

1 New Brunswick Energy and Utilities Board

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5 IN THE MATTER OF an application by New Brunswick Power
6 Distribution and Customer Service Corporation (DISCO) for
7 approval of changes in its Charges, Rates and Tolls (Includes
8 Interim Rate Proposal) - Motion to establish a deferral
9 account and to vary Interim Rates approved

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11 Delta Hotel, Saint John, N.B.

12 August 17, 2007

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Henneberry Reporting Service

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15 CHAIRMAN: Raymond Gorman, Q.C.

16 VICE-CHAIRMAN Cyril Johnston

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18 MEMBERS: Donald Barnett

19 Edward McLean

20 Roger McKenzie

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22 BOARD COUNSEL: Ellen Desmond

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24 BOARD STAFF: Doug Goss

25 David Young

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27 BOARD SECRETARY: Lorraine Légère

28 ASSISTANT SECRETARY: Juliette Savoie

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31 CHAIRMAN: Good morning, everyone. This is a continuation

32 of the August the 8th motion. I will start by taking

33 appearances for the Applicant?

34 MR. MORRISON: Good morning, Mr. Chairman and Board Members,

35 Terrence Morrison and Edward Keyes on behalf of the

36 Applicant. With me at counsel table this morning is Lori

37 Clark, Sharon MacFarlane, Darren Murphy, Vice-President of

38 DISCO and also John Todd, the author of the report that

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we will be putting forward as expert evidence.

CHAIRMAN: Thank you, Mr. Morrison. Formal Intervenors, I will start with Canadian Manufacturers and Exports, NB Division?

MR. LAWSON: Good morning. Gary Lawson appearing with David Plante.

CHAIRMAN: Thank you, Mr. Lawson. Conservation Council of New Brunswick Inc. Enbridge Gas New Brunswick. FPS Canada Inc.

MR. BAIRD: Chuck Baird, Mr. Chairman.

CHAIRMAN: Thank you, Mr. Baird. Irving Oil Limited, we did have a letter indicating they would not be participating yesterday or today. J.D. Irving Pulp and Paper Group?

MR. WOLFE: Wayne Wolfe, Mr. Chairman.

CHAIRMAN: Thank you, Mr. Wolfe. NB Forest Products Association. NBSO. Dr. Sollows?

DR. SOLLOWS: Here, Mr. Chairman.

CHAIRMAN: Thank you. Utilities Municipal.

MS. NEWMAN: Serena Newman, Mr. Chair, for Utilities Municipal. And with me I have Dana Young from Utilities Municipal, Eric Marr and Jeff Garrett from Saint John Energy.

CHAIRMAN: Thank you. Vibrant Communities Saint John.

MR. PEACOCK: Good morning, Mr. Chair. Kurt Peacock here.

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CHAIRMAN: Thank you. Public Intervenor.

MR. THERIAULT: Good morning, Mr. Chair. Daniel Theriault.

And I'm joined with Robert O'Rourke.

CHAIRMAN: Thank you. And the New Brunswick Energy and
Utilities Board.

MS. DESMOND: Ellen Desmond as Board Counsel. With me is
Board Staff, Douglas Goss and David Young and Board
Consultant, Andrew Logan.

CHAIRMAN: Thank you. Just by way of housekeeping, the
documents that the Board ruled on yesterday were marked as
confidential documents. And it strikes me that perhaps to
start off this morning, Mr. Morrison, perhaps we might
mark those documents.

MR. KEYES: Thank you, Mr. Chairman. We have copies, 18
copies of exhibit A, 18 copies of the report from Mr. Todd
and Mr. Todd's c.v. as well, which I can give to the Board
Secretary now. Although we will introduce it when Mr.
Todd takes the stand.

CHAIRMAN: Sure. Well, let's first of all make sure we get
our numbering correct here, so we don't get that out of
order. The confidential unredacted exhibit A was marked
as A-9C yesterday.

And so as not to get it confused with A-9 we are going to
give it a new exhibit number. So the documents being

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circulated at this time will become A-13.

It is not on my exhibit list. I don't recall that we marked it. Perhaps if somebody has the transcript.

MR. KEYES: The issue was it had some argument in it, I believe, Mr. Chairman.

CHAIRMAN: That is correct. I'm told by the Board Secretary that we in fact did not mark that as an exhibit. And the issue, I think as Mr. Keyes points out, was that that particular document contained argument as well as evidence and that it was not going to be entered as an exhibit.

The second document, which had a confidential document number, was John Todd's report dated August the 13th 2007 which was A-12C. That would now become A-14.

And if you have Mr. Todd's c.v., perhaps this might be as good a time as any to circulate that, and we will mark that as A-15.

Are there any other documents that the Applicant has to be marked as exhibits at this time?

MR. MORRISON: No, Mr. Chair.

CHAIRMAN: Ms. Desmond?

MS. DESMOND: Mr. Chair, we haven't got a copy of A-13 at the Staff's table. But in the event the word "confidential" is still on that document, perhaps we could ask that that be striked to avoid any confusion in the

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future with respect to what is in that document.

I understand "confidential" was originally on each page of that document.

CHAIRMAN: Yes. The word "confidential" -- it is entitled Exhibit A - Confidential. I don't think that much will be placed on the basis of the document as found not to be confidential. So I think the parties can disregard any meaning that that word might have.

Are there any -- I guess there is a report, as I understand it, from Mr. Logan, Ms. Desmond. So perhaps -- are you tendering that as an exhibit?

MS. DESMOND: Yes, Mr. Chair. We would like to tender two documents. One is the report of Andrew Logan. And the second is a confidentiality nondisclosure agreement that has been executed by Mr. Logan.

CHAIRMAN: And do you have a copy of both those documents?

MS. DESMOND: I have one copy, Mr. Chair, which I can provide to the Secretary at this time. And perhaps I can make copies at the break.

CHAIRMAN: Sure. It is my understanding that Mr. Logan's report has been distributed to the parties, is that correct? Is there anybody here that did not get it? So everybody has Mr. Logan's report.

So the other document that you are referring to is the

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confidentiality agreement that he signed.

All right. So the confidentiality agreement then will be circulated at a later time. Is that confidentiality agreement substantially in the same form as the one that was circulated yesterday?

MR. MORRISON: I believe it is, Mr. Chairman. But I haven't looked at it specifically line by line. But I believe it is substantially the same.

CHAIRMAN: Thank you. So if I haven't already indicated, Mr. Logan's report then would become NBEUB-1. And the confidentiality agreement would be NEEUB-2.

Any other documents, Ms. Desmond? Any other documents that you wish to enter at this time?

MS. DESMOND: No. Thank you, Mr. Chair. No.

CHAIRMAN: Thank you. Are there any other parties that have documents that are relevant to today's hearing that they feel should be marked at this stage?

DR. SOLLOWS: Mr. Chair, I have a number of documents, evidence filed by Ms. MacFarlane in the previous hearing, copies from -- financial reports of NB Power, those sorts of things that could file them all now. Or we could do them as we proceed through questioning.

MR. MORRISON: Mr. Chair, I believe there is a process for intervenors to file evidence in the regulatory schedule.

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2 CHAIRMAN: Has anybody been given any notice with respect to
3 tendering these documents?

4 DR. SOLLOWS: No. But I understood that this was a hearing
5 to deal just with the notion of whether or not to set up a
6 deferral account.

7 And these are documents related to NB Power's handling of
8 deferral accounts in the past so -- and the accounting
9 practice in relation to deferral accounts.

10 CHAIRMAN: Well, insofar as you may want to use those
11 documents with respect to examination of the witness, we
12 may have to deal with them on a document by document basis
13 as we proceed.

14 DR. SOLLOWS: Yes. All right.

15 CHAIRMAN: But I'm wondering would it be possible for you to
16 provide copies to the Applicant and perhaps to the other
17 Intervenors?

18 DR. SOLLOWS: Absolutely.

19 CHAIRMAN: It may be that there isn't going to be any
20 objection to them in any event despite sort of the
21 process. I don't know.

22 I didn't see the documents certainly. And,
23 Mr. Morrison, I take it that you have not as well?

24 MR. MORRISON: I have not. And my primary concern,
25 Mr. Chairman, is we are here valiantly attempting to

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2 produce the material as soon as possible.

3 And I am concerned about delaying obviously, if there is
4 documents going to be put to a witness of which we had no
5 notice. She is going to need time to review them before
6 she can respond to them.

7 So I just put the parties on notice. And I may be asking
8 for some adjournment.

9 CHAIRMAN: Well, before we proceed would it be useful to
10 take a few minutes for the Applicant and the other parties
11 to have a look at what is being proposed by way of
12 evidence. Perhaps the parties can agree. If not the
13 Board obviously will make a ruling. I don't want to delay
14 the proceeding any further. I understand that, but --

15 MR. MORRISON: I think it would be in order for us to see
16 them before we proceed, Mr. Chairman.

17 CHAIRMAN: Okay. We will take what I hope will be a brief
18 adjournment for that purpose. And if somebody could
19 notify the Board when that review has been concluded.
20 The parties can agree on what goes in. That is fine. If
21 not we will deal with them as they come up through
22 examination of the witness.

23 DR. SOLLOWS: That is fine, Mr. Chairman.

24 MR. MORRISON: Mr. Chair, if they are going to be used for
25 purposes of cross examination, unless he is going to offer

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2 a witness to prove them -- I don't know what the documents are
3 so I'm speaking on -- without any factual background.

4 Often they are not marked as exhibits but are marked by
5 identification for purposes of cross examination. Anyway
6 we can deal with that on a case by case basis.

7 CHAIRMAN: Well, and that may be -- it may well be that you
8 can have a discussion along those lines with Dr. Sollows
9 as to whether or not that would be satisfactory for him.
10 And there may be a compromise here.

11 I'm suggesting if we take a few minutes perhaps you can
12 reach some compromise. If not, as I said, the Board will
13 rule on it. And hopefully it won't take too long. And
14 somebody can advise us when the parties are ready to
15 proceed.

16 Thank you.

17 (Recess - 10:45 a.m. - 11:00 a.m.)

18 CHAIRMAN: Mr. Morrison, have the parties sorted out the
19 process?

20 MR. MORRISON: Well, I think what we are going to do,
21 Mr. Chairman, we -- and I guess not to fuss one way or the
22 other whether they are marked as exhibits. And Dr.
23 Sollows can proceed and put the documents to the witness.
24 I just will caution, although Ms. MacFarlane has -- there
25 is one document that she had read previously, a

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fairly lengthy document. She hasn't read it in some time.

So depending on where we finish today, we may need a little time at the lunch break just for her to refresh her memory on one particular document.

CHAIRMAN: Okay. And I think Dr. Sollows, in terms of when his turn would come up for cross examination, it may well be that we will get to a lunch break in any event. And that will give her an opportunity to read the documents.

Okay. So we will deal with the documents as they come up?

MR. MORRISON: As they come up, yes.

CHAIRMAN: Okay. Any other preliminary matters? Or can we I guess get on with this morning's motion?

MR. MORRISON: Thank you, Mr. Chair. There was some discussion this morning among Intervenors and Board Staff. And I'm going to put a statement on the record I guess. As a result of yesterday's confidentiality hearing and the outcome of that, Distribution Corporation recognizes that the Intervenors only yesterday received the details contained in the evidence filed with the Board in confidence. We appreciate the difficulty this poses to the parties with respect to scrutinizing the financial details. Distribution Corporation is therefore proposing a procedure to enable the Board to approve the deferral

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2 account and thereby facilitate the immediate realization of
3 the benefits of the settlement for customers while at the
4 same time preserving the ability of the Intervenors to
5 question the actual amounts flowing into and out of the
6 deferral account. In this way benefits can begin to flow
7 to customers immediately. And DISCO is not put at risk of
8 underrecovering as a result of a reduction at this time in
9 the interim rate. Therefore Distribution Corporation
10 proposes to establish -- proposes that the Board establish
11 a deferral account to manage the timing differences between
12 the amounts flowing to DISCO through the Coleson Cove
13 tolling agreement on account of the PDVSA settlement and
14 the benefits to be distributed to customers through
15 reduction in the Revenue Requirement -- over the term of
16 the tolling agreement. DISCO is specifically requesting
17 the Board to order the establishment of a deferral
18 account, the provisions of which will be that first, the
19 benefits of the settlement will flow to DISCO by way of
20 reduced fixed charges under the tolling agreement over the
21 life of the tolling agreement. Reduced fixed charges
22 flowing to DISCO through the tolling agreement on account
23 of the PDVSA settlement will flow into the deferral
24 account. Benefits will be distributed to customers
25 annually on a levelized basis. The levelizing period will

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be the term of the tolling agreement. Balances in the account will be subject to interest. The amounts in the account will be trued up annually to ensure the full benefits flow to customers over the period of the tolling agreement and DISCO is kept whole. And we believe that by proceeding in this manner essentially on a prima facie basis if you will that questions concerning the actual details of some of the financial details can be dealt with during the course of the full hearing into this matter in November, and in the intervening period the Intervenors can ask IRs with respect to the matters that are raised around the deferral account.

CHAIRMAN: Just for clarification purposes then, what you are asking for is the approval of a deferral account for the remaining term of the tolling agreement. But the numbers that are plugged into that would be subject to scrutiny at the full hearing. Is that essentially what you are telling us this morning?

MR. MORRISON: That is correct.

CHAIRMAN: Thank you. Are you ready to proceed then?

