay [1] 101:4</p> <hr/> <p style="text-align: center;">-L-</p> <hr/> <p>labour [7] 10:1,3 36:17 124:2,6,7,19 Labrador [14] 30:1,6 30:14,20 31:7 33:25 34:2 51:17 56:19 91:20 125:20 134:7 167:7,9 lack [5] 16:1 95:14 96:19 162:9,13 ladies [2] 18:22 120:24 laid [5] 55:22 81:14,16 115:1 120:2 lake [1] 111:9 large [4] 25:11 112:22 116:22 163:5 largely [2] 15:2 38:13 larger [2] 25:21 93:7 largest [2] 6:22 106:20 last [28] 14:10 15:8 17:11</p>	<p>27:23 28:23 38:18 41:11 41:15 42:25 49:13 50:18 62:7 63:6 69:14 82:3 92:7 96:5 127:17,21 135:21 138:19 139:11 145:15 146:18 147:16,21 155:1 165:3 late [6] 28:13 60:17 85:9 85:19 93:17 154:10 latest [3] 147:19,20,22 Lawrence [2] 2:1 20:14 lay [2] 51:21 125:23 lead [3] 107:18 149:19 149:22 leading [1] 118:11 least [11] 5:19 27:15 32:18 34:15 53:8 66:16 66:17 67:9 114:4 118:15 136:10 leave [7] 18:8,14,17 39:7 138:17 139:23 162:19 leaving [1] 119:25 led [1] 152:23 left [2] 14:18 59:9 legitimate [1] 83:14 less [21] 10:3 11:5 15:22 16:3 81:22 95:16 96:21 98:21 102:7,11,15,17 103:4 105:12,24 106:25 110:8 112:10 140:7 152:21 158:19 lessened [1] 38:20 letter [2] 50:13 56:9 letters [1] 4:24 level [6] 21:25 133:20 134:20 147:25 151:25 165:22 levels [6] 15:19 35:5 36:19 38:1 53:3 134:22 lies [1] 11:22 life [4] 10:16 22:9,10 40:10 Light [1] 152:6 lights [2] 60:5 81:22 likely [4] 135:5 147:24 150:14 165:20 Likewise [1] 117:18 limit [1] 156:1 limitations [1] 59:17 line [40] 42:9,17 43:5,15 44:25 56:1,6 69:13 72:6 115:16 121:6 123:13,24 124:5,16 140:9,10,12,18 140:22 145:21 146:5,6,7 146:9,22 157:10,16,22 157:23,25 158:16,19 159:22 160:1,11 161:8 165:11,12,14 lines [6] 125:2 126:17 147:2 150:2 151:13 161:4 link [1] 53:5 liquidity [1] 148:2 live [2] 53:6 136:12 lives [1] 22:6 load [4] 94:17 113:11,11</p>
--	---	---	---	--

<p>115:12 local [3] 91:14 92:24 93:6 location [2] 117:10 119:24 locations [1] 119:2 logic [1] 36:13 logically [2] 124:13 162:3 long-life [1] 32:21 long-lived [1] 33:17 longer [4] 17:16 35:24 78:15 90:24 look [87] 20:5 22:15 24:14 48:15,16,17,22 49:19 50:8,8 55:12 59:15 65:24 66:2,13 68:9 69:19 70:25 72:24 75:14,20 76:13,19 81:2,20 91:8 91:17,19 92:9,10 93:12 94:18 95:24 98:7,11,15 98:25 99:6,22 100:11 102:2 105:15 107:25,25 109:21 111:23 112:2,2,3 113:5 114:25 115:3,11 115:13,21 117:5,13 118:23,24 119:1,1 124:14 124:24 125:14,15,17,21 126:12,13,16 129:12,13 129:14 135:9,13,13,18 136:5,15 137:20,24 141:1 141:2 142:24 145:20 148:8 156:21 looked [7] 47:9 116:19 118:1 125:7 128:6 129:7 160:24 looking [18] 26:21 44:6 44:15 59:3 71:4 83:18 84:14 86:14 89:17 92:5 117:2 122:18 128:24 133:21 135:16 138:5 139:7 165:9 looks [1] 50:5 loose [1] 87:17 Lord [1] 1:14 losing [2] 120:10,11 low [5] 13:23 14:5,20 37:9 108:18 lower [16] 14:23 26:22 47:17,19 81:12 103:5 111:21,23 113:4 128:1 129:5,20 151:15,23 154:6 165:16 lowest [1] 28:7 luck [1] 59:24 Ludlow [145] 12:3 13:20 22:23 23:1,5,7,14,20,25 24:7,11,18 26:6 27:22 29:3,22 31:14 32:15 33:14 34:12 35:13 36:14 37:14 38:6,10 39:15,20 40:21,22 41:4,6,7,13,19 42:2,9,14,20 43:11,20 44:2,7,8,18,24 45:3,7,15 45:19 46:5,10 47:4,8,18 48:14 49:10,15 50:3 51:10,11,15 52:14 53:13 54:5,14,20,24 55:9 56:13 56:24 57:11,15,21 58:2</p>	<p>58:8 60:14,19 61:1,17 62:6,12,20 63:3,15,22 64:8,19 65:11,21 66:10 66:20 67:4,14,19 68:2,7 69:3,9,15 70:9,14 71:22 72:1,15,21 73:6,16,20 73:25 74:8,12,18 75:1,8 75:11,18 76:14 77:3,19 78:1 79:20 80:8 82:7 90:11 95:7 97:22 100:25 101:14 102:23 104:4 107:17 109:9 113:18 115:25 116:9 119:14 120:14 121:19 122:25 126:21,24,25 132:9,11 153:18</p> <hr/> <p style="text-align: center;">-M-</p> <p>MacDonald [6] 156:12 156:13 157:12,13,24 158:9 MacDonald's [9] 156:9 156:22 158:21 159:4,13 160:10,18 161:4 162:15 Madame [1] 144:11 main [1] 26:8 maintain [5] 30:23 34:14 36:23 134:19 166:1 maintained [2] 8:10 135:16 maintaining [7] 8:24 27:4 30:8 34:17 36:19 131:3 146:11 maintenance [7] 130:14 131:16,17,22 147:8 148:16 164:25 major [3] 92:16 93:8 140:2 majority [3] 94:24 109:24 110:23 makes [1] 117:17 manage [3] 59:11 76:2 112:12 managed [2] 26:11 60:9 management [13] 11:17 17:18 20:15 34:13 35:1 37:24 46:15,16 59:24,25 81:24 112:13 120:18 managers [17] 18:3 19:22 20:4 63:21 64:2 64:16 65:25 66:17 67:2 67:13 69:21 72:20 75:4 77:11 82:9 83:3,9 managing [2] 27:5 154:19 manner [1] 148:11 March [4] 2:16 56:25 58:10,22 margin [1] 151:8 Maritime [8] 24:2 101:12 104:16,19,20,23 125:22 129:15 marked [2] 24:16 156:24 market [15] 8:21 34:2,3 39:3,12 93:23 110:21 113:11 115:3 139:8 155:4 155:19 156:7 162:5,11</p>	<p>markets [20] 9:5 20:21 33:2 34:1 38:16 100:12 110:20 138:17,18 139:5 139:7,16 140:21 150:10 155:6 157:6,17 160:7 161:13 166:2 massive [1] 131:9 matches [1] 40:9 material [3] 83:7 127:19 131:5 materialize [1] 143:21 materially [2] 33:24 152:24 materials [2] 57:10 123:1 matrix [19] 106:3 125:14 146:10 147:3,5 148:3 149:18 151:4 152:3,11 163:25 164:19,20,24 165:2,9,15,16,24 matter [7] 19:6 33:13 50:4 75:12 98:20 144:25 167:3 matters [5] 6:1 9:14 21:20 89:8 145:5 Maureen [2] 84:21 126:24 maximize [1] 81:7 maximizing [1] 81:2 may [15] 3:18 5:20,22 6:2 6:17 17:6 29:10 36:24 57:16 80:11 88:21 97:7 122:6 140:20 165:18 McShane [6] 12:13 34:5 47:25 48:7 49:2 153:4 MDNA [1] 103:19 mean [35] 48:11 62:4 66:5 75:17 76:20 78:6 82:8 84:2 87:13 89:12 92:11 98:24 101:13 105:12 106:25 107:3 108:25 113:5 118:23 121:15,19,22,25 122:8,8 122:10 131:2 135:24 136:3 137:3,5,6 142:14 142:24 143:1 meaningful [2] 147:25 165:22 meaningless [1] 125:12 means [10] 59:16 76:1 76:21 83:8 87:20 92:12 135:1 137:3,13 167:8 measure [8] 13:1 16:2 68:12 95:15 96:20 98:1 99:16 102:11 measures [1] 68:15 mechanical [1] 118:25 mechanism [1] 24:25 mechanisms [5] 7:2 14:9 31:20,20,21 media [13] 50:19,23 51:16,17,24 52:10,15,19 55:1,7,15 56:11 166:17 median [1] 113:11 medical [1] 136:15 medium [1] 93:14</p>	<p>meet [3] 68:20 138:1 151:19 meeting [6] 27:2 64:17 75:25 118:16 120:7 121:23 meetings [1] 119:16 members [5] 65:7 69:21 71:16 72:19 140:18 memo [1] 122:4 memory [1] 73:8 memos [2] 119:11,22 