MR. MORRISON: I am. Mr. Chairman, Members of the Board, I would ask to call Sharon MacFarlane to the stand, please.

SHARON MACFARLANE, having been duly sworn, testified as follows:

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DIRECT EXAMINATION BY MR. MORRISON:

Q.1 - Ms. MacFarlane, could you state your full name and your position for the record please?

A. My name is Sharon MacFarlane. And I am Vice-President of Finance for NB Power Distribution Customer Service Corporation. I'm also the Vice-President Finance and CFO for the NB Power Group of companies.

Q.2 - Ms. MacFarlane, you are aware of why you are before the Board today. And essentially it arises because of what we call the PDVSA lawsuit.

Can you outline in general the terms of that settlement as it affects DISCO?

A. Yes. The settlement represents a reimbursement to NB Power Holdco of capital expended at the Coleson Cove plant to enable it to receive and burn Orimulsion fuel. The settlement included a cash portion and an in kind portion representing a commitment to deliver fuel. And the settlement represents total value to NB Power of \$338 million.

Q.3 - Now, Ms. MacFarlane, do you have exhibit A that is attached to your affidavit sworn to on August 8th before you?

A. Yes, I do.

Q.4 - I'm going to ask you to keep that handy because I will

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2 be drawing you to that.

3 So from your previous comments, in answer to my first
4 question, so the settlement consists of a cash payment and
5 a new fuel supply agreement, is that correct?

6 A. Yes.

7 Q.5 - Now when I look at page 1 of exhibit A, it indicates
8 that the cash payment was how much? Was it \$150.3
9 million?

10 A. It was \$110 million in U.S. currency. And when converted
11 to Canadian currency on the date of receipt it represented
12 \$115.3 million Canadian.

13 Q.6 - And has that cash payment been received?

14 A. Yes, it has.

15 Q.7 - Moving on further in page 1 of exhibit A. There is
16 reference to \$222.3 million as the in kind portion of the
17 settlement. Can you explain that please?

18 A. The in kind portion of the settlement represents
19 consideration through a new fuel supply agreement of a
20 specified quantity of heavy fuel oil at a specified price.

21 Because that price is less than what NB Power would
22 otherwise pay on the market, there is value there.

23 And the value of the consideration is the difference
24 between the market price for heavy fuel oil and the price
25 specified in the agreement times the quantity made

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available under the settlement.

Q.8 - And if you turn the page to page 2 of exhibit A, at the very top of the page, there is reference in -- it says "The settlement represents a recovery of the capital spent to prepare Coleson Cove generating station to receive and burn Orimulsion fuel." Can you explain what that means please?

A. The Coleson Cove Refurbishment Project -- and some of you would have been familiar with it from previous hearings -- was completed in 2004. And it represented four major items.

First and most significantly was the conversion of the boilers to burn liquid fuels in addition to heavy fuel oil and specifically in this case including Orimulsion. Secondly, to add significant emission control systems to allow burning of Orimulsion and other liquid fuels within environmental standards for air emissions.

We also undertook other work required to extend the life of the plant from 2017 to 2030. And in addition \$47 million was expended toward the building of a fuel delivery system which was never completed. This was a facility to receive Orimulsion from the supplier.

I'm sorry. I'm not complete. Because a portion of the capital that was spent, as I just outlined, was

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2 directly related to preparing Coleson to receive and burn
3 Orimulsion which would not have been spent if the
4 Orimulsion contact was not in place and Orimulsion had not
5 been made available. The settlement recovers those costs
6 for NB Power.

7 The decision therefore was made to have the settlement
8 proceeds directed as a reduction of the capital costs of
9 Coleson and to reduce the related debt.

10 Q.9 - And you spoke briefly about the \$47 million -- the fuel
11 delivery system. Can you explain the application of that
12 \$47 million?

13 A. That is outlined on the top of page 2 of exhibit A. \$47
14 million was spent toward the development of a fuel-
15 handling facility at the Saint John Port, the Canaport
16 area. The work was under way and not yet complete when it
17 became clear that there were difficulties around the
18 Orimulsion matter. The work was halted.
19 Because the work was incomplete no asset existed. And the
20 amount therefore, since no asset existed, it was not
21 capitalized. It was written off by NB Power in its
22 financial statements for the year ended March 2004.
23 The write-off in that year flowed into the NB Power
24 deficit. And because the NB Power deficit rose up to the
25 deficit of the Province of New Brunswick, that expenditure

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has effectively been borne by taxpayers.

In making the decision of how the settlement would be applied, it was directed that the first call on the settlement would be to repair that situation and reimburse the deficit and hence the taxpayer for this charge.

Q.10 - Now, Ms. MacFarlane, the balance indicates there is 291,000,000. And that is also referenced on page 2 of exhibit A. Can you explain how that is being applied?

A. Yes. The remaining 291,000,000 of the total 338' is being directed to reduce the capital cost of the Coleson Cove plant so it will lead to reduced amortization expense on an annual basis over time.

And the full amount is also being applied to reduce the debt that was issued to support those expenditures.

Q.11 - Ms. MacFarlane, can you explain how this settlement benefits DISCO and its customers?

A. The -- as I say, without the Orimulsion being available, the portion of the capital expenditures to convert the plant specifically for Orimulsion would not have been spent.

The settlement repairs that situation and therefore reduces the capital cost of Coleson, reduces the mortgage, shall we say, on the facility. This will result in reduced annual fixed charges for Coleson Cove in the way

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of amortization and interest.

And those savings by the way are referenced in table A on exhibit A. Those fixed charges are passed from Coleson to DISCO through the tolling agreement. So the fact that they are reduced means that the capacity payment from Coleson to DISCO can be reduced.

Q.12 - And we have gone through what I will call the treatment of the settlement. But part of the reason, probably the primary reason why we are here is we are proposing that a deferral account be established.

Can you explain, perhaps better than I have been able to explain, first of the deferral account and how it will operate?

A. Mmmm. In reviewing this matter the NB Power board felt that it was important to get the benefit of the settlement to ratepayers as quickly as possible and in as straightforward a manner as possible. By levelizing the return of that benefit to ratepayers equally over the life of the tolling agreement, all ratepayers through all generations have the same benefit.

Because to date they are all paying the cost of that higher capital cost plant.

However, the savings in the first two or three years that are derived from the settlement -- because the fuel

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supply agreement takes some time for its value to be achieved.

You can see in table A the savings flowing to DISCO from
Coleson climb over the first three years of the
settlement.

The reason for the request of the deferral account is
simply to manage those timing differences, to let the
settlement benefits flow as they will. And in the first
three years those are in amounts different in each of the
three years. But to get immediately to the ratepayer a
benefit that will be put in place and will stay in place
at an equal amount over time.

So the deferral account is about managing the differences
between the amounts flowing to DISCO through the tolling
agreement on account of the settlement and the benefits to
be distributed to customers through a reduction in the
Revenue Requirement on a levelized basis. And the hope
was to simplify and expedite the return to ratepayers in a
simplified manner, being levelized.

Q.13 - I believe you may have already answered this, Ms.

MacFarlane. But essentially -- I will let you -- the
purpose then of the deferral account in summary form is to
do what?

A. It is to ensure that the full benefit of the settlement
gets to customers in a way that respects the

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2 regulatory principle of intergenerational equity, respects the
3 regulatory principle of rate stability and keeps DISCO
4 whole over the term of this Coleson Cove tolling
5 agreement.

6 MR. MORRISON: Those are all my questions, Mr. Chairman.

7 CHAIRMAN: Thank you, Mr. Morrison.

8 Cross examination, Mr. Lawson?

9 MR. LAWSON: Thank you, Mr. Chairman.

10 CROSS-EXAMINATION BY MR. LAWSON:

11 Q.14 - I will try to be brief with the very easy subject that
12 we are dealing with today. So I apologize again for not
13 having learned all of the accounting concepts that we have
14 to deal with since 4:30 last night. It will be evident
15 that I didn't learn everything on my questioning.

16 May I start first by asking am I correct in understanding
17 that 100 percent of all of the savings that are to be
18 achieved or the settlement that has been achieved is being
19 passed down through to DISCO?

20 A. 100 percent of what is being used to reduce the Coleson
21 Cove plant value on related debt is being passed through
22 to DISCO.

23 You will not on the top of page 2 of exhibit A, as I
24 discussed just a moment ago, 47,000,000 is being used to
25 reimburse the write-off that was taken and passed through

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to the NB Power deficit.

And is effectively therefore held by taxpayers, DISCO and its customers never paid that. Therefore it would be a windfall if they received that.

Q.15 - Okay. So the \$47 million -- and I wasn't sure in your direct evidence. So the \$47 million in fact will have no impact on DISCO when it is paid to, as it is described here, as used as a recovery against the cost of a fuel delivery system?

A. It will have an impact on DISCO, the company, in the sense that the accounting for this will flow through DISCO's financial statements. It will not have an impact on the Revenue Requirement or ratepayers.

Because ratepayers -- it was never -- as a write-off it was never included in the Revenue Requirement. So it has never been included in rate. It has never been charged to ratepayers.

So therefore they don't get the reimbursement for it. It was charged to taxpayers. It is getting reimbursed to taxpayers.

Q.16 - So back in 2004, whenever it was that it was absorbed by the taxpayers, as you call it, that had no impact on DISCO's -- I guess DISCO wasn't in existence at the time, if my memory serves me correctly.

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2 A. Yes.

3 Q.17 - Is that right?

4 A. That's right.

5 Q.18 - So it was not factored in any fashion in the rates paid
6 by the customers of NB Power in the regulated rates?

7 A. That's correct.

8 Q.19 - Am I correct in assuming, and I'm taxing my memory,
9 that in 2004 there was no review of rates, no filing
10 required because the rate increase was under 3 percent in
11 any event?

12 A. That's correct.

13 Q.20 - So in fact we wouldn't know whether or not it was --
14 the rate increase was in fact inclusive of the 47'. You
15 are saying that it was not factored in for your own
16 internal purposes?

17 A. Well, let me clarify that the write-off was made at the
18 end of the year. It was made on March 31st 2004. Had
19 there been a rate application, as you know, it would have
20 been based on forecasted costs. It would have been done
21 before the year began.

22 That write-off couldn't have been anticipated. So it
23 would not have been included in the Revenue Requirement in
24 any event.

25 Q.21 - Now you said that it was written off because there

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2 wasn't any -- sorry, it was absorbed by the taxpayer because
3 there wasn't any asset per se to depreciate, is that
4 right?

5 A. That's correct.

6 Q.22 - So nothing -- there was no value achieved by NB Power
7 for that \$47 million?

8 A. That's correct.

9 Q.23 - Am I correct in understanding then, aside from that \$47
10 million, the \$291 million is all of the balance of the
11 settlement that is being achieved -- or valued as it has
12 been a value based on the assumptions of future fuel costs
13 I presume and so on?

14 A. That's correct.

15 Q.24 - And that is all being flowed through in the manner you
16 wish to propose it to. You are proposing it all being
17 flowed through down to DISCO?

18 A. That's correct.

19 Q.25 - Okay. Now what happens if there isn't a deferral
20 account?

21 A. If there isn't a deferral account DISCO would receive --
22 I will refer you to table A of exhibit A. DISCO in the
23 2007-08 fiscal year would receive savings of 13.5 million
24 flowing through the tolling agreement.

25 And DISCO would be here applying to have its Revenue

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Requirement reduced by 13.5 million, which is about a little over 1 percent reduction in rates.

In the following year when the Revenue Requirement is reviewed, the Revenue Requirement would be reduced by the actual amount of savings that DISCO receives in that year, which is estimated at 24.4 million. And that would have a positive impact on rates of -- I forget the calculation. But I believe it's about 1.9 percent. It would not be until the third year when the full value from the fuel supply agreement has been realized that we would see the reduction in rates of 2.5 percent.

The board of directors of NB Power believed that it was in the best interest of ratepayers that the settlement be done once, the benefit of the settlement be evaluated once, be evaluated in a levelized manner, so that each year the ratepayers are receiving the same value.

Q.26 - Now the premise on which those calculations are made starts on the top of page 2 where it says "Because the settlement represents a recovery of the capital spent to prepare Coleson Cove generating station"?

A. Yes.

Q.27 - I understand, and my understanding is purely from the press, that the claim that was made against -- whatever, however that company is pronounced -- the Venezuelan

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2 company, for which I apologize -- that it was about \$2.2

3 billion, is that right?

4 A. That's correct.

5 Q.28 - And obviously all of that wasn't for capital?

6 A. That's correct.

7 Q.29 - In fact the majority, in fact a significant majority of

8 it, was in fact claimed for the extra cost of fuel and

9 operating cost as opposed to capital cost, is that right?

10 A. Out into the future, yes.

11 Q.30 - Yes, out into the future. So how is it then that you

12 can make the statement that the settlement represents a

13 recovery of the capital cost when in fact the claim was

14 substantially higher than the amount of \$330 million

15 roughly, and the claim was for -- much more so for fuel

16 costs rather than capital costs?

17 A. The premise of the settlement -- and I was not included in

18 the settlement discussions. I have only been privy to

19 discussions about them.

20 But the premise of the settlement was a recognition by

21 both parties that in fact capital had been expended that

22 would not otherwise have been expended if Orimulsion was

23 not going to be available.

24 The Orimulsion is not available. That is a fact. PDVSA

25 was not prepared to make Orimulsion available. That

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was not on the table for a discussion in the settlement arrangements at all.

But what was on the table was a recognition between two parties that some unfairness had occurred because capital had been spent in expectation of something that didn't happen.

In fact in the Coleson fuel supply agreement there is a clause that contemplated that at some point in time the contract might not continue, that at some point in time Orimulsion deliveries may stop.

And that clause recognized that if that happened, PDVSA would reimburse NB Power for capital spent to prepare the plant to burn Orimulsion. So the discussions around the settlement focused on that clause, that amount, that premise.

Q.31 - Now I don't know if you have been engaged in litigation frequently. I hope not. But if you have -- for those of us who have been engaged in it with some regularity, settlements usually don't -- nobody cares when they are getting a cheque how it gets allocated.

Is it fair to say that to your knowledge there was no specific allocation in the agreement of these payments as to whether or not it was specifically agreed by the parties that it was for capital reimbursement?

2 MR. MORRISON: I think we have to tread a little carefully,
3 Mr. Chairman, in terms of the specifics of the settlement
4 agreement for the reasons I articulated yesterday. I just
5 raise it.

6 And perhaps Ms. MacFarlane can answer the question without
7 breaching any of the confidentiality provisions of the
8 settlement agreement. But I just raise it.

9 CHAIRMAN: Thank you. Perhaps we will see how she -- how
10 her attempt works out I guess to do that.

11 A. I will answer the question to agree with your premise,
12 that it is often not stated in the agreement, what the
13 settlement is to be used for. It is simply a settlement.
14 That's very much a common practice.

15 However, NB Power had an objective in reaching the
16 settlement. And it was to protect ratepayers from having
17 -- continuing with the burden of paying for capital for
18 which they were not able to get the value that they would
19 have gotten had they gotten cheaper fuel.

20 So from that perspective, it is a very logical outcome
21 that this would be used to reduce the capital costs of the
22 plant. I assume you are suggesting that it could be used
23 as fuel expense in the near term.

24 If that were the case, if this settlement or the fuel
25 portion of the settlement were used to reduce fuel expense

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2 in the near term, we believe that would violate the concept of
3 intergenerational equity.

4 Because it would put all the benefit to people in --
5 ratepayers in the near term, and leave the ratepayers in
6 the long term paying the higher mortgage on the plant
7 without necessarily getting the value from it

8 Q.32 - Well, rather than engaging in a debate of the merits of
9 your point, I think it is fair to say then your statement
10 that because the settlement -- this document statement
11 says "Because the settlement represents a recovery of the
12 capital spent" -- is in fact the decision of how NB Power
13 chose to attribute this money, not anybody else's
14 determination, no legal binding obligation to attribute to
15 capital?

16 A. That's correct.

17 Q.33 - Okay. And therefore you would agree it is open to the
18 Board to decide what is an appropriate way of allocating
19 these monies?

20 MR. MORRISON: Certainly I will be addressing that in
21 argument. And I can say that my position and state that
22 we don't think it is open to the Board.

23 What is before the Board is what flows to DISCO. What
24 flows to DISCO is reduced fixed capital charges flowing
25 through the tolling agreement.

2 So just to put Mr. Lawson on notice that Ms. MacFarlane
3 isn't going to engage in legal argument. But that is the
4 position that DISCO is taking.

5 CHAIRMAN: We look forward to hearing your argument on that
6 point later on.

7 Q.34 - So is it your understanding on behalf of DISCO that
8 DISCO must accept that which was decided by Holdco I'm
9 assuming as to -- in order to attribute this to capital
10 costs, is that right?

11 A. Yes.

12 Q.35 - DISCO wasn't participant in that decision?

13 A. DISCO -- the decision was made by the boards of directors
14 of the group of companies.

15 Q.36 - Which is all one board?

16 A. The members are common. It is five separate boards. So
17 the board of DISCO -- the board of all of the companies
18 together would have made this decision in the best
19 interests of the group of companies and the customer.

20 Q.37 - Now again relying on the press in my memory as my
21 sources, so I stand to be corrected, I thought I heard
22 somewhere that the board of directors took something like
23 10 minutes to decide how to allocate this money to the
24 capital cost and loan repayment.

25 Is that your understanding of what the press at least

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2 reported?

3 A. I did not see that in the press. And I was in the
4 meeting. And I can assure you that that is a false
5 statement.

6 Q.38 - I presume that the Board gave consideration to a
7 variety of alternatives of how to allocate these monies
8 before they reached the decision to allocate them as
9 capital costs, is that right?

10 A. A number of alternatives were discussed.

11 Q.39 - And could you outline for us what the alternatives were
12 that were discussed please?

13 A. I'm just not sure that I'm in a position to discuss what
14 happens in a board meeting, given that those board
15 meetings are not open to the public. That's my challenge.
16 I don't know that.

17 MR. MORRISON: We are getting into an area, Mr. Chairman --
18 I can understand the witness' discomfort with the
19 question.

20 I guess the best way I can characterize it is that from
21 DISCO's perspective -- DISCO is the regulated entity and
22 DISCO is the Applicant here. DISCO is the only one of the
23 NB Power group of companies over which the Board has
24 jurisdiction. DISCO is going to receive the benefits of
25 the settlement in a particular manner. That has been

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decided.

What other alternatives were considered before making that decision and before DISCO basically -- I don't like to use the word fait accompli. But as far as DISCO is concerned there is a benefit flowing to it that has been structured.

The alternatives that may have been open to a Board, as far as DISCO is concerned, may be irrelevant. Because the final analysis, it is what it is as far as DISCO is concerned. And that is my challenge, Mr. Chairman.

CHAIRMAN: Mr. Morrison, my understanding of the question is simply to have the witness answer whether or not other alternatives were considered and what those alternatives might have been.

We are here today to determine whether or not a deferral account is the appropriate way to proceed. And insofar as this witness would have been present at the DISCO board meeting, it strikes me that that would be something she could be questioned on. Now with respect to board meetings of the other companies, that is perhaps a different issue.

But I understand Mr. Lawson's question is simply what are the other alternatives that may have been discussed? Were there other ways of dealing with --

2 MR. MORRISON: We are certainly not trying to -- I just
3 understand the witness' discomfort with disclosing what
4 she probably believes are confidential discussions in a
5 board meeting.

6 CHAIRMAN: Sure. And I think that she could perhaps answer
7 the question in such a way as to not breach certainly any
8 confidentiality with respect to the other Board meetings
9 not relating to DISCO, and at least in a general sense
10 answer Mr. Lawson's question with respect to whether or
11 not there were other alternatives that perhaps were talked
12 about.

13 A. Perhaps I can answer your question by indicating what
14 other alternatives management advised the board were
15 available as alternatives. Does that sound reasonable?

16 Q.40 - That would be a good start. Thank you.

17 A. Okay. All right. The discussion -- let me start by
18 saying that management believed very strongly that this
19 was the appropriate way to treat this settlement.
20 It's -- like to get an analogy, if a person sells their
21 house, the responsible thing to do is to pay off the
22 mortgage. You could instead take a trip around the world
23 and you would probably enjoy it in the short run, but
24 when you came back you would have no place to live and you
25 would still have the debt.

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So the Board was very much of the view, and management believed very strongly, that the responsible thing here to do was to reduce the capital cost and to pay down the mortgage.

Having said that, other alternatives that were put forward were not ones that management believed in, but felt that might be raised in other parties or that at least people should be aware, the board members should be aware that people might be thinking of them.

And one of them was that the fuel portion of the settlement should be treated as fuel in the two plus fiscal years in which the fuel was received. That was put forward.

And it was made clear that the fact that the in kind consideration is fuel is irrelevant, it's consideration, it's value. It could have been -- because in kind settlements are quite common in business. It could have been equipment.

It could have been consulting services. It could have been received in anything as long as it was a consideration that provided value to achieve the desired outcome of the settlement. And the value is an equivalent to cash.

So on that understanding there is no reason to treat

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the in kind portion any differently than the cash portion.

And therefore the fact that it is fuel that is being received is irrelevant to what is actually done with the value of the settlement. So that is one discussion that took place.

In terms of other alternatives the other -- the discussion about other alternatives were around if there were to be to DISCO, once DISCO receives the value, and if there was a desire to return that value to the ratepayer, what options should the DISCO board take in that regard?

One was simply to pass on the savings as they were achieved. One was to recognize that by -- on table A you will see by the third year the amount stabilizes.

So one option that was discussed was to say okay, let's average out the first three years and do this in two steps. Let's take the first three year's benefit, levelize that and then carry on with the rest of the settlement without a deferral account. Because what would flow to DISCO would then flow to customers. That was an option that was discussed.

Another option that was discussed was to take the levelizing period over the life of the former fuel supply agreement as opposed to over the life of the tolling agreement. The fuel supply agreement, the original

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2 Coleson fuel supply agreement was 20 years. And the life of
3 the plant is 23 years.

4 So those were options that management put forward simply
5 to inform the Board of the types of discussions that had
6 been had. All of those discussions and all of those
7 alternatives having been set aside as unacceptable,
8 certainly less appropriate than the recommendation
9 management made and the board accepted.

10 Q.41 - I might just comment, your analogy of taking the money
11 and running away on an around the world trip, I don't know
12 would be an equivalent analogy.

13 I'm assuming that the cash that was received and will be
14 received over the next couple of years, my accounting
15 understanding is that the book entry doesn't deal with the
16 cash.

17 You are going to put the cash and presumably not declare
18 management bonuses with it. It will be to reduce debt, is
19 that right, regardless?

20 A. It will be used to reduce the capital cost of the plant
21 and to reduce debt.

22 Q.42 - Regardless of what you do with it from an accounting
23 point of view, whether it is -- whether you attribute it
24 to the capital cost allowance or otherwise?

25 A. No. I'm sorry. If that cash were being used to build

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2 a new building or if the cash were instead being directed to
3 management bonuses, it would not be directed to reducing
4 the debt.

5 Q.43 - But am I correct in understanding that you could -- for
6 example, one of the options you mentioned was it was an in
7 kind amount. You dealt with it the same as cash and
8 therefore ruled it out.

9 But basically taking the savings in fuel in the year in
10 which it is accomplished. So in years 2 and 3, where the
11 bulk of it would be, put it in there.

12 If the cash savings were achieved and you put that into --
13 didn't attribute it to capital, the cash savings itself,
14 you would have an operational -- let's say profit -- and
15 we will say -- I'm assuming a profit would result in those
16 two years. I don't know what the forecasts are. But
17 let's assume a profit would result in those two years.
18 You would also have the cash available in those years.
19 And that cash could equally, am I correct, not be applied
20 towards reducing the debt of the company?

21 A. I'm sorry. I didn't quite follow your reasoning. But
22 generally whatever it is you are doing with the
23 settlement, the cash flows with it.

24 Q.44 - Let me just try to make it as simple as I can. And I'm
25 usually pretty good at making things simple, perhaps not

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2 easy to understand. But if in year 2 there is \$100 million in
3 savings in fuel --

4 A. Yes.

5 Q.45 - -- that \$100 million can be considered as part of the
6 operating costs, if you will, a savings, a reduced
7 operating cost in that year, correct?

8 A. Mmmm.

9 Q.46 - That was one of the options I understood to be
10 considered. And as a result your needs would be reduced
11 by \$100 million for fuel costs?

12 A. Yes.

13 Q.47 - You have -- is there some cash available -- I guess I'm
14 mixing up the fuel savings and the \$100 million in cash,
15 aren't I?

16 A. Yes. But I understand your point. I know there isn't
17 cash available. Because I'm assuming that we would have
18 less fuel costs, which means our revenue requirement would
19 be less. So we would not receive the cash from a
20 customer.

21 Q.48 - The \$100 million then, the \$115 million or 12' or
22 whichever that amount came out to be -- \$115 million that
23 you got in cash?

24 A. That is correct. Similarly that 115 million, if a
25 decision had been made to reduce the revenue requirement

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2 immediately by \$115 million, then that money would not be
3 available to pay down debt.

4 And it is no different than if the fuel is used
5 immediately as an in-year benefit. That violates
6 intergenerational equity. Ratepayers are left to pay the
7 full capital cost of that plant out to the period 2030
8 because a few ratepayers received the benefit of the
9 settlement in years 1, 2 and 3.

10 Q.49 - Now you mentioned you ruled out that option of sort of
11 taking it as the savings are achieved because you viewed
12 the cash as no different. It was an in kind saving, if
13 you will. Again isn't it true that some of the loss that
14 was suffered by NB Power which precipitated the \$2.2
15 billion claim was lost fuel -- extra fuel costs?

16 A. That is a lost opportunity cost.

17 Q.50 - That's right.

18 A. This is actually -- the capital cost was actually cash out
19 the door, mortgage assumed. It's real. The fuel portion
20 was a lost opportunity.

21 Q.51 - Well, the fuel costs were lost cash savings?

22 A. No, because the fuel was never expended in the first
23 place. It is a lost opportunity in the future to have
24 cheaper fuel, whereas the capital cost of the plant is a
25 sunk cost. Historically it's done, it's there. It's

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2 money that was expended and ratepayers are supporting.

3 Q.52 - In year two --

4 A. Yes.

5 Q.53 - -- which would be the next fiscal year, if the

6 Orimulsion deal had taken -- been fulfilled --

7 A. Yes.

8 Q.54 - -- your fuel costs would have been significantly -- and

9 I don't know the order of magnitude -- significantly lower

10 next year -- DISCO's fuel costs?