mention [8] 9:23 53:9 53:11,14,15 54:11 119:13 134:16 mentioned [4] 93:2 102:24 152:8 158:5 merit [2] 66:24 119:13 met [9] 46:14 65:5 67:3 67:12 68:13 69:19 76:13 77:1 96:25 methodology [12] 10:12 10:13,15,17,20,22,25 40:7,12 65:15,22,24 mid [1] 115:10 middle [2] 131:8 165:1 might [10] 30:3 35:4 60:2 61:20 94:21 113:25 138:10 141:20 150:12 156:16 military [1] 60:2 million [23] 11:5 13:5,7 13:9 32:5 40:14 42:12 43:8,9 44:17 46:1,2 52:4 59:6 75:17,22 126:6 149:4,15 150:19,20 163:2 163:12 millions [1] 44:16 mind [4] 25:12 44:4 83:6 155:2 mindful [1] 155:7 mine [2] 71:11 90:24 minimum [3] 75:16 76:12,13 mining [1] 112:21 minute [3] 58:9 73:7 98:8 minutes [2] 18:16 78:22 missing [1] 54:15 mix [2] 129:17 141:21 mobility [1] 111:14 moderate [1] 13:25 modest [1] 7:25 modified [4] 17:7 155:21 156:5,11 moment [6] 3:15 43:2 63:13 66:2 68:6 72:25 money [6] 32:22 52:3 81:20,20 139:5,18 month [1] 50:22 months [3] 59:11,19 154:23 Moody's [13] 109:20 147:14,17,19,22 151:14 151:17,21,24 152:2,9</p>	<p>165:18,19 moratorium [1] 35:15 morning [9] 1:3 2:7,9 23:4 41:6,8 127:4 144:4 166:12 mortgage [1] 147:13 Moss [2] 167:2,11 most [11] 10:21 30:2,6 30:12,20 84:23 85:3 100:18 117:17 145:18 154:10 Mount [1] 134:15 move [7] 63:11 88:13 89:4 90:2,23 91:24 140:21 moved [1] 112:18 movement [2] 30:22 112:16 moving [9] 49:18 62:7 88:6 136:7 140:21 146:1 146:22 158:16 161:8 Ms [44] 2:4,6 6:7 9:9,10 12:6,12 34:5 39:4 48:7 50:25 51:5 53:23 73:5 74:6 76:18 77:17 79:6 79:10 88:21 97:7 100:12 102:5 104:2,5 105:18 106:17 130:2,5 132:4 136:25 143:2,17 144:14 144:16,18 145:5 153:4 156:25 159:17 162:6 164:4,14 166:14 multi-bound [2] 119:20 121:12 multi-year [1] 17:13 multiple [7] 50:7 58:18 102:22 113:12 115:4 131:1,1 multiples [1] 116:20 multiplied [1] 158:2 Muskrat [1] 120:8 must [10] 4:23,25 14:22 15:14 33:4,9,10 96:13 118:18 119:11</p> <hr/> <p style="text-align: center;">-N-</p> <p>name [3] 1:5,23 84:21 namesake [1] 134:16 national [1] 125:16 nature [5] 25:15 58:11 58:13 133:2 136:3 near [1] 111:13 nearly [3] 95:12 98:1 99:16 necessarily [3] 68:5 115:5,6 necessary [1] 37:13 necessity [2] 5:5 88:19 need [11] 35:5,11 48:10 51:1 90:16 104:6 117:11 117:20 119:23 121:5 133:12 needs [2] 80:2,5 negative [2] 37:2 41:22</p>
--	---	---	--	---

<p>negatively [1] 166:3 negotiated [1] 154:13 negotiating [1] 154:11 negotiation [1] 3:8 neither [3] 5:7 151:20 156:13 Nelson [1] 111:7 net [6] 13:4,10 42:11 43:7 46:2 163:3 never [3] 32:7 89:1 139:13 nevertheless [1] 81:10 new [18] 2:11 9:7 63:13 85:17 86:2 92:11,12,22 93:24 94:2,6,15,18,20 130:12,16 152:7,8 Newfoundland [214] 1:4,19,20 2:11,13 6:5,18 8:8,11,13 9:2,12,24 10:2 11:11 12:2,16,24 13:12 13:16,19,21 14:3,7,18 14:22 15:1,4,8 16:2,7,16 16:19,25 17:3,17,20 19:2 20:8 21:6,8 22:1,8,16 23:6,24 24:7,12 25:14 25:16,18 26:5,8 27:18 27:24 28:15,18,23,25 29:2,4,20,25 30:1,5,12 30:14,20,22 31:6,10,15 32:4,8,14,16,24 33:6,10 33:25 34:2,7,13,18,24 35:8,16,19 36:6,15,21 37:5,12,16,22,24 38:6 38:23 41:11,14 42:1 43:1 43:3,17 47:5 48:10 49:24 51:17 56:19 57:25 61:22 62:11,23 77:11 79:21,23 83:9,11 84:4 90:12 91:17 92:21 95:15,19 96:20 97:24 98:2,9 99:14,17 105:9,12,23 106:13,19 107:19 108:14,22 109:15 111:3,21 114:19 115:16 116:10 123:3,19 124:1,6 124:9,15 125:19 127:9 127:15,20,23 128:12,14 130:8,11 131:17 133:15 134:7 135:12,14 136:13 141:10 144:20 146:2,11 146:15,25 147:10,12,17 148:10 149:10,16,22 150:2,9,17 151:16,22 152:1,3 153:3,6,9,23 154:1,3,7,10,18 155:7 155:13 156:6 159:2 161:12,25 162:4,8,17,20 163:8,13 164:3,12,25 165:2,20 167:3,7,9 Newman [1] 1:6 newspapers [1] 93:6 next [25] 5:13 11:25 12:5 14:18 22:22 26:4 30:19 39:15 48:2 49:4 53:22 113:6 116:14 132:12 134:4 143:9 146:14 147:10 150:22 151:12 157:13 158:3 159:9 160:14 162:22 nice [1] 137:4</p>	<p>nine [2] 138:10,11 nobody [1] 73:13 non [1] 67:23 non-GRA [1] 17:10 non-regulated [5] 15:20 66:4,5,25 67:25 non-utility [1] 15:20 noon [1] 4:23 nor [3] 74:6 151:21 156:13 normal [9] 5:15 9:5 38:16,18 39:12 130:22 138:18,20 139:16 Normalization [1] 4:4 north [4] 28:8 42:11 57:2 152:21 notably [1] 154:10 note [2] 147:4 158:22 noted [4] 95:12,13 96:16 96:18 notes [1] 15:25 nothing [4] 17:4 19:5 83:16 144:13 notice [2] 4:18 104:2 notices [1] 5:25 Notwithstanding [1] 60:17 Nova [2] 61:14 129:12 November [4] 5:3 154:22 155:11 157:19 now [57] 6:13 7:6 11:14 15:7 17:15 28:13 34:4 43:2 44:3 47:10 56:18 59:8 64:15,24 66:2,4 67:7 68:5 71:1 72:5 78:9 87:15 89:3 91:1 92:23 92:25 93:12,21 98:14 99:12 100:8 101:5,12,25 104:4 107:17 112:12,17 112:19 117:5,20 130:11 130:18,25 133:15 134:14 134:23 138:2,14 145:5 146:1 149:25 153:7 155:13 156:21 162:22 164:23 nowhere [1] 111:13 nuclear [1] 129:16 number [25] 8:25 46:14 49:21,25 53:14 55:14 68:20 69:14 76:5,9 89:13 89:14,16,17 92:12 104:24 116:3,22 119:24 122:14 133:8,17,20 154:9 160:25 numbers [11] 43:12 48:22 71:2 92:14,17 93:10 97:18 121:18 134:3 138:7 166:15 <hr/> -O- <hr/> o'clock [1] 144:3 objection [5] 85:5,8,19 85:25 86:3 objectives [2] 8:19 118:17</p>	<p>obligation [3] 32:17 34:14,22 observe [1] 11:13 observed [1] 29:12 obtained [1] 66:18 obtaining [1] 91:11 obvious [1] 80:8 obviously [8] 7:21 53:9 63:19 64:2 80:17 89:7 123:19 131:11 occurred [2] 7:14 129:23 occurrence [1] 61:25 October [3] 2:22 54:3 55:5 odd [2] 89:2 121:22 off [9] 18:19 58:25 63:11 87:18 104:24 136:25 143:3,5,6 officer [7] 12:4,7 23:6 29:24 32:1 129:24 144:20 offset [1] 29:13 oil [4] 26:25 91:21 94:2,9 Okanagan [1] 112:24 older [4] 112:25 135:10 135:15 136:12 omission [1] 85:1 once [4] 15:1 16:13 72:16 97:2 one [57] 14:12 16:11 17:7 18:7 21:22 27:19 30:20 33:24 37:4 42:3 48:19 51:24 53:17,18 58:17 61:18,20,23 70:22 71:14 71:23 72:24 73:10 78:22 81:7 88:13,18 98:21 101:3 103:5,11 104:4 106:20 109:5 110:9 116:19 117:13 119:8 122:20 125:6,13 127:8 129:4,5,19,19 131:7 135:1,23 136:5 139:19 140:2 145:6 148:24 152:1 159:10,18 ones [2] 78:11 108:3 ongoing [2] 121:3 131:21 Ontario [5] 24:3 101:1 101:10,11 104:21 onto [6] 3:13 5:10 45:24 51:1 60:8 164:15 op [1] 131:9 