11 A. Right.

12 Q.55 - And therefore it's needs would be less, correct?

13 A. That's correct. And you are speaking in the future tense

14 which means it is an opportunity, not a real --

15 Q.56 - Semantics aside for the moment --

16 A. Okay.

17 Q.57 - -- the ratepayers would have had to pay less next year

18 if the Orimulsion deal had gone ahead because its fuel

19 costs would be cheaper for DISCO?

20 A. That's correct.

21 Q.58 - And what we are talking about in this analogy or this

22 option you consider would be a savings in fuel costs next

23 year by DISCO customers, correct?

24 A. That's true, and if the Orimulsion agreement had carried

25 forward there would have been a savings for 20

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2 years.

3 Q.59 - Well a balance of 17 years, isn't that right?

4 A. But because the settlement is such that it is if it were
5 applied to fuel it would only be two years worth of
6 ratepayers that would benefit, not the entire 17 years
7 benefit for the customers. Again it violates the inter-
8 generational equity principle.

9 Q.60 - I understand. Now your 23 years that you have chosen
10 is the balance from today forward of the life of the
11 tolling agreement, correct?

12 A. That's correct.

13 Q.61 - And it would be about 17 years left on the life of the
14 Orimulsion contract, is that right?

15 A. That's subject to check.

16 Q.62 - Okay. It was a 20 year contract?

17 A. I'm sorry, I would have to check it.

18 Q.63 - There is reference in one of the documents that was
19 filed that says it was a 20 year contract, so I think
20 that's where I did my math, and I presume it was in 2004
21 or thereabouts that it was to start. So it is in the
22 neighbourhood of 17 years, would you agree?

23 A. I say subject to check because it may have been that the
24 contract -- I just forget. It may have been that the
25 contract was for delivery of a quantity.

2 Q.64 - As opposed to a 20 year?

3 A. Right.

4 Q.65 - As I say I'm just going on the basis I believe it was
5 Mr. Todd's report or some -- one of these documents refers
6 to it as 20 years.

7 A. Okay.

8 Q.66 - Perhaps you can just explain to me how you envisage
9 this -- I will call it the separation of the deferral
10 account concept and the subsequent review through the IR
11 processes and the evidence to follow, the numeric
12 component of the deferral account? In other words is the
13 2.5 the right number as opposed to the deferral concept?
14 Perhaps if you could explain to me how you understand it
15 would work if it should flow subsequently that the 2.5 was
16 not the right number? So for example it should have been
17 3 or it should have been 2 how would you envisage that
18 happening?

19 A. My understanding is that the numbers will be examined and
20 the deferral account having been established the number
21 that flows from the tolling agreement into DISCO will go
22 into that deferral account and it will be subject to
23 examination. And a calculation will be done and verified.
24 We have done it. It has been looked at by the Board's
25 expert but it will be verified that in fact the

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2 benefits over the life of the tolling agreement that will flow
3 through the Coleson agreement will be X, and a mortgage-
4 style calculation, which has been done and looked at by
5 the Board's expert, will be verified to say if that's the
6 case what is a levelized return to the ratepayer. And
7 that amount will come out of the deferral account.

8 So my understanding is that DISCO, regardless of the
9 numbers that we use in the interim rate hearing as it goes
10 to this particular issue, DISCO will be kept whole,
11 because what goes into the account is a savings, what
12 comes out of the account is the amount that should be
13 distributed to ratepayers, and if a different amount was
14 distributed that will sit in the deferral account for
15 collection at a later period.

16 Q.67 - And that includes any adjustment as you anticipate in
17 this fiscal year as a result of an adjustment in the
18 interim rate?

19 A. That's correct. As you see in the proposal that Mr.
20 Morrison read earlier, we have requested as is common
21 place in deferral accounts that there be a true up to
22 actuals on this account as time goes on, including at the
23 beginning of it.

24 Q.68 - And I do apologize, I'm going to ask Mr. Morrison for a

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copy of his notes because he went way faster than my mind and my hand were able to track about what the specifics of the request were. So I apologize. I got lost at the life of the tolling agreement which was .1.

Now I hope I'm not crossing into the numeric piece of it but I did like -- I would like to know what the interest components are. If you could explain the interest components both in table A generally, I don't need the numbers, but what the interest component is on table A and on attachment 1, both of which are in exhibit A-13?

A. Okay. Those two interest amounts are different amounts and I will take you through each of them separately. On table A what we see here is a calculation that suggests that if we take the settlement and -- first the cash portion and then the in kind portion as it turns into cash, and reduce our debt in Coleson Cove, obviously Coleson is going to have less interest charges.

So you will see in the first year there is a reduction to enable interest to be lower by \$5 million, by the second year as more is received interest is reduced by \$12 million, and by the time the full fuel supply agreement has reached its value and all of that consideration has been applied against the debt, interest expense is reduced

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2 by \$18 million a year.

3 Q.69 - And that is interest that flows through effectively to

4 DISCO from Coleson Cove?

5 A. Yes. This is interest expense on debt for Coleson Cove,

6 so it forms part of the capacity payment that DISCO pays

7 Coleson Cove.

8 Q.70 - Right.

9 A. The exhibit -- pardon me, attachment 1 is a Disco

10 document. We were just looking at a table that looked at

11 Coleson's costs and --

12 Q.71 - Flowing through to Disco?

13 A. That's right.

14 Q.72 - All right.

15 A. So you would see the numbers that came from table A on

16 line 4 of this document.

17 Q.73 - Yes.

18 A. So line 4 is the savings that come through Coleson to

19 DISCO. Line 2 is the levelized amount that is going to be

20 distributed to customers. And you will notice in the

21 first year that DISCO gets 13.5 million in savings on line

22 4 and on line 2 it returns to customers 29.2 million.

23 Well obviously that means there is 16 million outstanding

24 that DISCO has not recovered and will recover on this

25 schedule over the next 23 years.

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2 So there is an interest component recognizing that DISCO
3 is going to have to finance that amount and the interest
4 component is -- as you see here there is a calculation
5 that suggests it's a million dollars and you see how it
6 declines over time as the balance outstanding declines
7 over time.

8 Q.74 - Yes. Okay. Understood. I would have thought that as
9 the average, I'm going to call it, levelized number of \$29
10 million as time goes on because the rule amount would be
11 in the neighbourhood of \$31 million that there would
12 actually be a credit -- I don't know if it's debit or
13 credit -- but the opposite to the charge of a million
14 dollars to that account because there is a surplus.

15 A. Yes.

16 Q.75 - Is that in there or am I missing it? It appears to be
17 an interest cost all the time.

18 A. Yes. And if you follow the table, in column 1 you see
19 line 5 is the balance. 29 million has been given to
20 customers and only 13 million has been received by DISCO.
21 So it leaves a balance of 16.7 million. In the next year
22 that becomes the opening balance and you pay out 29', you
23 receive 24', and it carries on. You will see out in
24 column -- in year 10 let's say, that you are paying out to
25 customers 29' but you are receiving 31'. So you would be

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2 suggesting that you are getting more savings than you have
3 distributed to customers. But if you look at line one
4 there is an opening balance from all those years when you
5 did the opposite of 18 million.

6 Q.76 - Netting out to zero at the end?

7 A. Right.

8 Q.77 - I understand. Was Mr. Todd consulted by DISCO or
9 Holdco to your knowledge to review the options of how to
10 proceed with the surplus, or was he retained for the
11 purpose of this hearing?

12 A. He was retained before this hearing. He was retained for
13 -- by DISCO for purposes of looking at how DISCO treated
14 the settlement benefits it would receive under the Coleson
15 Cove tolling agreement.

16 Q.78 - But was that after the decision had been made by DISCO
17 and the other Board as to how they were going to treat it?

18 A. That's correct.

19 Q.79 - Okay. So this was prepared effectively for the
20 regulatory process, not for the internal review process?

21 A. Well to the extent that the internal review process
22 included an option that was -- we don't -- we will only
23 return savings as they are received, an option that said
24 we will levelize the first three years and an option that
25 said we will levelize it over the life of the tolling

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2 agreement, Mr. Todd was consulted as to which of those options
3 were best for a regulated utility.

4 Q.80 - Okay. But again am I understanding correctly he was
5 consulted after the determination had already been made --

6 A. After --

7 Q.81 - -- about how it was going to be dealt with?

8 A. After the determination that the settlement would be
9 applied against the debt and the capital cost of Coleson.

10 Q.82 - Can you tell me whether or not the fuel portion of the
11 settlement, the fuel savings portion, will in fact affect
12 the dispatch of power or the type of power that is going
13 to be used in any given time by GENCO or Colesonco or
14 whomever?

15 A. It will not.

16 Q.83 - It won't affect it. And is -- I don't know anything
17 about the volumes, the \$222 million of savings it
18 generates, but it sounds like a lot of money to me -- it
19 is a lot of money to me, I might add, not just sounds like
20 it. In a span of 18 months is it possible that DISCO,
21 Colesonco or NB Power will not be able to use all of the
22 fuel itself under that agreement that is contemplated, the
23 quantity, to achieve the \$222 million in savings?

24 A. Our operational modelling tells us that we can, but of
25 course that has certain assumptions in it about plant

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operations, about availability of ports, about weather and load, et cetera. So there is a possibility.

The deferral calculations are based on an assumption that as it states in exhibit A all of the fuel will be received by June 2009. However, the settlement agreement continues until such time as the quantity specified in the agreement is received.

Q.84 - Okay.

A. So it could be later than that.

Q.85 - As opposed to time running out and --

A. That's correct.

Q.86 - -- you don't get all the savings. Now my understanding is that any risk associated with the failure to achieve, whatever reason, failure to achieve the planned fuel savings, basically flows to DISCO, is that right? So if for example something happens and PDVSA doesn't honour the settlement agreement, the savings we are contemplating in here wouldn't be achieved, is that right?

A. That's correct.

Q.87 - So the settlement agreement itself I am assuming -- and I haven't seen the litigation documents but I'm assuming the settlement agreement itself is with Holdco or at least it was the party who started the action and presumably settled it?

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2 A. That's correct.

3 Q.88 - So Holdco reached a settlement presumably and DISCO

4 bears the risk that the settlement that they reached, it

5 wasn't a good one, is that right?

6 A. DISCO is getting the benefit of any settlement that

7 occurs.

8 Q.89 - And bears the risk if the settlement doesn't come good?

9 A. Presumably DISCO would have borne the risk if there was no

10 settlement. If there -- we have a settlement. It's

11 something that New Brunswickers should be very happy

12 about, because it is a fair recognition, a repair of --

13 reimbursement of capital that was spent on an

14 understanding that was never realized, and that benefit

15 goes to DISCO.

16 If that settlement amount turns out to be a lesser amount

17 then that benefit will go to DISCO. But we have every

18 confidence that we are dealing with a settlement agreement

19 that will be realized.

20 Q.90 - Did DISCO's board actually approve the settlement, or

21 was that just Holdco's board?

22 MR. MORRISON: I don't think we should be getting into the

23 actual -- what Mr. Lawson is getting at is not what I will

24 call the treatment of the settlement but actually looking

25 -- the litigation settlement if you will -- and I

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just don't think this is an appropriate place. It's very difficult, and Mr. Lawson knows that quite well, to second-guess any kind of a settlement in litigation. It's virtually impossible for this Board to pass judgment. So the details of how that litigation settlement occurred are really not germane to this discussion.

CHAIRMAN: What would the relevance be, Mr. Lawson, with respect to the question that you pose to the witness?

MR. LAWSON: Mr. Chairman, first I'm not challenging the issue of the prudence of the settlement because to be honest with you I haven't got two clues whether or not it's a prudent settlement. I'm totally -- I think I read somewhere again, which may be wrong, there were \$6 million spent in legal fees in the battle. I'm not going to pretend over night to have come up with an opinion equally as qualified as theirs. So as to prudence, no question. Really my only point is is that the decision was made by DISCO -- or sorry, by Holdco as I understand it to accept this settlement, that the risk of the settlement not being achieved for whatever reason in fact flows down to DiSCO, and this -- and my question is did DISCO's board get an opportunity to make the decision of whether or not that was a risk that should be taken?

CHAIRMAN: I think your question really is whether or not

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2 DISCO participated in the settlement negotiations, is that
3 effectively what you are asking?

4 MR. LAWSON: Well did DISCO -- having the responsibility
5 resting ultimately on the board, to DISCO's board, but did
6 DISCO itself have any role in the decision making of
7 whether or not to accept it? I would assume that would be
8 a board decision but --

9 A. That was a board decision, and --

10 Q.91 - Of DISCO's?

11 A. It was -- the boards of the companies met as a group, and
12 subject to check of what is documented in the minutes, and
13 I will have to do that, the boards of the group of
14 companies made the decision.

15 This was a very long, protracted and difficult undertaking
16 and was reviewed at every regular and certainly many
17 special board meetings, and the boards reviewed it as a
18 group.

19 Q.92 - Again the theory is all five of them were -- or all the
20 board members were the same for all the companies?

21 A. Yes. And frankly, part of the reason for that is because
22 it's so seldom that something happens to one company that
23 it does not affect another company. So the ultimate --
24 the ultimate reason for having the boards meet together is
25 to ensure that the impact on all companies and

2 ultimately the impact on the customer and the shareholder are
3 considered together.