opening [5] 6:2 12:20 24:23 46:17 50:11 operate [5] 29:7 70:18 110:21 122:8 156:16 operated [2] 69:13 155:9 operating [35] 9:12,21 12:19 13:24 20:6 25:11 32:4 47:21 49:18 53:1 58:20,24,25 59:7,18 60:24 68:22 69:8 80:4 99:5 111:11 112:8,12 115:2 117:21 122:25 123:2,4,7,15,21 124:1 125:1 126:17 130:7 operation [11] 7:10 28:14 71:13 154:2,8</p>	<p>155:12,14 156:11 157:7 159:13 161:24 operational [6] 10:7 26:7,9 27:4 29:10,21 operations [16] 12:17 20:9 25:15 26:5,10,14 26:16 33:21 37:5 100:11 104:16 117:16 119:19 121:5 153:22 163:25 opinion [2] 97:4 127:19 opinions [1] 34:5 opportunity [5] 34:25 37:17 46:20 147:1 148:10 oral [1] 4:22 Orange [1] 152:6 order [7] 9:8 14:19 17:11 28:23 34:8 95:24 147:16 ordered [3] 10:15,18 51:20 organization [4] 76:2 117:18 118:2 122:19 Osoyoos [1] 112:23 outlets [1] 51:17 outlined [1] 128:23 outlook [3] 146:16,25 154:18 overall [8] 2:14 8:13 9:20 32:11 80:6 91:8 123:25 162:6 overstatement [1] 13:16 overview [4] 26:4 52:16 145:14 146:15 overwhelming [3] 15:25 95:13 96:18 own [4] 78:5 110:13,22 132:24 owned [4] 28:8 106:21 152:20 154:6 ownership [1] 130:13 Oxford [1] 1:7 <hr/> -P- <hr/> P [1] 118:24 p.m [9] 92:4 101:6 113:16 123:10 132:8 143:7 148:4 159:20 166:24 P.U [1] 68:1 package [2] 128:12,25 page [6] 68:8 123:24 145:16 147:21 150:2 151:13 pages [1] 72:17 paid [9] 65:7 78:6 84:3 140:6,7,24 141:6,25 151:9 panel [4] 1:15 2:8 52:15 118:20 paper [5] 44:4 54:7 116:5 121:17 138:25 papers [1] 4:19 Paradise [1] 134:17 parameters [4] 12:11 107:12 113:3 159:7</p>	<p>Pardon [1] 49:9 part [9] 22:3 25:2,11 49:13 52:21 88:7 119:8 125:6 141:15 participate [1] 3:6 participated [1] 21:15 participation [1] 4:22 particular [11] 20:7 30:9 44:6 68:8 69:23 70:22 85:11,13 88:13 98:7 140:15 particularly [5] 62:9 73:2 80:2 92:15 165:5 parties [13] 3:4,5,12,16 3:17 4:3,4 5:4,8 6:2 19:12 166:12,16 parts [8] 39:5 48:25 49:1 49:6,6,13 52:20 111:24 party [2] 5:7 131:10 pass [2] 2:4 113:18 past [14] 8:20 29:13 30:16 41:21 46:13 48:2 52:4 60:6 63:1 71:3,15 85:21 88:10 163:4 patterns [1] 62:8 pay [8] 17:19 18:2 19:21 20:2 33:4,9 64:3,6 payer [1] 66:9 payers [4] 140:25 141:6 141:10,13 paying [2] 40:13 141:11 payment [1] 77:10 payments [2] 65:6 66:18 payout [2] 75:15 149:14 payouts [3] 66:4 67:1 69:24 pays [2] 66:8,19 PBR [4] 114:2,10,14 115:8 peacefully [3] 18:24 19:8,15 Pearl [1] 134:15 peers [1] 152:4 peg [1] 108:7 PEI [2] 61:14 101:12 penchant [1] 14:8 pension [5] 3:22 14:13 20:24,25 126:4 people [10] 49:24 84:23 85:3 111:15 115:11 118:9 134:13 135:2 137:5 142:1 people's [1] 19:8 per [6] 43:15 68:22 117:22 124:3,20 149:4 perceive [1] 165:21 perceived [2] 147:24 149:21 percent [148] 2:16,18,18 2:19 6:20,21,23 7:3,6,9 7:9,13,16,17,19,24 8:8 8:12 10:2,3 13:11 24:9 24:13,22 25:5,6,8,9,22 25:24 28:1,3,6,11,17 34:8 42:19 43:18 45:4</p>
---	---	---	--	---

46:24 47:3,11 64:5,9,10 64:12,13 65:4 66:18 67:3 67:9,11,23 68:14,18,21 68:23,24 70:1,6 71:11 75:15 77:6,10,12 82:3,5 82:11,18,21 83:13 84:2 87:6 94:8,14,15 95:2 102:18 104:23 106:2,13 108:18,19,21 112:11,11 113:20 124:3,20 135:20 140:13 141:12 145:23,24 146:4,6,10,21,24 148:14 148:25 149:1,2,12 150:3 150:4,4 151:16 152:13 152:18,22,25 153:2,25 154:4 155:3 157:11,14 157:18,25 158:1,2,4 158:13,18,18,19,20,24 159:23,25 160:2,4,5,9 160:12,16,24 161:6,10 161:14,16,18 162:14,18 165:8,15	picks [1] 66:7 piece [4] 83:19 85:13 126:15 149:25 pieces [3] 92:19 99:21 114:12 pile [1] 139:18 pitch [1] 49:25 placard [2] 18:9,15 place [7] 17:13 22:4 27:20 70:8 115:7 135:19 139:10 places [1] 61:15 placing [1] 37:24 plan [4] 60:18 72:18 74:22 126:4 plans [1] 116:15 plant [2] 112:20,24 plants [3] 110:3,22 112:25 play [1] 25:11 pleasure [1] 61:20 PLT [1] 90:23 plus [1] 94:19 pockets [1] 91:18 point [39] 11:12 37:4 39:4 45:22 47:20,24 49:16 53:3,4 54:15 55:19 56:15,16 66:21 69:5 71:15 75:12 76:24 85:14 85:20 86:5,8 92:6 96:1 98:23 102:5 107:8 111:5 111:18 113:10 115:13 124:22 127:11 132:4 137:15 138:12 158:22,25 163:8 pointed [3] 11:17 95:7 126:15 points [3] 50:7 53:17 158:23 pole [3] 33:22 111:12 131:2 poles [3] 14:4 58:15 109:15 police [1] 18:18 policy [9] 38:3 40:17 63:20 72:6 140:9,9,12 140:20,22 pontificating [2] 118:10 118:15 populated [1] 30:7 population [13] 30:15 30:18,22 93:16,19 113:1 132:12 133:7,10,12 134:7 134:22 135:21 populations [1] 30:21 Port [2] 117:8 121:7 portfolio [1] 26:21 portion [2] 109:13 140:17 pose [1] 31:10 posed [3] 103:9,10 104:2 position [8] 35:2 37:25 38:9 108:14 113:4 117:8 128:14 144:21	positions [2] 24:4 122:14 positive [1] 137:11 possible [1] 81:1 Possibly [1] 110:12 post [1] 14:16 pot [2] 81:24 98:12 potentially [1] 162:21 Pous [4] 21:12,23 22:4 164:7 power [146] 1:4,19,20 2:11,13 6:5,18 8:8 9:2 9:25 10:2 12:2,25 13:12 13:19,21 14:3,7,18 15:1 15:4,8 16:3,7,16,25 17:3 17:20 19:2 21:9 22:1,8 22:16 23:6,24 24:8,12 25:16,18 26:8 27:24 28:18,25 30:1,12 31:6 31:10,15 32:5,8,16 33:10 34:8,24 35:8,16,19 36:6 36:15,21 37:12,16,24 38:3,6,24 41:14 42:1 43:3,17 47:5 48:10 49:24 50:20 53:20 55:14 57:25 77:12 79:21,23 83:9,11 84:4 90:12 94:22 95:16 95:19 96:20 97:24 98:2 98:9 99:14,17 101:5 105:9,12,23 106:13,19 107:19 108:14,22 109:15 111:4 114:20 115:16 116:11 123:3,14,19 124:10,15 127:9,20,23 128:12,14 129:12 130:8 130:11 131:17 144:20 146:25 147:12 149:10 150:9 151:16 152:1,6 153:3,6,9,23 154:1,3,7 154:10,18 155:7,13 156:6 162:8 164:3,12 165:3,20 Power's [54] 8:11,13 9:12 11:11 12:16 13:16 14:22 16:19 17:17 20:9 21:7 26:5 27:18 28:16 28:23 29:2,4,20 31:6 32:14,24 33:6 34:13,18 37:5,22 41:11 43:1 111:21 124:1,6 127:15 146:2,12,15 147:11,18 148:10 149:17,23 150:3 150:17 151:22 152:3 159:2 161:12,25 162:4 162:17,20 163:9,13 164:25 167:4 practical [2] 11:21 149:8 practice [5] 17:22 85:22 88:9 89:2 131:20 pre-filed [3] 23:18 145:3 156:24 pre-hearing [2] 2:21,25 precisely [2] 82:19 87:9 precision [1] 86:9 predecessor [1] 66:16 predict [1] 136:4 predictability [1] 148:9 predictable [1] 13:23 predicting [1] 42:6 predominantly [1] 14:4	prefer [1] 116:6 preference [4] 150:11 150:13,15,19 preferred [1] 150:5 preliminary [1] 5:25 premise [1] 99:19 premised [1] 67:11 prepared [1] 77:4 preparing [1] 9:24 present [2] 49:4 88:2 presented [2] 75:19 76:17 preserved [1] 45:13 president [16] 12:3,7 23:5,24 48:9,12 66:15 67:1 69:25 70:4 100:10 104:13,14,15 137:22 144:19 President's [1] 100:9 presidents [2] 66:17 71:10 Press [2] 143:12,14 pressures [1] 25:13 Presumably [1] 86:16 presume [1] 142:2 presumption [1] 11:19 pretty [12] 69:12,16 92:24 93:13 96:9 117:4 131:13 132:21 135:4,25 137:4 140:1 previous [3] 63:7 69:25 70:2 previously [5] 21:5 55:7 73:11 83:17 153:18 price [4] 33:4,8 40:3 55:18 primarily [1] 93:7 primary [8] 17:23 19:24 32:17 78:11,12 79:22 80:12,20 prime [2] 132:20,22 Prince [2] 24:4 101:1 principal [3] 8:2 21:13 24:19 principle [1] 156:17 privilege [2] 30:5 100:6 pro [8] 97:17 115:3 118:3 129:11 156:15 157:5,7 159:5 problem [3] 87:8,16 89:25 procedure [2] 22:10,11 procedures [1] 2:24 proceed [3] 6:5 18:24 19:15 proceeding [11] 12:1 20:11 22:17 25:17 34:4 38:7 39:6,18 118:4 162:7 166:11 proceedings [3] 18:22 21:16 153:16 process [20] 3:7,8 11:7 38:21 85:10,12,16,20 87:17 88:7 89:7 114:10	118:6,11 119:12,18 120:12 122:11 153:21 155:21 processes [1] 38:24 produce [1] 156:18 produced [5] 119:9 122:23,24 153:20 155:20 production [1] 109:12 productivity [5] 10:5 17:10 124:2,7,19 professional [2] 21:15 71:17 professor [1] 20:14 profile [4] 8:14 29:2,4 99:8 profit [8] 17:20,24 18:4 19:24 20:4 43:3 54:13 80:9 program [8] 3:24 4:2 70:19 81:6,17 82:16,23 131:9 programs [2] 21:18 91:2 project [1] 154:19 projected [2] 45:12 116:13 projections [1] 132:18 projects [4] 15:21 93:3 93:8 132:11 prominent [2] 148:17 162:25 promote [1] 8:18 promoted [2] 46:12,23 promoting [1] 9:2 prompt [1] 149:14 propane [1] 94:9 properly [3] 5:24 74:16 85:6 property [1] 22:7 proposal [2] 54:12 150:6 proposals [13] 6:10 55:23 146:19 148:23 156:8 162:24 163:1,9,15 163:23 164:21 165:25 166:3 propose [1] 162:9 proposed [33] 2:17,19 4:11,13 7:3 22:1 27:20 38:7 39:1 43:5,9 88:22 150:1 156:11,14,22 157:11,24 158:3,21 159:10,12,16,24,24 160:15,18 162:3,7,13,15 162:19 165:2 proposes [6] 11:2 17:3 25:4 104:3 157:13 160:1 proposing [4] 8:15 24:8 43:6 155:14 proposition [2] 88:24 109:14 pros [1] 98:17 protected [1] 13:22 Protection [1] 118:25 PROTESTOR [1] 18:10
---	---	--	--	---

protestors [1] 19:6 proud [1] 135:12 proven [1] 40:18 provide [15] 17:9 26:14 27:6,11,15 32:18,19 33:5 82:7,12 90:5 119:10 122:22 146:14 153:14 provided [6] 35:7 36:10 85:23 97:19 104:5 156:14 provides [2] 37:16 151:7 providing [1] 30:25 province [11] 4:20 30:15 30:17 31:24,24 38:4 52:24 91:25 92:1 102:20 135:2 provinces [3] 29:25 30:4 128:24 provincial [1] 34:1 provision [1] 32:24 proxies [1] 15:25 proxy [2] 15:15 96:14 prudence [1] 11:15 prudent [1] 11:24 PU-43 [1] 95:8 PUB-NP-014 [1] 108:10 public [7] 2:24 4:21 37:15 52:16 152:7 166:18 167:6 published [2] 4:19 5:25 pull [1] 98:24 pulling [1] 134:14 purchase [1] 31:6 pure [1] 114:5 purpose [7] 8:17 38:11 51:14 96:2,25 150:16 153:12 purposes [6] 4:9 65:8 76:25 97:25 107:23 109:20 pursuant [1] 154:13 pursue [2] 17:10 127:5 push [2] 59:18,19 pushed [1] 59:20 pushing [1] 134:18 put [38] 5:22 13:3,11 43:23 47:4 48:7,8,16,22 49:16 53:11 55:25 56:3 56:5 59:25 74:11 77:12 81:23 83:21 86:11 87:5 87:21 90:2 97:20 98:11 99:9 100:15 103:13 104:4 105:3,8 108:1,7 114:20 131:4 136:11 148:23 156:8 putting [3] 55:12 74:16 166:17 <hr/> -Q- <hr/> Q.C [56] 1:17 6:6 22:21 23:2,3,9,16,22 24:6,15 26:3 27:17 28:22 29:19 31:11 32:12 33:12 34:9 35:9 36:12 37:11 38:5 39:14 40:20,24 82:14	83:15 84:11,20 85:2 86:1 86:4,7 87:4,14 88:4,14 89:5,18,24 90:8 103:24 126:24 132:5 142:10,17 143:11,16,23 144:17 148:5 157:3 159:21 164:17 166:7,22 quality [2] 36:1 113:21 quarter [1] 138:11 questionable [1] 46:14 questions [15] 6:17 12:18,21 83:17 84:13 85:23 88:10 104:1 126:20 127:3,6,12 128:3 132:6 132:10 quibbling [2] 56:5,7 quick [1] 142:18 quite [6] 63:4 114:9 137:19 152:2,9 159:14 quote [2] 15:11 93:11 quoted [1] 139:25 <hr/> -R- <hr/> rain [1] 58:16 raise [1] 63:18 raised [2] 10:10 39:17 raising [1] 71:8 range [6] 47:10 59:6 108:17 141:16 145:25 165:18 ranging [1] 2:17 rapidly [1] 30:21 rate [66] 1:4 2:10 4:7,9 4:12,12,14 9:14 11:2,3 12:25 13:19 15:8 17:8 21:16 22:3,17 23:10 24:8 25:1,4,12,21 27:19,24 28:23 37:8 39:22,23,24 40:10 41:12,16 43:16 48:16 50:22 51:19 52:7 52:18 55:18,20 66:8,9 68:19 77:4 92:7 96:3,25 127:17,21 140:24 141:6 141:10,13 145:15,22 146:2,3 147:16 154:15 157:13 160:1 163:13,14 163:17 167:4 rated [3] 147:14 158:8 161:2 rates [23] 2:11,15 6:20 7:7,11,17 11:4,8,8 13:6 13:8 14:22 21:25 24:14 25:5,8 40:3,14 64:13 77:15 141:25 146:22 164:21 rather [3] 9:1 59:13,22 rating [14] 147:23 148:6 148:8,15 149:6,21 150:14 150:17,18,23,25 151:6 151:19 166:1 ratings [5] 106:8 147:15 149:23 152:11 166:4 ratio [11] 8:12 101:25 102:18 133:13 136:22 141:7 148:14,17 150:3 151:17 165:15	reach [1] 93:22 reached [1] 6:8 react [1] 61:10 read [6] 52:18 95:24 114:6 116:6 133:11,17 reading [1] 93:5 readjust [2] 59:11 76:3 ready [4] 22:24 117:2 119:25 120:8 realistic [1] 21:2 reality [3] 99:1,5 112:7 really [8] 7:2 17:1 25:17 48:10 50:4 55:5 103:18 113:3 reason [6] 40:17 100:5 121:4 125:25 126:8 151:10 reasonable [27] 11:24 15:15,15,24 27:1 28:4 31:15 34:19 35:1 37:7 37:18,19 38:22 39:3 45:22 46:21 52:5 53:16 54:25 59:12 67:9 96:13 96:14 99:14,18 147:2 161:21 reasonableness [3] 9:21 11:15 88:19 reasonably [2] 26:13 77:7 reasons [1] 154:9 rebalancing [2] 6:23 24:20 rebuilding [1] 115:9 rebuttal [1] 144:24 receive [3] 10:4 33:8 69:4 received [5] 2:10 35:22 36:25 37:3 166:15 receives [1] 69:4 recent [2] 10:21 115:25 recently [1] 130:7 recognize [1] 147:17 recognized [1] 8:11 recommence [1] 18:22 recommendation [5] 70:20,23 71:6 72:4,10 recommendations [7] 100:13 164:7,8,11 165:5 165:8,11 recommended [2] 152:14,18 recommending [1] 46:24 reconcile [1] 108:13 record [18] 3:14 5:10 18:19 19:1 24:17 48:6 51:2 65:10 85:13 92:14 105:8 143:3,5,6 157:1 159:18 