4 MR. LAWSON: Those are all the questions I have. Thank you.

5 CHAIRMAN: Thank you, Mr. Lawson. Mr. Baird?

6 CROSS-EXAMINATION BY MR. BAIRD:

7 Q.93 - Thank you, Mr. Chairman, members of the Board, Ms.

8 MacFarlane. I have a few questions. Most of them have
9 been covered already, so I won't go over the same ground.

10 My first question is does the settlement cover the entire
11 direct loss that was incurred by the group of companies on
12 the orimulsion project?

13 A. I was not party to the settlement negotiations or
14 discussions. So I'm sorry to say that I can't directly
15 answer your question. Settlements are reached as you
16 know, you have been part of many of them yourself, through
17 negotiations and ultimately what the parties believe is
18 fair. And the NB Power negotiating team endorsed by the
19 NB Power board believes that this was fair reparation of
20 the situation where capital was expended to receive a
21 certain fuel that wasn't received.

22 Q.94 - As the chief financial officer of NB Power you would
23 have knowledge of the direct cost of the project that was
24 out-of-pocket without having to know about the settlement.

25 A. I would have an understanding of the direct cost of

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2 the capital project, but there are indirect costs where some
3 expenditures on the Coleson Cove project were -- could be
4 put in the category of life extension, preparation for
5 orimulsion, some could be put in the category of improved
6 air emissions to burn orimulsion or benefit from those
7 same expenditures to meet other environmental standards.
8 So we can understand that there isn't a clear line, but
9 certainly the intent was to ensure that those expenditures
10 which were only made to -- that were only made to allow
11 the plant to burn orimulsion and provided no other benefit
12 were recouped in the settlement.

13 Q.95 - Okay. Thank you. I may not be exactly right on the
14 number, but the \$47,000,000 that was written off, was that
15 the total amount of the deficit that flowed from NB Power
16 to the government that particular year?

17 A. I would have to check the financial statements, but I
18 believe that amount was -- that write-off was netted off
19 against a small profit in that year. But the amount
20 itself is certainly accumulated in that deficit account.

21 Q.96 - So the government never actually incurred a loss by you
22 writing that off?

23 A. They did, because this write-off would have reduced
24 profit, shall we say, that they might otherwise have
25 incurred. Do you mind if I -- rather than continuing on

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this particular line, it would be very easy for me to check the financial statements at the next break and answer that question directly.

Q.97 - Yes. And while you check it, would you check to see if there were any direct loans from the government made to NB Power to cover that \$47,000,000, and, if so, were there any payment, liens, encumbrances on the corporation for that amount of money?

A. I can answer those questions directly. The cash inflows and outflows of NB Power or the net difference on a daily, weekly, monthly basis is managed through short-term and long-term financing from the Province of New Brunswick. It's not done on an expenditure by expenditure basis. It's done on total cash flow forecast. So certainly that amount of money would have been supported by borrowing from the Province of New Brunswick because it would not have been supported by revenues from rates. And the monies that are loaned from the Province of New Brunswick to NB Power do not have any liens or encumbrances on them.

Q.98 - So you are going to check the exact amount --

A. Yes.

Q.99 - -- that might have come from profit. So in effect the taxpayers of New Brunswick, if this was written off

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2 against profit, did not suffer a direct loss, merely an
3 opportunity loss?

4 A. They -- that amount is sitting in the deficit of NB Power
5 and the deficit was rolled into -- whatever the numbers
6 were was rolled into the purse of the Province of New
7 Brunswick, and therefore the net debt of the Province of
8 New Brunswick.

9 Q.100 - But they didn't have a direct loss? They didn't send
10 you the money that was lost?

11 A. They did in the sense that that -- those expenditures as
12 they incurred on a week by week basis would have formed
13 part of the borrowing of NB Power from the Province of New
14 Brunswick.

15 Q.101 - Okay. So the decision to pay this money to the
16 government instantly as opposed to over the amortization
17 period, who made that decision?

18 A. The decision of the treatment of the settlement was made
19 by the boards of directors of NB Power.

20 Q.102 - So on the one hand the board concluded that the
21 government should get its money in one lump sum, but the
22 rest of the benefit should accrue to the ratepayers over a
23 20-odd year period?

24 A. Let me address that. The write-off was made in 2004 in
25 one lump sum. So the reparation of that write-off is

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2 happening in one lump sum. Whereas ratepayers are paying for
3 the capital costs and related debt charges of Coleson Cove
4 over 23 years annually through amortization and finance
5 charges, they are not paying for it in one lump sum.
6 Therefore the settlement is being returned to ratepayers
7 over the same period of time.

8 Q.103 - But if it was good for the ratepayer to get it over a
9 longer period of time it should be equally good for the
10 government to get it over a longer period of time.

11 A. As I say, it was a one time write-off, therefore it's a
12 one time recovery. However, the charge to ratepayers for
13 Coleson is over a period, therefore this reimbursement is
14 over the same period.

15 Q.104 - We have evidence filed before this hearing you -- NB
16 Power hedges its fuel for an 18 month period.

17 A. Yes.

18 Q.105 - Are there any cancellation or other cost implications
19 for setting those hedges aside in order to consume the oil
20 that is in the discounted settlement?

21 A. We are reviewing that now. My understanding is that the
22 preliminary conclusion -- because we do want to take that
23 plant delivery schedule of the value that will be received
24 through fuels and do our best to fix the value of it
25 through hedges. I understand -- my understanding of

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the preliminary analysis is that the hedges that we have in place for fuel that we will not buy will be able to be transferred and provide the fixed value for these fuel -- under the fuel supply agreement. So no, there will not be any charges associated with unwinding those hedges.

Q.106 - Will any of the discounted fuel be burned at other stations than Coleson Cove?

A. The fuel received in the settlement, part -- some part of it will be burned at Dalhousie as well.

Q.107 - So that benefit for Dalhousie getting the lower priced fuel comes with the GENCO agreement, not the Coleson Cove tolling agreement?

A. No. It will come through the Coleson Cove tolling agreement. Remember, the settlement amount is the settlement amount. The fact that the -- part of it is in kind and the consideration just happens to be fuel, it is the settlement that we are dealing with here. It is the value of the consideration, not the consideration itself that we are dealing with.

And so regardless of where that fuel is burned, it will be dealt with as if it is market price fuel and burned in our system just like any other market price fuel, but the value for the settlement comes from the difference between that market price and what we actually

2 pay for it under this fuel supply agreement. And that value
3 is what will flow through the Coleson tolling agreement.

4 Q.108 - Okay. In the event that some of this fuel is burned
5 for export or third party sale which creates a profit
6 opportunity, how will that profit opportunity flow back to
7 DISCO?

8 A. Well again, regardless of how the fuel was used it will be
9 used and recorded as an expense at market value, because
10 the difference between the market value and the reduced
11 price is the settlement benefit that is going against the
12 Coleson Cove plant and the debt.

13 So once that fuel is at market price it doesn't matter
14 whether it's used for export or for in-province use. It
15 is treated the same as any other fuel, and if there are
16 benefits coming from those exports they flow through the
17 GENCO vesting agreement back to DISCO.

18 Q.109 - Which means under that I believe DISCO gets some
19 percentage of the third party margin, I forget what it is?

20 A. Yes.

21 Q.110 - But they don't get 100 percent of it?

22 A. They are getting -- I believe the vesting agreement
23 specifies, based on the forecast, what the total amount
24 for the year will be, and then any variances from that

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outside of a band DISCO gets 50 percent over the band of the value of it.

Q.111 - Are you familiar with the capital projects economic justification process laid out in the evidence before the Board?

A. Yes.

Q.112 - In that it requires for every capital expenditure or project that you bring forward that a net present risk value analysis be done.

A. Yes.

Q.113 - Was such an analysis done the various options that you considered as to how to pass this to the ratepayer?

A. No.

Q.114 - If you did it what do you think it would say?

A. I'm sorry. I'm not sure that analysis would even be relevant to something like this. The net present value analysis that you are referring to is about making a decision to expend money in one manner or another and looking at the combination of capital and fuel costs as to what represents the least cost option.

Q.115 - If one were to do a net present value analysis of the decision to defer the payment out over 20 years versus paying it in three years as a business case, in a business environment, do you think it would favour the 20 year

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2 option or the three year option?

3 A. I think it would be equivalent in the following regard.

4 We are taking the full value of the settlement and

5 reducing the debt, and therefore saving interest. In

6 other words, we are giving to DISCO the future value. We

7 take the present value of the statement and by virtue of

8 eliminating interest DISCO gets the future value. If the

9 opposite calculation is done for a net present value, you

10 take the future value and you discount it back for

11 interest. But I believe a question was asked earlier why

12 is it that 29.2 times 23 years is more than 330,000,000?

13 Well that's because DISCO is getting the interest benefit

14 over that period of time, so that the future value with

15 interest is equivalent to what the value would be if cash

16 was passed today.

17 Q.116 - Could you do those analyses to demonstrate that?

18 A. Certainly.

19 Q.117 - Would you?

20 MR. MORRISON: I fail to see the relevance, Mr. Chairman, to

21 start doing analyses for practical purposes. The record

22 won't close today, for one thing.

23 CHAIRMAN: I would question how long would it take to do

24 that analysis. I think you already have some homework

25 over the lunch break, if we ever get there. I think you

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2 were to review the financial statements and review some
3 documents that Dr. Sollows is going to use, but this
4 analysis you are talking about, is that something that
5 would be available for the benefit of today's hearing,
6 because if it's something we can do in future, quite
7 frankly, I don't know that it would be of any benefit in
8 the context of today's hearing.

9 A. Could I suggest that perhaps the analysis gets at are the
10 numbers right as opposed to is the deferral mechanism
11 appropriate, and perhaps it can be dealt with through an
12 IR and considered in the hearing when the numbers are
13 examined.

14 MR. BAIRD: I would accept that. I have very few questions
15 left, Mr. Chairman. Will the fuel discounted by the
16 settlement be supplied from Venezuela or is it a financial
17 treatment against oil that you are buying anyway?

18 A. No. It's a physical contract.

19 Q.118 - It's a fiscal contract.

20 A. Physical, yes. It will be delivered from Venezuela.

21 Q.119 - Are there additional operating costs involved in
22 burning Venezuelan crude versus Texas sweet or Arabian
23 crudes?

24 A. To the extent that there are -- I'm sorry. I don't know
25 the -- I know the answer to the question in the sense

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2 that I have heard these discussions on an ongoing operating
3 basis, but I would have thought that the North American
4 actually would have caused more problems. So I can't
5 answer the question. I don't know.

6 Q.120 - I will proceed on the basis that I would believe that
7 it would cost more --

8 A. Okay.

9 Q.121 - -- and if that is true would those costs be passed
10 through the O&M process to the ratepayer?

11 A. The vesting contract in GENCO, the formula for the vesting
12 energy does not on a dollar for dollar pass through those
13 variable costs. So it would not be directly passed
14 through. But there is an indirect pass in the sense that
15 there is a dollar per megawatt hour charge and if heat
16 rates are different or if other operational concerns are
17 such that we don't get the same amount of energy, then
18 obviously that dollar per megawatt hour charge is
19 different.

20 Q.122 - And is that the same in the tolling agreement as in
21 the GENCO vesting agreement?

22 A. The tolling agreement for Coleson is only for the capacity
23 of the plant. And the amounts are specified in the
24 agreement. So again unless there was something particular
25 under one of the clauses that allows for

2 change, and I don't believe incremental operating costs is one
3 of them, then no, it would not pass through.

4 Q.123 - Okay. During the period from start-up of Coleson Cove
5 from refurbishment to the settlement date was fuel
6 consumed at Coleson Cove?

7 A. Yes.

8 Q.124 - Should that amount of fuel that was consumed against
9 the current ratepayers be credited to the current
10 ratepayers as opposed to all of it going out as capital
11 deferment?

12 A. Perhaps I could ask you to re-ask your two questions,
13 because I didn't understand.

14 Q.125 - What I am trying to focus on is that there was fuel
15 consumed at Coleson Cove from the date of start-up from
16 the refurbishment to the date of settlement. That was
17 paid for by the current ratepayers. All the settlement
18 and disbursement that you are giving is going out into
19 these ratepayers and future ratepayers. Why was it not
20 considered to give some of that for the fuel that they
21 paid the extra for from start-up to now back to those
22 ratepayers?

23 A. Fuel is -- if I may, fuel is not the issue, but you are
24 correct in saying that those ratepayers have incurred
25 higher capital costs during that period of time until the

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2 settlement was reached, and no, consideration was not given to
3 that because there isn't a mechanism I know of to enable
4 that to happen.

5 MR. BAIRD: I think that's all I have at this point, Mr.
6 Chairman.

7 CHAIRMAN: Thank you, Mr. Baird. Mr. Wolfe, do you have
8 many questions? I am just wondering when we might break?

9 MR. WOLFE: I would be probably less than five minutes.

10 CHAIRMAN: Then let's we will have your questions now then.

11 CROSS-EXAMINATION BY MR. WOLFE:

12 Q.126 - My first question is when the deferral account is in
13 place how do you intend to report, who do you report to,
14 how will we know?

15 A. It will be reported in our financial statements --

16 Q.127 - Which are --

17 A. -- which are published annually and are subject to review
18 by the standing committee on Crown corporations, and it
19 would be subject to any review procedure or mechanism
20 ordered by this Board.

21 Q.128 - You do not see reporting it to this Board on an annual
22 basis or something?

23 A. If it is ordered by the Board, and that's not atypical for
24 a deferral account, that's not uncommon, then yes, we
25 certainly would do that.

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2 Q.129 - One problem with your financial statements is they are
3 very, very late in coming. So it's a year-and-a-half
4 before we know what really happens.