164:16 166:16 recover [1] 148:10 recovered [1] 24:24 recoveries [1] 9:13 recovery [7] 4:5 7:14 25:25 31:19,22 32:3	149:3 recruitment [3] 27:10 36:16,22 recurrent [1] 139:24 Red [1] 90:25 reduce [7] 8:18,19 38:11 38:13 39:22 153:16 162:21 reduced [8] 7:9 28:6 36:6 101:23 127:3 150:4 151:10 164:1 reduces [2] 26:24,25 reducing [8] 10:25 17:8 35:3 38:1 40:2 71:7 155:4 163:10 reduction [15] 11:7 28:10 40:1 147:25 148:24 149:1,11,22 157:25 158:20 161:25 163:17 165:6,7,22 reductions [6] 35:3,21 35:23 36:9 37:1 117:22 reevaluation [1] 149:20 refer [3] 101:15,21 103:19 reference [5] 56:18 57:17 113:19 116:10 117:25 referenced [2] 134:11 160:23 referred [2] 9:10 101:12 referring [6] 42:9 58:3 101:20 107:22 114:22 124:4 reflect [4] 14:23 25:5 77:16 124:1 reflecting [1] 162:3 reflection [2] 76:6 91:13 reflective [2] 43:16 102:20 reflects [1] 37:19 refresh [1] 108:24 regard [2] 93:2 95:20 regarding [1] 134:6 regards [1] 21:11 Regatta [2] 144:7,10 regime [3] 17:13 114:5 115:8 regimes [1] 137:17 regions [1] 30:7 registered [2] 2:23 135:19 regular [10] 46:3 61:25 62:5 91:9 117:4,25 120:6 120:7 121:2,10 regulated [9] 13:13 33:15 42:18 43:18,23,24 67:24 108:13,17 Regulation [1] 114:15 regulator [1] 21:23 regulators [3] 39:9 151:3,4 regulatory [40] 8:18,18 8:25 9:1,6 13:24 15:23	21:22 29:15 31:12,15,20 31:21 38:12,19,21 39:13 47:22 98:10,14 99:9 102:19 106:2,14 115:19 128:8 129:13 137:2,7,17 137:22 148:1,7,12,18 149:20 153:15,21 155:21 165:23 rejiggle [1] 76:3 relate [1] 127:8 relates [1] 25:2 relation [10] 8:6,14 19:20 21:9,18 22:6 55:7 74:22 96:4 99:15 relationship [1] 162:10 relative [7] 29:21 32:9 45:25 107:11 123:20 124:14,20 relatively [3] 7:25 25:19 33:20 release [9] 50:19,24 51:16,25 52:8,15,19 55:2 55:15 relevant [2] 89:8 151:5 reliability [8] 33:7 35:24 36:1,4 68:11 81:4 129:14 136:14 reliable [10] 26:14 27:7 27:12,16 30:8 32:18,25 34:16 39:2 143:15 relied [2] 15:14 96:13 rely [8] 3:18 16:17 30:10 49:19 93:13 94:3 100:2 100:12 relying [2] 94:16,24 remain [6] 98:13 156:21 157:6,17 160:7 161:13 remainder [1] 4:15 remaining [1] 4:21 remains [3] 14:6 26:17 108:4 remember [1] 7:7 removes [3] 14:13,15 122:13 reoccurs [1] 19:11 repeat [3] 13:18 66:22 127:11 replaced [1] 150:5 replacing [1] 17:3 reply [2] 80:8 123:6 report [15] 5:3,5,8 9:16 116:10 119:7,14 120:3 121:12,13 122:7,15,19 147:20,22 reports [4] 119:9,11 122:22 153:4 representative [1] 5:6 representing [2] 1:19 22:15 represents [3] 7:24 25:10 106:13 reproductive [2] 133:13 136:22 repurchase [2] 154:12 154:14
--	---	--	---	--

request [7] 13:2 82:19 85:4,4,5 86:13 120:5	return [114] 7:5,8,12,15 7:23 8:4 9:5 11:3 13:3 13:10,13,17 14:21 15:2 15:6 16:19 21:8 25:3,4,4 25:6,18 27:19,25 28:3,6 28:8,10,16,20 33:9,16 34:7,11,20,21,24 35:1,6 35:11 37:8,18 39:12,23 42:18 43:18,23,24 44:15 44:16 45:13,20 46:3,20 46:22 47:3,6 52:6,25 53:10,16 54:12,25 56:15 58:1 60:13 82:3,11 83:13 108:21 113:20 126:10 145:22,25 146:3,4,6,23 147:2 148:12 149:1 150:22 151:7,10 152:13 152:18,19,22,25 153:2,6 153:13,25 154:4,5 156:6 157:8,10,12,14 158:3,15 158:17,24 159:3,23,25 160:2,14,15 161:9,12 163:14 165:7	127:16,20,24 128:6,7,8 128:8,11,13,18,25 129:2 129:6,8 137:1 149:17 157:12 159:25	riskier [3] 15:21 114:8 130:1	scrapping [1] 17:2	settlement [2] 3:6,10
requested [4] 3:5 85:7 85:17 124:11	risks [1] 29:21	risky [4] 16:3 95:16 96:21 98:2	road [3] 15:7 17:1 167:6	screen [1] 147:21	seven [2] 71:16 112:19
requesting [4] 2:13 6:19 24:13 28:19	role [1] 104:12	roughly [4] 94:12,19 109:25 110:2	Rockland [1] 152:6	Seaboard [1] 61:13	seven-year [1] 3:24
requests [4] 3:1 4:22 82:15 160:25	room [2] 46:19 84:24	run [7] 101:21 112:4,16 121:10 122:10 125:12 138:15	ROE [9] 84:2 89:13 138:12 151:15,22,25 156:18,20 164:7	Seal [1] 90:25	several [2] 8:20 22:6
require [3] 64:16 88:10 117:7	Rotman [1] 20:15	running [8] 11:18 38:25 59:9 60:5 71:1 81:25 112:11 118:7	Rogers [1] 94:23	second [9] 7:5 18:7 21:11 25:2 70:11,13,15 149:18 150:13	severe [1] 30:6
required [10] 3:4 5:20 11:3 32:22 68:12 88:18 88:20 158:15 160:13 161:7	returns [13] 21:2 37:9 41:11 108:12,16 147:4 150:24 151:2,3,5 153:20 154:6 155:20	runs [1] 126:3	role [1] 104:12	Section [2] 23:12 144:23	shale [1] 129:16
requirement [8] 67:18 77:1,5,10,24 78:4 163:12 165:25	revenue [13] 4:6 67:18 77:1,4,9,24 78:3 86:17 86:18 87:5,7 112:13 163:11	rural [8] 30:22,24 52:1 92:18 117:11 135:12,14 136:12	roughly [4] 94:12,19 109:25 110:2	sectors [1] 31:2	shall [3] 18:22,25 19:12
requires [3] 30:23 34:19 83:12	Reversing [1] 11:6	safe [4] 27:6 32:18,24 34:16	room [2] 46:19 84:24	see [27] 1:13 24:19 29:1 40:17 58:13 68:11,14 69:23,24 70:4 85:13 91:22 93:5,6,10 94:12 99:11,25 115:11 132:22 134:6 136:16 137:22 144:3 145:22 146:5,12	shape [2] 26:16 59:10
research [1] 20:18	review [4] 3:15 9:11 35:25 154:25	safety [4] 68:18 81:5 125:15 151:8	Rotman [1] 20:15	seeing [7] 64:1 92:20,22 93:1,2,6 134:9	share [2] 26:1 120:16
Reserve [1] 4:4	reviewed [1] 116:14	SAIDI [2] 68:13 125:15	roughly [4] 94:12,19 109:25 110:2	seek [3] 36:4 154:1,8	shareholder [7] 17:24 18:1 19:25 20:1 66:7 80:9,14
reserved [1] 4:1	revisit [2] 39:10 63:12	SAIFI [1] 125:15	ruled [1] 28:3	seeking [1] 12:25	shareholders [8] 17:21 78:9,11 79:23 80:10,18 80:21 142:1
residences [1] 134:14	reward [1] 17:17	salaries [2] 63:25 65:17	rulings [1] 138:3	seeks [1] 13:10	shares [5] 150:5,11,13 150:15,19
residential [3] 2:20 25:20 52:23	RFI [6] 83:21 85:10,12 86:6,8 115:25	salary [4] 18:2 20:2 63:20 64:5	run [7] 101:21 112:4,16 121:10 122:10 125:12 138:15	self [1] 29:17	sheer [1] 59:17
resolutely [1] 19:13	RFI's [1] 82:23	sale [1] 130:9	running [8] 11:18 38:25 59:9 60:5 71:1 81:25 112:11 118:7	send [1] 63:9	shift [1] 93:20
resolution [1] 68:17	RFIs [1] 125:13	sales [2] 59:9 92:17	runs [1] 126:3	sends [1] 1:14	ship [1] 71:1
resource [3] 59:17 116:15 118:22	right [44] 4:1 18:24 19:2 19:3,4,8,14 27:14 33:24 40:16 42:13 43:10 44:13 44:17 54:13 57:7 62:15 63:21 64:18 66:9,19 68:1 69:2 71:1 75:7 81:1,13 87:3 92:23,24 93:21 95:4 104:11 109:22 110:17 114:24 124:11,16 132:15 134:1,22 136:16 144:5 147:22	sample [1] 100:2	rural [8] 30:22,24 52:1 92:18 117:11 135:12,14 136:12	senior [3] 24:3 100:9 104:14	short [10] 17:18 19:21 36:24 40:1 72:18 74:22 93:14 112:16 163:10,24
resources [2] 117:15 153:22	right-hand [1] 65:19	satisfaction [2] 26:17 68:15	safe [4] 27:6 32:18,24 34:16	sense [7] 80:12 82:6 94:4 94:6 113:17 120:21 142:21	shortfall [1] 4:7
respect [15] 6:9 9:9,20 12:15,18 85:4,18 107:13 127:12 128:4 130:13 131:16,21 140:3 151:1	rigorous [1] 82:23	satisfied [1] 68:16	safety [4] 68:18 81:5 125:15 151:8	sensitive [1] 137:10	show [4] 45:4 52:20 57:18 65:12
respectful [1] 13:15	rising [1] 162:2	Saturday [2] 59:4 60:6	SAIDI [2] 68:13 125:15	sent [8] 50:17,19,20,21 54:4,8 55:6,21	showed [5] 15:17 60:2,4 96:16 121:18
responding [1] 131:2	risk [91] 8:14 13:23 14:5 14:8,9,13,15,19,20,23 14:24 29:1,2,4,18 32:11 47:23 97:4 98:10,10,11 98:14,14 99:8,8,10,16 99:23,24,25 101:13,15 101:19,21 102:2,7,9,12 102:15,17,24,25 103:5 105:13,24 106:10 107:1 107:7,14 108:2,3,6,15 108:23 109:2 110:9 111:6 111:7,20,25 112:3,3 114:4,6,25 115:2,22 126:12,12,14 127:9,9,13	save [1] 26:22	SAIFI [1] 125:15	sentence [2] 52:9,13	showing [1] 165:4
response [3] 26:23 58:21 128:3	risk [91] 8:14 13:23 14:5 14:8,9,13,15,19,20,23 14:24 29:1,2,4,18 32:11 47:23 97:4 98:10,10,11 98:14,14 99:8,8,10,16 99:23,24,25 101:13,15 101:19,21 102:2,7,9,12 102:15,17,24,25 103:5 105:13,24 106:10 107:1 107:7,14 108:2,3,6,15 108:23 109:2 110:9 111:6 111:7,20,25 112:3,3 114:4,6,25 115:2,22 126:12,12,14 127:9,9,13	say [2] 73:11 124:3	salaries [2] 63:25 65:17	separate [1] 80:19	shown [5] 15:14 96:13 146:17 164:22,24
responses [1] 3:2	right-hand [1] 65:19	says [3] 75:16 123:13 124:18	salary [4] 18:2 20:2 63:20 64:5	sent [8] 50:17,19,20,21 54:4,8 55:6,21	shows [7] 44:11 63:19 136:8 157:7 164:18,20 165:1
responsive [2] 97:14 137:25	rigorous [1] 82:23	scariest [1] 136:5	sale [1] 130:9	sense [7] 80:12 82:6 94:4 94:6 113:17 120:21 142:21	sic [1] 104:3
responsiveness [2] 26:10 27:5	rising [1] 162:2	scenario [1] 90:24	sales [2] 59:9 92:17	sensitive [1] 137:10	side [2] 106:3 110:6
rest [1] 31:17	risk [91] 8:14 13:23 14:5 14:8,9,13,15,19,20,23 14:24 29:1,2,4,18 32:11 47:23 97:4 98:10,10,11 98:14,14 99:8,8,10,16 99:23,24,25 101:13,15 101:19,21 102:2,7,9,12 102:15,17,24,25 103:5 105:13,24 106:10 107:1 107:7,14 108:2,3,6,15 108:23 109:2 110:9 111:6 111:7,20,25 112:3,3 114:4,6,25 115:2,22 126:12,12,14 127:9,9,13	Saturday [2] 59:4 60:6	sample [1] 100:2	series [2] 21:18 84:12	signal [2] 161:18,25
rests [1] 151:2	right-hand [1] 65:19	save [1] 26:22	satisfaction [2] 26:17 68:15	serious [2] 149:4 164:12	significant [8] 13:1 14:2 15:17,19 25:13 40:11 149:12 154:16
result [13] 11:7 31:7 35:6 38:23 70:17 72:4 152:11 153:17 155:3 156:5 159:2 159:7 163:15	rigorous [1] 82:23	saw [2] 73:11 124:3	sale [1] 130:9	seriously [2] 138:2 150:10	significantly [2] 152:19 154:5
resulted [1] 35:16	rising [1] 162:2	says [3] 75:16 123:13 124:18	sales [2] 59:9 92:17	serve [1] 10:2	similar [4] 15:6 29:16 55:1 65:24
resulting [2] 3:10 32:6	risk [91] 8:14 13:23 14:5 14:8,9,13,15,19,20,23 14:24 29:1,2,4,18 32:11 47:23 97:4 98:10,10,11 98:14,14 99:8,8,10,16 99:23,24,25 101:13,15 101:19,21 102:2,7,9,12 102:15,17,24,25 103:5 105:13,24 106:10 107:1 107:7,14 108:2,3,6,15 108:23 109:2 110:9 111:6 111:7,20,25 112:3,3 114:4,6,25 115:2,22 126:12,12,14 127:9,9,13	scariest [1] 136:5	sample [1] 100:2	served [2] 24:1 29:23	similarities [1] 159:11
results [11] 16:17 39:3 42:1 73:2,3 75:15 120:15 121:24 145:17,21 147:7	right-hand [1] 65:19	scenario [1] 90:24	satisfaction [2] 26:17 68:15	serves [1] 20:23	similarly [2] 41:25 97:7
retailers [2] 141:19,19	rigorous [1] 82:23	schedule [5] 1:10 2:24 5:16,22 43:13	sale [1] 130:9	service [44] 22:6 25:23 26:2,15,19 27:7,12,16 29:9 30:8,24 32:17,18 32:19,25 33:5,8,9,18 34:16 35:5,7,12,22,25 36:1,8,10,19,25 37:3,6 38:1 81:4 109:11 110:25 113:21,24 114:5 134:19 134:21 135:2 136:13 152:7	simple [3] 37:4 56:12 88:20
retain [2] 3:4 120:10	rising [1] 162:2	scheduled [1] 5:13	sales [2] 59:9 92:17	sets [1] 66:4	simply [9] 6:23 10:12 39:21 85:19 153:2 156:3 157:7 162:8 165:9
retained [1] 21:24	risk [91] 8:14 13:23 14:5 14:8,9,13,15,19,20,23 14:24 29:1,2,4,18 32:11 47:23 97:4 98:10,10,11 98:14,14 99:8,8,10,16 99:23,24,25 101:13,15 101:19,21 102:2,7,9,12 102:15,17,24,25 103:5 105:13,24 106:10 107:1 107:7,14 108:2,3,6,15 108:23 109:2 110:9 111:6 111:7,20,25 112:3,3 114:4,6,25 115:2,22 126:12,12,14 127:9,9,13	School [1] 20:15	sample [1] 100:2	setting [2] 14:22 131:3	single [1] 112:17
retire [1] 139:21	right-hand [1] 65:19	Scotia [3] 61:14 129:12 160:22	satisfaction [2] 26:17 68:15	settled [3] 4:11 6:11,14	sister [1] 125:5
retirement [1] 31:8	rigorous [1] 82:23		satisfied [1] 68:16		sit [6] 5:19 81:19 91:16 107:9 119:21 142:20
retirements [1] 116:13	rising [1] 162:2		Saturday [2] 59:4 60:6		sits [1] 129:14
retractable [4] 150:5,11 150:13,19	risk [91] 8:14 13:23 14:5 14:8,9,13,15,19,20,23 14:24 29:1,2,4,18 32:11 47:23 97:4 98:10,10,11 98:14,14 99:8,8,10,16 99:23,24,25 101:13,15 101:19,21 102:2,7,9,12 102:15,17,24,25 103:5 105:13,24 106:10 107:1 107:7,14 108:2,3,6,15 108:23 109:2 110:9 111:6 111:7,20,25 112:3,3 114:4,6,25 115:2,22 126:12,12,14 127:9,9,13		save [1] 26:22		sitting [5] 5:16,21 97:22 98:20 118:9
retraction [1] 92:17	right-hand [1] 65:19		saw [2] 73:11 124:3		six [3] 2:16 12:2 71:15