5 A. Okay.

6 Q.130 - Back to what Mr. Baird was asking. As I understand it
7 NB Power buys their required fuel well ahead of time,
8 seven months ahead of time?

9 A. We don't purchase it, but we do through forward contracts
10 fix the prices well ahead of time, yes.

11 Q.131 - So now we are in August, all of a sudden we have got a
12 very large volume coming at you in the next two years?

13 A. Yes.

14 Q.132 - If Coleson Cove needs to burn more than they would
15 have normally and they saw this on the export market,
16 there is all that money, income or less income, depending
17 how they sell it, is there any mechanism going to be in
18 place that that money will flow through to DISCO, not just
19 some portion of it, because it's all part of this deal?

20 A. Unless the PPAs change there is a formula in the PPA for
21 how export benefits flow through to DISCO, and it's not
22 contemplated that that would change.

23 Q.133 - I realize that, but could it be changed for this one
24 part?

25 A. I think it would be very difficult to change it for

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2 this one part, because once fuel is in the fuel stream it's
3 very difficult to determine which fuel droplets are
4 flowing to which place. But I do -- that does not suggest
5 that the export benefit and how it flows through to DISCO
6 in total is not something that could be changed.

7 Q.134 - The ratepayers in the last couple of years I would
8 gather have been paying the \$6 million legal fees?

9 A. That's correct.

10 Q.135 - Is there any thought to paying that back to the
11 ratepayers on top of the deferral account?

12 A. That amount is not being recovered through the settlement.
13 Are you -- theoretically what is being received here is
14 338 million less the cost it took to receive it, and those
15 costs have already been expended and accounted for.

16 Q.136 - Like refund to the ratepayers of \$6 million?

17 A. Well I'm sorry, there is nothing to refund, because we
18 didn't recover those legal costs in the settlement.

19 Q.137 - But you can use part of your 300-some-odd million to
20 do that?

21 A. That could have been done, yes.

22 Q.138 - Schedule A says that the write-off is \$47 million?

23 A. Yes.

24 Q.139 - Your annual report says \$44 million?

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2 A. Yes. An estimate was made at the end of March 31st, '04,
3 of what the value of the asset would be after dismantle
4 There was an allowance made given that steel had been
5 ordered, there was an allowance made for salvage value of
6 the steel, there was an allowance or accruals made for
7 certain outstanding bills they were estimated, and at the
8 end of the day by the time we concluded bringing the fight
9 back to a greenfield we did not receive as much value as
10 we anticipated for the salvage. Some of the accruals were
11 higher than we had estimated. So there was an additional
12 2.2 million dollar write-off in the following fiscal year.

13 And because the amount was small it was included in OM&A
14 in the following fiscal year.

15 Q.140 - So it doesn't show up here as a write-off then?

16 A. That's right.

17 Q.141 - My last question, 23 years seems like a long time.

18 You talked to Mr. Lawson about a mortgage and going for a
19 world cruise instead, but when I have a mortgage I always
20 want to pay a lump sum once a year and get rid of it. Was
21 there any consideration to having the deferral time much
22 lower than 23 years and accelerating the write-off?

23 Essentially the equipment at Coleson is not needed, so it
24 could be written off quicker.

25 A. There is two sides to the equation. The value or

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consideration under the settlement is being applied against
the debt as quickly as possible. Okay.

Q.142 - Yes.

A. But then the debt that is left outstanding has a mortgage
on it. We have for purposes of intergenerational equity,
spread the mortgage over the life of the physical asset,
so that all ratepayers who are getting the benefit of that
asset pay for it over the same period of time. I would
love to finance our assets over 10 years and charge
customers for it over 10 years, because then we would be
much more fiscally sound, but that doesn't meet the
definition of generation -- intergenerational equity,
because the later customers would get a free ride. So
let's start with the context that we are paying the cash
down against the debt but because the term of the debt is
the same as the life of the plant, that's where the
interest savings accrue. It's in the annual amount we pay
each year on the interest for that. And the same with the
amortization. We are charging the amortization of the
plant over its useful life, so that all ratepayers pay the
same amount as that plant produces electricity over time.
We could theoretically amortize it over a shorter period
of time but then we would still have a revenue stream for
electricity being produced in the later years with no

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costs. It would violate the matching principal.

MR. WOLFE: Sounds good to me. Thank you.

CHAIRMAN: Thank you, Mr. Wolfe. I think that we will break now and reconvene at 1:30. Ms. MacFarlane, is that enough time for you to review the documents? So we will reconvene at 1:30.

(Recess - 12:30 p.m. - 1:30 p.m.)

CHAIRMAN: Okay. Dr. Sollows, are you ready to proceed?

MR. SOLLOWS: Yes. Thank you, Mr. Chair.

CROSS-EXAMINATION BY DR. SOLLOWS:

Q.143 - Good afternoon, Ms. MacFarlane. Good to see you again.

A. Yes.

MR. SOLLOWS: Mr. Chairman, I would like to start by asking your indulgence to enter two exhibits, one being the direct evidence of Ms. MacFarlane in the -- it is dated October 17th 2005 and carries the notation "Board Reference 2005-002" being a description of the accounting changes that NB Power made in the period from -- between the 1990 Generic Hearing on Accounting and Financial Policies to Fiscal Year Ending March 31st 2004", that being one document.

The second document being an excerpt from the 1994-95 Annual Report labeled "Management's Discussion &

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Analysis", pages 18 through -- I think it went to 22 -- 22.

Copies have been provided to the Board Secretary earlier.

And it has been circulated to participants.

CHAIRMAN: Mr. Morrison, do you have any objection to having those entered as exhibits at this time?

MR. MORRISON: My mike is not working. But the answer is no.

CHAIRMAN: Have you distributed copies of those documents?

MR. SOLLOWS: They were distributed to participants earlier, before lunch. And copies are being distributed by the Board Secretary now.

MR. MORRISON: My mike is working. We have no objection.

CHAIRMAN: Thank you. The first document then that has been distributed is the "Direct Evidence of Ms. Sharon MacFarlane", October 17th 2005. And it appears to be a six-page document. That will be KS-1.

The second document that is being distributed is "Management's Discussion & Analysis of Financial Conditions and Results of Operations." It appears to be a five-page document. And that will become KS-2.

Ready to proceed?

MR. SOLLOWS: Thank you, Mr. Chair.

Q.144 - Ms. MacFarlane, I would like to first direct your attention to KS-1 which is the evidence package, your

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direct evidence in the previous hearing. It addresses in Question 4 on page 2 the disposition of the deferral accounts that NB Power had in the past.

And it seems from this pretty clear that NB Power eliminated its generation equalization account and export sales stabilization account in the three years commencing in fiscal year '94-95, is that correct?

A. That's correct.

Q.145 - Can you explain to this Board -- if I recall it was a big issue. But can you perhaps explain to the Board why NB Power did that?

A. It does predate me. So I would be operating on the basis of documents that I have read and information that has been given to me. And it was kind of you to put in evidence KS-2 because that is one of the documents that I have read that explains it.

And in KS-2 -- do you mind if I refer to your document?

Q.146 - Not at all. That is where I was going and you can follow me.

A. Okay. In the first page on Background, the fifth paragraph that begins with "The electric utility industry is going through a period of change", it talks about changes made by the provincial government in 1993 to move

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the utility closer to operating like a private sector corporation.

Changes included measures like having a nonelected Chairman. Prior to that it was always a Minister of government, a broader representation on the board of directors, changes in the regulatory framework, et cetera.

And my understanding is that the board at the time believed that they should also change their accounting policies to be more private sector. Regulatory accounting is something that is put in place for regulatory bodies and includes income-smoothing and rate-smoothing as one of its principles, which are not typically principles that are used by private -- not typically used by private sector companies.

My understanding is that was what the motivation was. And accounts were cleared out over a three-year period. And those amounts were brought into the revenue requirement.

Q.147 - Thank you. Again now in -- you took us to KS-2. If I go to page 20 it has a section labeled "Adjustments to Income/Accounting Policy Changes"?

A. Yes.

Q.148 - Now I'm wondering if I could get you to read into the record the first two paragraphs. We don't need to go into

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2 the bullet points.

3 But just -- I think that sort of summarizes where they
4 were coming from. And I think it would be helpful for
5 this Board to hear it.

6 A. Okay.

7 CHAIRMAN: Just in the interest of time I wonder if it is
8 absolutely necessary to have it read into the record or --

9 MR. SOLLOWS: If it is not then fine.

10 CHAIRMAN: Well, no. But you have made reference to it. I
11 can assure you that the Board will read it, you know. If
12 you insist upon it being read into the record, that is
13 okay. But it seems to me that in the interest of time --

14 MR. SOLLOWS: Okay. I think I can probably proceed to the
15 question.

16 Q.149 - Without going to that, let's go next to page -- I
17 guess it is page 22 which is the "Consolidated Statement
18 of Income"?

19 A. Yes.

20 Q.150 - Am I reading it right when I see that the change in
21 accounting policy that was described turned a \$61 1/2
22 million loss into a \$27 1/2 million -- and I will say
23 profit for lack of a better word -- for the fiscal year
24 ending March 1995?

25 A. That's correct.

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2 Q.151 - Okay.

3 A. And likewise because this would have been anticipated at
4 the beginning of the year when the budget is being set and
5 the Revenue Requirement is being determined and rate
6 decisions are made. It would have meant that the Revenue
7 Requirement would be lower --

8 Q.152 - Right.

9 A. -- by virtue of bringing those credits into the revenue
10 requirement. So rates were lower.

11 Q.153 - And because rates were lower, NB Power could avail
12 itself perhaps of the 3 percent rule and not have to come
13 to that board for a rate increase?

14 A. That's correct. I do want you to know though that our
15 budget is set. Our revenue requirement is set. And then
16 the number is looked at. And if it is above 3 percent the
17 utility goes forward for a rate increase. If it's below 3
18 percent it doesn't. And that is by virtue of legislation.

19 Q.154 - I understand. But the decision could have been to
20 move less than that amount into income and therefore go
21 forward with a rate application?

22 A. That could have been the decision, yes.

23 Q.155 - Thank you. Now going back to the two paragraphs that
24 we aren't going to read into the record, I do note in it
25 that the statements are made that the -- a deferral

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2 account it references, particularly to the deferral accounts,
3 the statement is made the "These accounting approaches
4 have proven to be confusing to readers of the
5 Corporation's financial statements." Do you agree with
6 that?

7 A. Well, let me say that as a person coming from the private
8 sector, I certainly found them confusing when I joined the
9 utility. I think I have become a regulated person. And I
10 don't find them confusing anymore.

11 Q.156 - You have fallen from grace have you? So I guess that
12 would be a no?

13 A. If they are properly disclosed and properly managed, I
14 don't think they have to be confusing. And certainly in
15 NB Power's financial statements they were always disclosed
16 below the line, shall we say. They were very transparent.

17 Q.157 - Okay. It also contains a statement that such accounts
18 are uncommon among utilities today. Would you agree with
19 that statement?

20 A. I do not agree with that statement for regulated
21 utilities.

22 Q.158 - Fair enough.

23 A. I do agree with the next statement though, that they are -
24 - and this is one of the reasons why NB Power did not
25 reinstate them until postrestructuring or contemplate

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2 reinstating them until postrestructuring.

3 I do agree that they are not acceptable for a nonregulated
4 company.

5 Q.159 - That was my next question.

6 A. Yes.

7 Q.160 - That is fine. Thank you very much.

8 Now did NB Power seek the approval of the regulator before
9 it eliminated those accounts?

10 A. No, it did not.

11 Q.161 - Do you know why?

12 A. I wasn't there at the time. So I don't know why not. I
13 do believe that since the amounts were withdrawn from the
14 account in a way that went into prospectively the revenue
15 requirement and therefore to that extent were reflected in
16 rates and rate decisions, that the ratepayer certainly got
17 full value out of those accounts.

18 Q.162 - But we don't -- as far as we know, the regulator of
19 the utility at that time had no opportunity to pass
20 judgment as to whether it was approved, the decision?

21 A. That's my understanding.

22 Q.163 - Okay. Thank you.

23 MR. SOLLINGS: Now I would like to enter into evidence two
24 more documents now, them being, Mr. Chairman, an Exposure
25 Draft of the Accounting Standards Board Proposed

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2 Accounting Standards for Rate-Regulated Operations and the
3 Background Information and Basis of Conclusions that
4 accompanies that document.

5 And with DISCO's permission, Mr. Morrison's permission, I
6 would ask that they be marked.

7 MR. MORRISON: No objection.

8 CHAIRMAN: You should distribute those documents then.

9 MR. SOLLOWS: They have been distributed prior to lunch.

10 And the Board Secretary is distributing the Board's copies
11 now.

12 CHAIRMAN: Thank you, Dr. Sollows. Accounting Standards,
13 "Rate-Regulated Operations, March 2007" will become
14 exhibit KS-3.

15 The document entitled "Rate-Regulated Operations,
16 Background Information and Basis for Conclusions" will be
17 marked as exhibit KS-4.

18 DR. SOLLOWS: May I proceed, Mr. Chairman?

19 CHAIRMAN: Yes. Please do.

20 DR. SOLLOWS: Thank you.

21 Q.164 - Ms. MacFarlane, before I proceed to those documents, I
22 realize there was one more point that I wanted to go over
23 on the consolidated statement of income from the '94-95
24 Annual Report?

25 A. Yes.

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2 Q.165 - When I look at that, the transfer out of these
3 accounts was some \$87 million on a revenue from sales of
4 942 million, which is something under 10 percent roughly -
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6 A. Yes.

7 Q.166 - -- in the order of 8 or 9 percent, is that right?

8 A. Yes.

9 Q.167 - And so in terms of transfers to or from these kinds of
10 accounts, is that an unreasonable thing to have done, that
11 it would be that large that we would, on 950 million total
12 sales we are going to transfer 80 million into revenue
13 from those accounts?

14 A. And I think as reasonable -- a comparator too is the size
15 of fuel and purchase power since the generation
16 equalization account was designed to smooth anomalies from
17 hydro in fuel and purchase power.

18 And yes, it is a large amount. I do not know why the
19 three-year period was chosen.

20 Q.168 - But if, for example, we wanted to treat the current
21 amount of money that we are talking about, you have what,
22 sales, revenues of 1.3 billion, 1.4 now? Is that roughly
23 right?

24 A. Yes.

25 Q.169 - So we would be -- we could easily on this precedent

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2 simply put \$100 million into the current year and write down
3 your revenue providers for the province by the same
4 amount. We would be treating it more or less the same
5 way?

6 A. I don't think the analogy is fair. Because this was a
7 longstanding matter around which a decision was made. We
8 are dealing with in the settlement a very, very unusual
9 one-time issue. And the two are not even vaguely
10 comparable.

11 Q.170 - I guess accepting that they are both -- your proposal
12 is to create a deferral account --

13 A. That's correct.

14 Q.171 - -- which could be in the future wound up in this way?

15 A. That would very much depend upon the guidelines that the
16 Board sets for the deferral account.

17 Q.172 - Yes. We will get to that.

18 A. Thank you.

19 Q.173 - So I guess at this stage I would go on to the Exposure
20 Draft that has been marked KS-3 and see if I can find my
21 notes here. Give me one moment.

22 Now it was this -- it is a copy of the Accounting
23 Standards Board Proposed Accounting Standards for Rate-
24 Regulation Operations. And circulated is an Exposure
25 Draft in March of 2007. Are you familiar with it?

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2 A. I read it at the time, yes.

3 Q.174 - Okay. Thank you. It was marked that comments should
4 be received by June 30th 2007. And I checked on the
5 website and found that there were 39 or 40 interested
6 parties that commented upon it including utilities like
7 Emera, Newfoundland Power, Enbridge, Fortis, Hydro One and
8 a host of others, the Nova Scotia Utilities Review Board,
9 a number of people.

10 NB Power didn't appear to be among those making comments
11 on a proposed policy. Can you confirm that NB Power did
12 not file comments on the standard?

13 A. That's correct.

14 Q.175 - I can't infer from that that you don't have an opinion
15 on it though. So I was wondering if you could give NB
16 Power's position on it?

17 A. Yes. And just to explain that situation, I think if you
18 check earlier exposure drafts you will see that it is NB
19 Power's practice to comment on exposure drafts. We have
20 had a change of staff. And with this rate hearing we have
21 been short resources.

22 That said, we have been following this matter very
23 closely, not only as it goes to the deferral account
24 discussions that we are entertaining today, but also
25 because we all know that we are entering into a period of

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2 an 18-month refurbishment for Point Lepreau where the fixed
3 costs of the plant will continue, and it's 95 percent
4 fixed costs, and yet we will have replacement power costs
5 in the order of some 400,000,000.

6 And obviously there needs to be some consideration to a
7 regulatory method such that neither the utility or the
8 ratepayer is harmed by that. So we are contemplating an
9 application for a deferral account for that. And so we
10 have been following this very closely.

11 NB Power's position is the same as the Canadian Electrical
12 Association's position, which is that these methodologies
13 are valid, not only valid, very important to protect the
14 ratepayer and also to protect the financial position of
15 the utility, particularly those that are borrowing in the
16 public capital markets. And that when a decision is made
17 by a regulator it is not outside of normal generally
18 accepted accounting principles.

19 It is in effect the creation of a receivable within -- or
20 a payable, in this instance it's a payable -- within the
21 context of those generally accepted accounting principles.

22 And regulatory accounting is very valid and should
23 continue.

24 Q.176 - So I would summarize that I think fairly that DISCO
25 does not agree with, and I will quote their words, "to

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proposed elimination from Canadian generally accepted accounting practice of all recognition and measurement of guidance relating specifically to rate-regulated operations."

You don't agree with the Exposure Draft?

A. That's correct.

Q.177 - Right. Thank you. Now referring to section 1100.36 that appears in the Exposure Draft, it is I think from the CICA Handbook. And the reason I will do it in this way is because I have no knowledge of accounting. And I'm entirely reliant on you.

But I'm looking at the bottom of what is labeled page 1, section -- "Generally Accepted Accounting Principles, Section 1100", item .36.

And what they propose to strike says that "Rate regulation exists when all of the following criteria are present."

And it lists three criteria.

If you will allow me to paraphrase it, and correct me if I'm wrong, the three criteria are that rates must be set or subject to the approval of a regulator, that the rates must be designed to recover costs and that the rates must be reasonably expected to result in the required revenue.

Is that a fair characterization?

A. That's correct.

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Q.178 - And so you support leaving -- you support that definition?

A. Yes.

Q.179 - Fine. Thanks. Now the rates that were in effect from last July until this spring were not sufficient to recover costs were they? Do you want me to repeat the question again?

A. No. I understand the question. They were not sufficient to recover rates. I am not prepared though to second-guess the decision of Cabinet --

Q.180 - Nor am I.

A. -- that their view that they were designed to cover rates.

Q.181 - Right. But the bottom line is that the rates that were in effect from last July until this Board approved your interim rates didn't meet criteria (b)?

A. At the end of the day they did not meet criteria -- in retrospect they did not meet criteria (b). As I say, when Cabinet made that decision it was making it prospectively. And it perhaps believed that they could recover rates. As I say, I'm not prepared to second-guess their decision.

Q.182 - But the prior Board -- the Board just two week earlier, on the basis of evidence that you filed, had set

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2 rates that were designed to recover costs that were
3 substantially higher?

4 A. I agree.

5 Q.183 - So it would seem to me hard just to interpret those
6 rates as being designed to recover costs. And then again
7 referring to section 1036, by that definition, DISCO was
8 not a rate-regulated entity?

9 A. I have had this definition and the impact of the 3 percent
10 legislated allowance, shall we say, reviewed by our
11 external auditors to ensure that we fit it. And this is
12 viewed as over the long term. And over the long term
13 rates are designed to recover cost.
14 There are anomalies that happen from time to time for
15 various reasons, like Cabinet overruling Board orders.
16 But over the long term the structure is such that rates
17 are designed to cover costs. That is the view I received
18 from our external auditors.

19 Q.184 - Do you agree with that view?

20 A. Yes, I do.

21 Q.185 - Okay. Thank you. I will leave for argument, one of
22 the comments came from the Auditor General for
23 Saskatchewan. He disagrees.
24 Again under the accounting rules, and you may have dealt
25 with, if in a future year you filed with rates just

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2 sufficient to cover cost, and you projected a 5 percent
3 increase in costs, but decided to take the 3 percent
4 increase say to avoid the time and expense of a rate
5 hearing, in that case you would still consider DISCO a
6 rate-regulated utility, even though you are deliberately
7 setting costs that don't cover rates in the rate-setting
8 year?

9 A. Well, let me say decisions of that nature have not been
10 taken while I have been CFO. So I don't know what the
11 thinking would have been if in fact that was done
12 During the period of time that I have been CFO, we set a
13 budget. We look at what rates are required to recover
14 that budget. Where possible we reduce the budget.
15 If the amount is 3 percent or less, then the legislation
16 says we don't come to the regulator if it's above. We
17 come to the regulator.

18 Q.186 - Fair enough. The reference I was really making was to
19 the '90s when you were not there.

20 A. Right.

21 Q.187 - Yes. Thank you. Now I would like to turn your
22 attention to another aspect of this. And I think you
23 touched on it with one of your earlier comments.
24 Again my recollection of the Nuclearco DISCO PPA is that
25 Nuclearco only gets paid if it delivers energy?

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2 A. That's correct.

3 Q.188 - That is the right interpretation.

4 So again I recall discussions in previous years around the
5 notion of creating deferral accounts and to help cover the
6 expenses during the refurbishment.

7 I think you have confirmed that you have considered that
8 approach?

9 A. Yes.

10 Q.189 - Does this proposed deferral account help in that
11 regard? Does that provide that bridge financing if
12 necessary?

13 A. The one that we are talking about today?

14 Q.190 - Yes.

15 A. No, it does not.

16 Q.191 - Does not. So what happens to the cash?

17 A. Which cash are you referring to, sir?

18 Q.192 - The \$100 million that is flowing in?

19 A. It is being directly applied against our debt.

20 Q.193 - Okay. So in effect your debt is \$100 million lower
21 than it would be going into the refurbishment?

22 A. That's correct.

23 Q.194 - So it does have an impact in that it reduces the
24 amount of debt that is passed on to the Province or the
25 loss that is passed onto the Province, because Nuclearco

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2 is an agent of the Crown?

3 A. You could look at it that way. Or you could look at it as
4 a reduction in debt that has already been incurred.

5 Q.195 - Thank you. So if this Board approves your proposal
6 with the cash portion of the settlement that is not
7 returned to customers in the current year, you have used
8 the rest to buy down debt?

9 A. That's correct.

10 Q.196 - You have made that clear. And if the Board approved a
11 deferral account to bring the cash settlement in income
12 over a shorter period of time, what impact would that have
13 on revenue requirements, if instead of doing it for 23
14 years they did it for three or five or 10?

15 A. It would increase the revenue requirement.

16 Q.197 - Increase the revenue requirement --

17 A. Yes.

18 Q.198 - -- in the current year?

19 A. Yes.

20 Q.199 - How so?

21 A. Perhaps I didn't understand your question properly. But
22 what this deferral account is doing is effectively saying
23 we are going to give customers more in the early years and
24 collect it back in the later years.

25 If the collection period was shorter then obviously

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2 that means we would have to collect more sooner. So the
3 revenue requirement would go up. Perhaps I didn't
4 understand your question.

5 Q.200 - Maybe I'm completely misunderstanding the notion here.

6 I have got \$100 million flowing in this year --

7 A. Yes.

8 Q.201 - -- and another say 250 million over the next three
9 years --

10 A. Yes.

11 Q.202 - -- that are going to flow into an account that we are
12 going to take money out of and apply to income every year
13 for the next 23 years, is that not the case?

14 A. No. i'm sorry.

15 Q.203 - Okay.

16 A. The actual use of the dollars coming from the settlement
17 will impact Coleson Cove and the debt of Coleson Cove.

18 Q.204 - Okay.

19 A. It is the outcome of that use that will flow to DISCO. So
20 the 300' and -- the 300 million shall we say that is going
21 to be applied to reduce the cost of the Coleson Cove plant
22 means that there will be less amortization every year for
23 the next 23 years.

24 Q.205 - Right.

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A. And it is that benefit that flows to DISCO.

Q.206 - And is that that you have levelized over 23 years?

A. We haven't levelized the benefit going to DISCO. What will flow is the benefit that is received. What we have levelized is how that gets distributed to customers.

Q.207 - So it seems to me that if you had adopted a method that returned more of the benefit to customers in this year and say the next year and the year after that, that would have reduced your need for revenue increases that would be recovered through the rates and would therefore have provided you an opportunity to deal with some of the rate design issues to flatten the rate more quickly without having a big rate shock impact on customers in the residential and general service class. Was any consideration given to that?

A. Certainly it was discussed. But if this settlement was taken into income in the period in which it is received, it may negate the need for a rate increase in the near term.

But that doesn't mean that the costs go away. So there would be a significant rate shock at the end of that period to bring rates back up to recover those ongoing costs.

Q.208 - I just don't want to confuse revenue from rates --

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2 A. Yes.

3 Q.209 - -- with rates here.

4 A. Yes.

5 Q.210 - When I refer to rates I'm trying to get to the actual
6 rate design --

7 A. Yes, I know.

8 Q.211 - -- which we all acknowledge that needs to be fixed?

9 A. And we are concerned about a rate shock there. But the
10 rate shock there would be very minor compared to the
11 impact of having no rate increases for three years,
12 because we used this settlement in the short run for a
13 benefit, and then having to bring our rates up
14 dramatically to then cover ongoing costs.

15 Q.212 - I guess I wasn't trying to suggest that. What I was
16 suggesting is that you limit your requirements for
17 revenue, use this to limit your requirements for revenue
18 out of rates over the next three years, so that you can
19 adjust rates in these three years to bring you closer to
20 your revenue cost targets of one, and to address the
21 outstanding issues of intraclass equity in the rates,
22 without imposing undue burdens on individual customers in
23 the classes.

24 That would still end up without such major, I would think,
25 such a major impact after the three or four or five

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2 years.

3 A. So let me just be clear. The settlement has been directed
4 by our board to be applied to reduce our mortgage in
5 Coleson. And certain benefits flow to DISCO over a period
6 of time.

7 It is the case that, as you will see in the cost
8 allocation and rate design that will be filed with this
9 reduction in it that we have not used this opportunity to
10 adjust the rate design and to adjust the revenue to cost
11 ratios. And that will be subject of debate in the full
12 hearing.