<p>91:12 skills [1] 117:6 slam [1] 75:21 slight [2] 70:7 71:10 slightly [2] 45:11 91:3 small [11] 14:3 25:19 29:6 38:23 102:21 107:12 109:18 110:3,5 121:13 150:9 smaller [2] 91:25 135:10 smallest [1] 25:22 Smith [6] 12:16 20:10 59:1 76:19 113:25 132:2 snow [2] 61:6,7 sole [1] 112:17 solely [1] 107:8 solicitors [1] 84:18 solid [1] 81:25 somewhat [2] 25:21 152:4 somewhere [1] 105:1 soon [1] 155:1 sorry [8] 18:7,14 51:4 91:7 105:4 116:5 129:21 133:10 sort [4] 43:25 83:6 109:8 121:24 sought [2] 27:25 28:2 sound [3] 81:24 166:1 167:8 sounding [1] 129:7 sounds [1] 107:2 source [2] 112:17 132:20 sources [1] 132:17 sourcing [1] 113:12 Southern [1] 16:15 speak [5] 6:14 18:13 100:8 113:7 151:19 speaking [2] 156:3 162:8 special [1] 119:6 specific [6] 68:12 86:12 87:20,21 119:13 129:18 specifically [2] 6:14 125:18 specifics [2] 97:4 117:1 specify [1] 158:9 split [4] 70:15 71:9 101:22 131:3 spoke [2] 122:25 123:2 sponsored [1] 123:2 spots [1] 121:8 spread [14] 138:12 156:1 158:5,6,10,13,13,14 160:17,20,23 161:5,7,22 spreads [1] 155:24 spurred [1] 116:18 St [6] 91:5 92:15 117:12 134:15 167:6,9 Stabilization [1] 4:14 stable [2] 13:22 133:12 staff [3] 21:21 108:11 118:24</p>	<p>stage [1] 131:7 stake [6] 74:3,5 75:5 83:3 83:4 106:1 standards [1] 113:22 standing [1] 25:24 standpoint [1] 118:22 start [10] 4:18 5:11 63:13 87:17 142:22 145:10,12 145:13 157:10 159:23 started [5] 1:15 2:5 4:20 60:6 127:4 starting [3] 158:10 159:22 160:20 starts [1] 157:16 state [3] 19:1 21:22 152:5 statement [4] 46:18 79:25 123:25 124:17 statements [1] 6:3 States [4] 15:3 21:17 22:12 63:1 stating [1] 127:23 statistics [1] 125:16 status [1] 90:25 stay [2] 99:2,4 stayed [1] 40:12 steady [1] 14:1 step [2] 31:16 116:19 Stephenville [1] 121:6 steps [3] 37:13 96:2,24 STI [10] 66:4,18 70:19 74:4 77:10 81:6,15,16 82:16 140:17 still [9] 29:17 38:17 53:6 53:6 94:9,10 127:7 134:13 159:3 stop [1] 18:6 storm [17] 5:21 32:1 56:21,23,25 57:7,8,12 57:16,22 58:3,6,10,10 58:13,16 60:1 storms [8] 56:22 58:4,6 58:18 60:23 61:12,16 98:18 story [1] 60:21 stove [1] 94:2 strains [1] 111:13 strategies [1] 116:16 strategy [2] 122:13,13 stream [4] 86:18,19 87:5 87:7 streams [1] 112:13 strength [1] 148:16 strengths [1] 32:9 stresses [1] 111:13 strike [1] 132:1 strikers [1] 19:7 strikes [3] 51:24 121:22 121:25 striking [1] 48:18 strong [7] 29:14 91:15 91:18 92:2 102:19 106:2 106:14</p>	<p>stronger [1] 32:9 struck [1] 80:2 structural [1] 20:17 structure [31] 4:12 8:4 8:6,8,9 29:14 32:10 101:16,16,17,18 102:8 103:1,4,6,15 105:10 106:5,8,24 107:5,9 136:21 137:21 145:8 148:25 149:7,9 151:23 164:8 165:6 structured [1] 137:20 structures [5] 103:22 130:10,14 131:18 154:12 struggled [1] 129:4 struggling [1] 129:5 studies [1] 10:19 study [3] 22:2 141:9,15 stuff [1] 76:15 subject [7] 4:9 12:5 32:7 65:1,25 108:24 114:4 subjected [2] 19:9 75:25 subjective [2] 75:16,17 submission [2] 4:23 13:15 submitted [5] 3:2,19 4:23,25 5:3 subsequent [1] 58:23 subsequently [1] 72:12 substantial [1] 33:3 substantially [2] 29:5 93:17 substantive [2] 62:8 101:24 succeeds [1] 10:6 such [8] 16:14 21:1 37:1 59:15 102:18 115:15 149:19 163:5 sudden [1] 101:25 sufficient [1] 43:17 suggest [8] 59:6 88:21 99:23 102:15 117:3 130:18,19 131:13 suggestions [1] 17:6 sum [1] 122:18 summarized [1] 85:6 summer [1] 134:14 supplied [1] 94:22 suppliers [1] 115:4 supply [11] 6:24 7:1 24:21,24 31:19 36:1 52:2 52:25 94:25 112:17 129:17 support [16] 15:23 31:12 31:16 102:19 106:3,14 130:10,14 131:18 148:1 148:7,13,18 149:20 154:12 165:23 supportive [6] 13:24 29:15 115:21 137:2,8,12 supposed [2] 52:9,12 surely [2] 120:13,20 surface [2] 105:15,20</p>	<p>surprise [1] 49:23 surprised [1] 151:24 survey [1] 140:5 suspend [4] 28:14 154:1 154:8 155:12 suspension [2] 28:2 152:23 sustainable [1] 37:6 sustained [3] 148:2 152:10 165:23 sustains [1] 8:13 swear [1] 144:12 sworn [3] 22:24 23:1 144:16 system [7] 26:12,15 29:7 110:21 134:17,18 136:15 systems [1] 130:24</p> <hr/> <p style="text-align: center;">-T-</p> <hr/> <p>T [1] 109:22 table [11] 44:7,19,25 46:6 46:9,11 66:3 68:9,9 69:23 70:4 tact [1] 55:11 takes [1] 46:18 taking [3] 65:17,18 153:21 talks [3] 51:25 52:2,2 tandem [1] 81:2 tangle [1] 134:8 target [22] 64:10,15 65:6 65:18 66:7 67:3 69:24 69:25 70:1,2,3 73:12,15 73:24 74:23 75:6 77:1,6 77:6,7,22 140:13 targets [19] 18:4 20:4 63:19,20 64:18,18 65:5 67:10 68:6,10,25 69:13 69:19,20,22 72:9,19 73:10 74:23 tax [1] 163:3 teaching [1] 20:21 team [6] 17:18 72:20 80:24 96:23 97:12 121:4 technical [1] 36:17 technically [1] 158:20 technology [1] 117:10 Teck [1] 112:21 telling [2] 83:12 100:3 tells [1] 83:16 temper [1] 132:21 ten [3] 61:18 63:6 118:23 tend [1] 36:20 tendency [4] 58:14,19 61:5 119:21 term [19] 17:19 19:21 34:17 35:12,24 36:20,24 37:6 39:25 40:1,18 72:18 74:22 92:10 93:14 94:8 112:16 163:24 164:2 terms [28] 11:10 42:1,6 47:6 56:6 67:18 73:1 75:4 79:20 82:6,10 83:10</p>	<p>88:17 90:11,15 91:11 92:5 93:22 94:15 97:13 101:18 114:2 121:17 127:23 128:10 141:12 154:11,14 territories [1] 110:25 territory [1] 29:9 test [6] 8:2 9:24 11:14,16 11:24 153:14 testified [5] 21:4,5,19 21:21 83:2 testify [3] 12:4,15 21:7 testifying [1] 83:5 testimony [12] 6:15 12:12 23:13,18 40:21 48:1 49:2 97:21 144:24 144:25 145:3 166:5 Texas [1] 21:14 Thank [24] 1:18 2:2,7 6:7 12:22 22:18,22 23:4 24:17 40:25 51:9 79:20 90:9 116:8 132:6 144:18 157:1,4 159:9,19,22 164:18 166:8,23 theme [1] 63:13 theory [1] 20:21 therefore [4] 20:1 88:23 151:5 161:24 they've [4] 106:7 114:9 115:4 135:19 thinking [5] 108:24 117:13,24 119:3 120:1 third [4] 25:9 44:25 131:10 146:1 THOMAS [1] 41:4 Thornton [4] 5:3,6 9:11 9:15 Thornton's [1] 9:19 thought [6] 55:17 80:7 129:3 137:11 138:20,23 thousand [1] 110:1 three [17] 6:21 24:19 41:21 52:20 53:18 59:19 68:8 71:2,14 111:24 121:6 126:13 127:7 136:1 145:8 149:2 151:20 through [38] 6:13,25 7:1 7:9 17:18 31:20 38:21 39:5 41:16 46:1 57:2 59:2,2 60:9 61:21 70:19 72:11 73:14 74:3 82:22 108:5 110:20 111:1,8,14 112:24 116:23 117:15,16 121:2,13 130:23 136:7 141:25 143:17 145:5 147:3 159:10 throughout [5] 4:16,19 8:22 119:4 120:12 tied [4] 17:19 73:2,3 102:25 tight [1] 71:1 timely [1] 148:11 times [6] 102:22 146:7,9 151:20 165:12,14 timing [1] 142:19 today [20] 1:11 5:11 11:5</p>
--	--	---	---	--

16:22 27:7 30:3 36:13 38:18 40:1,15 55:24 61:5 92:1 97:21 98:25 99:3 118:5 139:1 147:6 157:22 today's [3] 1:9,10 27:9 together [4] 48:16,22 49:16 115:19 tolerate [1] 19:14 Tom [1] 1:25 tomorrow [6] 1:13 4:23 40:3 143:21 144:10 166:11 tomorrow's [1] 12:5 tonight [1] 99:4 too [5] 37:9 70:7 85:9,19 105:17 took [4] 59:21,22 70:8 95:23 top [5] 64:3 71:23 72:3 104:24 105:6 topic [1] 75:25 Torbay [1] 167:6 Toronto [2] 20:16 21:1 total [17] 65:5 68:22 89:19 91:18 92:1 110:4 112:12 128:6,11,12,25 133:22 140:23,25 141:1 141:5,8 totally [4] 14:12,14 49:19 100:3 towards [3] 58:20 94:7 94:9 training [1] 27:10 transcribed [1] 167:7 transcript [1] 167:3 transcripts [1] 1:9 transfer [2] 14:9 163:2 Transferring [1] 163:5 translate [1] 139:3 transmission [6] 109:10 109:16 110:2,7,10,24 transpired [1] 52:17 treat [1] 109:21 treated [1] 99:24 trees [1] 58:21 Trepassey [1] 61:24 tribunal [1] 19:16 tropical [3] 60:23 61:12 61:15 true [2] 17:15 167:2 truism [1] 78:10 truth [3] 144:12,12,13 try [3] 34:23 59:16 142:8 trying [11] 74:13,13 87:18 89:23 99:2 102:23 124:25 125:23 129:9 134:19 136:17 Tuesday [1] 59:4 turn [13] 11:3,25 39:15 43:25 53:21 84:17 85:12 88:25 118:3 150:22 153:7 153:15 162:22 turning [3] 43:4 48:23	130:7 turns [1] 80:9 two [28] 14:11 16:11 20:12 26:8 30:16,19 41:21 49:23 50:17 56:22 68:15 77:18 81:8 88:18 88:19 125:20,20,22 127:7 134:21 135:2 145:7,20 146:18 149:1 151:20 156:8 159:13 type [8] 15:11 58:15 117:14,23 118:18 119:2 129:22 133:5 types [3] 58:22 117:12 118:2 typically [4] 33:18 117:14 148:8 150:23 <hr/> -U- <hr/> Uh-hm [4] 137:18 138:16 140:19 141:23 unacceptable [1] 81:9 unbalanced [1] 159:5 uncertainty [2] 154:17 154:20 unchanged [3] 157:17 160:8 162:21 under [12] 43:8 73:11 77:7 81:9,22,25 87:22 102:3 113:21 138:15 159:3 165:16 understand [16] 28:7 42:7 56:20 67:25 69:12 70:3 73:1 85:5,8 112:1 116:7 119:5 135:23 143:9 143:20 153:12 undertaking [8] 82:8 82:13,20,25 83:23 86:9 86:13 88:22 undertakings [6] 85:17 85:22 87:18 88:11,17,25 unfair [1] 153:20 uninformed [2] 139:6 139:15 unique [5] 29:6 62:11,22 92:20 110:13 unit [1] 117:8 United [4] 15:3 21:17 22:12 62:25 University [2] 20:16 21:1 unless [5] 12:21 85:24 94:7 125:8 135:14 Unlimited [1] 1:8 unnatural [1] 122:1 unrealistic [1] 13:2 unreasonable [1] 9:17 unreliable [1] 136:1 unusual [1] 31:23 up [37] 7:11 14:14,21 26:12 44:1 46:2 50:23 60:2,4 61:6,13,21,21 65:19 66:7 70:2 72:25 74:17 78:17,21 91:6,7 92:14 94:1 98:21 108:10	115:16 116:2 117:17 120:25 122:3,18 129:10 138:25 142:2,6 147:21 update [1] 10:22 updated [1] 10:18 urban [3] 30:23 117:11 134:15 urbanization [2] 92:20 134:11 used [6] 4:8 14:21 39:10 77:20 92:19 159:7 using [7] 10:22 72:5 133:18,18,19,23 161:2 usually [1] 127:25 utilities [22] 15:5 24:4 29:12,16,24 31:18 37:15 47:9 100:7 108:13,17,19 109:2 123:5,8,20 125:5 125:9 128:15 152:6 154:7 167:6 utilities" [1] 123:16 utility [55] 9:7 13:13,23 21:13,16,20,23 22:12 28:8 29:1,7,18 32:11,21 33:15,17,21,22 37:21 38:23 46:19 50:1 98:14 99:23 102:21 106:21 107:12,21 108:20 109:12 110:9 112:20 127:16,24 128:13,18,25 150:24 151:2 152:20 155:25 158:5,6,7,8,10,12,14 160:16,20,23 161:2,5,7 161:21 utility's [1] 162:12 utility" [2] 108:15,23 <hr/> -V- <hr/> Vale [2] 91:20 120:9 value [1] 150:16 Vanderweide [6] 12:13 34:6 47:25 48:7 49:2 153:5 variables [2] 108:1 115:14 variance [2] 7:1 24:25 various [7] 51:21 52:25 55:22 81:3 99:7 108:6 129:8 Vectrin [1] 16:15 vegetation [1] 58:21 versus [3] 71:14 87:12 117:11 vertically [1] 110:16 vice [10] 12:6 66:16 71:9 100:9,10 104:13,14,15 137:22 144:19 vice-president [2] 12:17 20:9 vice-presidents [2] 67:1 71:2 view [5] 37:22 39:21 92:6 96:9 127:15 viewed [1] 160:5 views [1] 39:18	virtually [1] 15:18 virtue [2] 73:23 75:5 visibility [1] 141:22 volatility [3] 15:22 139:10 155:6 Volume [1] 42:8 VP [2] 119:18 121:5 vu [1] 16:6 <hr/> -W- <hr/> wait [1] 1:13 wand [1] 48:24 wants [2] 13:6 86:11 warrant [1] 165:19 warranted [1] 151:15 ways [1] 26:22 weaker [2] 148:1 152:4 weather [11] 4:3 12:5 29:8 30:2 56:18 61:2 62:8 98:25 112:8 130:22 143:20 website [1] 53:5 week [5] 3:9 5:13,14 48:2 49:4 weekend [2] 48:3 58:12 weeks [2] 118:8,8 weight [4] 68:23,25 69:1 129:9 weighting [4] 68:14,17 68:21 70:5 Wells [2] 1:5,21 west [3] 61:22 101:4 138:4 whereas [1] 58:15 white [1] 111:8 whole [13] 48:17 81:16 84:12 87:16 95:22 97:1 111:22 113:2 115:18 119:17 122:12 140:3 144:12 wholly [1] 13:2 wide [1] 22:11 widely [1] 21:4 Wiedmayer [1] 12:14 willing [1] 106:11 wind [7] 30:6 58:16 61:6 61:7,8 111:10 144:11 windy [1] 111:9 wires [3] 14:4 58:22 109:15 wise [2] 8:1 44:22 wish [5] 23:17 53:2 89:3 104:25 145:2 wishes [2] 5:7 43:3 within [10] 36:9 46:16 46:19,21 93:19 107:6 117:18 131:5 145:25 158:21 without [7] 5:5 16:18 60:7 75:22 76:21 82:2 116:25 witness [16] 12:6 16:11	20:13 21:12 22:22,23,24 83:2,8 103:25 104:3,6,9 142:11,12 143:10 witnesses [16] 5:12 6:13 7:20 12:1,3 15:3 16:12 16:25 20:12 22:5 47:25 88:12 97:13,16,19 100:4 wondering [3] 77:15 99:3 138:19 wood [1] 94:2 wood/oil [1] 94:10 word [1] 134:8 words [2] 17:14 141:7 worked [7] 31:18 98:5 100:21 104:9 106:7 109:6 115:8 workers [12] 27:8 31:2 90:11,12,16,21,22 91:12 92:22 93:1,3 113:9 workforce [11] 27:3,6 31:1 36:17 91:4 113:2 116:1,12 119:8 120:15 122:21 workload [2] 91:5 116:14 works [1] 121:14 world [1] 56:8 worldwide [1] 62:17 worst [2] 57:8 58:18 wrapped [1] 119:17 wrapping [2] 78:17,21 write [2] 93:10 119:22 written [6] 4:24 86:13 87:20,22 88:10 90:3 wrong [2] 65:9 139:1 <hr/> -Y- <hr/> year [22] 8:1,2 9:24 11:15 11:24 37:18 41:25 58:4 59:9,21 75:21 76:6 124:3 124:20 130:11,18 131:18 147:2 149:4 151:20 158:8 161:2 years [35] 8:21 10:20 17:11,22 31:4 36:9 40:6 41:12,22 42:24 46:14 52:4 57:9 62:8 63:2 66:25 67:8 69:14 72:5 76:3 82:3,5 89:2 112:18 112:20 113:7 116:14 118:23 130:12 132:12 134:4 135:16 136:1 145:24 153:14 yesterday [1] 50:17 yet [3] 14:1 17:5 42:3 yield [3] 38:22 157:24 161:16 yields [18] 139:10 155:5 155:8,24,25 156:3 157:15 158:7,9,23 159:1 160:3 161:15,20,23 162:1,11 162:15 Yogi [1] 16:6 York [1] 152:7 yourself [7] 64:1 66:15
--	---	--	---	---

72:19 77:17 97:12 120:22 129:23 yourselves [3] 1:16 82:9 126:10 -“- “Current [1] 108:16 “How [2] 108:11 124:6 “In [1] 116:11 “Newfoundland [1] 123:14 “x” [1] 119:24				
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