13 Q.213 - Okay.

14 A. But that is based on the amounts flowing to DISCO on the
15 basis that the settlement has all been used to reduce the
16 mortgage.

17 If you are suggesting that some of the settlement could
18 have been used directly to come into revenue and avoid
19 rates, that was not the decision of the board.

20 Q.214 - Fair enough. Thank you.

21 DR. SOLLOWS: Now the last document I think that I have to
22 enter here is from -- Mr. Chairman, it is transcript pages
23 4380, Cross by Mr. Hyslop, through to 4383, Cross by Mr.
24 Hyslop, in which he is cross examining Ms. MacFarlane
25 during the Revenue portion of the last rate hearing.

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Again these have been circulated in advance and given to the Board Secretary. And if Mr. Morrison has no objections I would like to enter those on the record.

CHAIRMAN: Mr. Morrison?

MR. MORRISON: No objection.

DR. SOLLOWS: Thank you.

CHAIRMAN: That excerpt of the cross examination, which appears to be an excerpt from page 4380 through to 4383, will become exhibit KS-5. Go ahead.

DR. SOLLOWS: Thank you, Mr. Chair.

Q.215 - Now Ms. MacFarlane, I am looking at page -- and I have got to find it here again. You were being cross examined as part of a panel with Mr. Kennedy by Mr. Hyslop. And he was interested in, as I understand it, the outcome from the litigation that was under way. Because we very quickly get into Mr. Morrison objecting about the details. And somewhere here it said -- yes. At page 4382 at the top it stated -- it attributes to you, "I think the reason for section 4.3.4" -- of one of the agreements -- "is because if you recall Disco has the right to and has in fact paid for all of the capacity off of Coleson Cove. So because it has paid for all of the capacity, which includes the capital costs, any recovery of capital costs would accrue back to Disco."

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A. Yes.

Q.216 - Any but not all, because of the 47 million that went back to government?

A. That was not a recovery of capital spent on Coleson Cove.

Q.217 - What was it?

A. That was a recovery of monies expended in the attempt to build a fuel delivery system that was never completed and was therefore written off.

Q.218 - But wasn't a fuel delivery system a part of the Coleson Cove Orimulsion project?

A. It was. But it was never capitalized. If you look at this, when it says that DISCO has the right to and has in fact paid for it, I should have said will over time pay for, it does that by virtue of the amortization charges for Coleson and the finance charges for Coleson flowing through the tolling agreement.

Q.219 - Okay.

A. These -- this \$47 million was never capitalized. It was written off. It was never added to the capital cost of Coleson. Therefore there is no amortization and there is no debt charge.

Q.220 - Thank you.

DR. SOLLINGS: At this point I guess I would like to go to

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2 what I think is exhibit A-2, Mr. Chairman. And it is schedule
3 1.1.17 of the vesting agreement between DISCO, Genco and
4 Holdco I guess.

5 Yes. I'm working from my binder from the previous
6 hearing. But I understand it has been entered into
7 evidence.

8 CHAIRMAN: It has. And I don't know that we have that
9 document here.

10 DR. SOLLOWS: Oh, I have --

11 MRS. LEGERE: We only have one copy.

12 CHAIRMAN: I'm told we only have one copy of the document.
13 But do have -- have you made copies?

14 DR. SOLLOWS: I didn't make any copies. Because I
15 understood it was already in evidence.

16 CHAIRMAN: Is it going to be problematic for you to ask a
17 question without us having the document in front of us?

18 DR. SOLLOWS: Well, why don't we give it a shot.

19 CHAIRMAN: I agree.

20 Q.221 - Ms. MacFarlane, you have -- do you have it?

21 A. If you are referring to page 42 of the vesting contract,
22 yes, I do.

23 Q.222 - No. It is schedule 1.1.17, page I. It is labeled
24 "Capacity Payment Definitions." And it starts "In this
25 schedule Coleson Cove price means" -- so much -- "Genco

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price means" -- so much.

A. Yes.

DR. SOLLINGS: Make sure we have it.

Q.223 - So when I look at this, the first table, it lists for each month in the fiscal year ending March 31st, and it has years running, it has a price in dollars per megawatt. That is labeled the "Genco price". What does that mean?

A. That is the -- and this is subject to check -- that is the price that is included in the capacity payment to reimburse Genco for its fixed cost.

Q.224 - Okay. So does that -- is that relevant at all to the fixed costs associated with Coleson Cove?

A. No. Again subject to check. The reimbursement for the fixed costs for Coleson Cove are in the first line.

Q.225 - Okay. So --

A. And I say that subject to check. Because I haven't seen this schedule for some time. And the two numbers may be combined. But I don't think so.

Q.226 - Because when I flip it over I see something called the monthly payment which is a similar table with a number of dollars per megawatt that is substantially less.

Just let's leave it subject to check. I guess what I want to get at here is the fact that I'm looking at these

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2 dollars per month payments. And they don't look to be
3 levelized.

4 A. Okay.

5 Q.227 - They seem to indicate that between the year that just
6 ended in March 2007 and the year March 2008, your capacity
7 costs increased by 19 percent, 19.6 percent?

8 A. Okay.

9 Q.228 - And then they stayed flat for eight or nine years.
10 And then they fall for the remainder?

11 A. Yes. Okay. So let me start with your first point which
12 is that the table on the page II, the numbers are less
13 than the table on page I.

14 Q.229 - Yes.

15 A. At the top of page II it indicates that this schedule
16 begins for fiscal years commencing April 1, 2030. So the
17 first schedule carries on until 2030.

18 Q.230 - I don't think so. Because for each month of the
19 fiscal year ending March 31st it starts 2005, 2006 and
20 goes to 2030.

21 A. Okay. Well, I will figure that out. Your point is they
22 don't appear to be levelized. In fact in a sense they are
23 levelized in the following regard.

24 When these PPA's were put together -- and again I'm going
25 from my understanding, because these were built off

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models prepared by the Province's consultant, CIBC World Markets.

They put together a long-term model. And they gradually increased the payments from DISCO to Genco so as to ease the burden on ratepayers, but over time increase the payments to Genco, so that it eventually recovered its costs and moved toward a commercial return.

So you will see that in the years 2005 up to 2008 there is more or less a 3 or 4 percent jump that happens. And that is bringing the returns or the interest coverage in Genco -- the intent there was to bring it up to a commercial level rate over a four-year period without causing rate shock.

Q.231 - But when I looked at that I saw, between 2005 and '6, there was a 7 1/2 percent increase between 2006 and '7. It was a 7 percent increase. And between 2007 and 2008 it was a 19.6 percent increase?

A. That's correct. And that is the design that the financial advisors put in place to balance those two objectives.

Q.232 - Okay.

A. When you see reductions out in the future -- for example when you get to the year 2017, this is when certain assets retire.

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Q.233 - Right.

A. And therefore there are no longer any amortization or interest costs for those assets. As you know, the PPA is designed such that Heritage asset costs are recovered. And as those Heritage assets drop off the system or are retired, DISCO can then go to the market and buy replacement power or manage their power purchases in whatever manner they wish to.

So when you see these declines out over time, that is what is being reflected, is that certain assets are retiring and there are no longer any capacity payments related to them.

Q.234 - Now looking at these numbers, it would seem to me that the amortization period, if you really do want to sort of levelize things, would be to simply use the eight years at which it is the highest and put your deferral account for that period. And that would sort of knock the peak off and levelize things out over the longer -- the full term of 23 years.

So I guess I'm wondering why you did -- if your interest was in levelizing things and sort of spreading it out, why didn't you knock the peak off? Why did you take it off in each year rather than trying to bring the high years down?

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2 A. Are you referring to this table?

3 Q.235 - Yes.

4 A. Well, for starters I didn't do it.

5 Q.236 - Okay.

6 A. And secondly NB Power didn't do it.

7 Q.237 - No. I'm saying in your proposal for a deferral

8 account --

9 A. Yes.

10 Q.238 - -- it would seem to me that if you made it for eight

11 years, it would match the years where the rate is the

12 highest. It would knock that eight-year or nine-year peak

13 off and overall, over the full term of the agreement,

14 result in a flatter capacity payment profile.

15 A. Again this is subject to check. But I believe that the

16 capacity payment for Coleson, which is embedded in these

17 numbers, is flat. You see the first line, Coleson Cove

18 price.

19 Q.239 - Yes.

20 A. It is flat over the life of Coleson. So if you are seeing

21 increases and decreases, those are resulting because of

22 other plants.

23 Q.240 - Okay.

24 A. Since this settlement is specific to the Coleson Cove

25 plant and reparation to recognize that money was spent on

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2 Coleson, represented in the capacity payment that DISCO pays
3 and customers pay. And since the Coleson price is flat,
4 therefore the settlement is --

5 Q.241 - I see where you are coming from. Because you are
6 tying it to the Coleson Cove plant. Got you.

7 I will see if there was anything else here. One last
8 question I think. And I think you can probably handle
9 this instead of Mr. Todd.

10 When I go to page 3 of Mr. Todd's report, he indicates
11 that the actual capital cost of the refurbishment ended up
12 \$497 million higher than the original cost estimate for
13 refurbishing the plant as an oil-fired facility.

14 Now, I went back to the Coleson Cove evidence before the
15 previous Board and found that the oil-fired option was
16 estimated to cost 157.4 million in 2006 dollars. And when
17 I add his 497 to it I get a final project cost of 654.4
18 million, which is about 105 million lower than the 759.9
19 originally estimated for the Orimulsion conversion.

20 So I just want you to -- if you can explain the
21 discrepancy. I'm just trying to make sense of why the
22 numbers don't add up. Or did you really come in \$100
23 million under your original projections?

24 A. The capitalized cost of the Coleson refurbishment was 665
25 million. Now that does not include the 47 million

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that was expended toward the fuel delivery system, because it was never -- the fuel delivery system was never completed.

And the original project would have contemplated a completed fuel delivery system.

Q.242 - And that would have brought it up to the 760 million roughly?

A. I believe that there were some parts of the project that were less expensive than was in the estimate.

Q.243 - Okay.

A. But by and large it would have been the fuel delivery system that would have been the difference.

Q.244 - In relation to that fuel delivery system, as I -- if I interpret it correctly, its original cost was based on delivery through the monobuoy at Canaport. And certainly the EIA concluded that that is how the fuel delivery system should operate.

The decision -- when the government announced the final decision, certainly was presupposed that that would be used. But it very quickly turned into the construction of a wharf. Was the wharf construction done for the same price as the monobuoy?

A. I'm going by memory now. I do not believe the wharf construction at Canaport would have been as cost-effective as the monobuoy.

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But as tests were done on flowing Orimulsion fuel through the monobuoy, there were technical difficulties that they could not overcome. I believe it had something to do with the viscosity of the product and the inability to heat it properly at the monobuoy.

There were also issues related to docking at the monobuoy.

And it was technical issues such that after the concept was put forward and improved environmentally, it proved not to be technically feasible. So the next best alternative was --

Q.245 - We will probably deal with this in a later hearing.

A. Yes.

Q.246 - Because I do know -- I did participate in the environmental review. And I asked those specific questions about technical feasibility. So we will leave that for later.

One last question. In the period between the cancellation of the project and the decision not to proceed with the fuel supply system and the reorganization of NB Power into the group of companies, were either of the power purchase agreements with either the Grandview Avenue station or the Bayside combined cycle plant, were either of those PPA's open for renegotiation for changes in the payments?

2 MR. MORRISON: I fail to see what this has anything to do
3 with the deferral account, Mr. Chairman.

4 DR. SOLLOWS: You are right. That will be for another day.

5 MR. MORRISON: There will be lots of time to debate other
6 aspects of this rate application.

7 CHAIRMAN: Dr. Sollows has agreed with you.

8 DR. SOLLOWS: I had to push it, Mr. Chairman. Thank you
9 very much, Ms. MacFarlane.

10 A. Thank you.

11 CHAIRMAN: That is all of your questions. Dr. Sollows?

12 DR. SOLLOWS: Yes. Thank you, Mr. Chairman.

13 CHAIRMAN: So I guess as soon as you vacate that front seat,
14 next on the list is Utilities Municipal. So Ms. Newman?

15 MS. NEWMAN: We have no questions. Thank you, Mr. Chair.

16 CHAIRMAN: Thank you. Mr. Peacock?

17 CROSS-EXAMINATION BY MR. PEACOCK:

18 Q.247 - Thank you, Mr. Chair. I hope I'm not paraphrasing you
19 incorrectly, Ms. MacFarlane, but I believe you had said at
20 one point earlier today that New Brunswickers should be
21 very happy about -- when you say that do you refer to this
22 proposed deferral account or just in the settlement?

23 A. It's a personal opinion and it was in reference to the
24 settlement.

25 Q.248 - Okay. Wonderful. I have just a very -- I think about

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five questions in part to help me understand how the proposed 23 year deferral account will be of benefit to the low income consumers our organization represents. Many of them face financial uncertainty over the next 23 months or in many cases in the next 23 weeks. Our organization in brief simply does not easily deal with 23 year time frames. So the set of my questions deals specifically with the benefits of a 23 year deferral account. Has NB Power ever in its history maintained a deferral account for a period of 23 years prior to today's request?

A. I know the generation equalization account and the hydro - the export equalization account were longstanding, Mr. Peacock, but I'm sorry, I don't know how longstanding.

Q.249 - Okay. Okay. I believe the deferral account as proposed is in excess of \$300 million. I forget the exact number but it's a big number at least from our perspective. To your knowledge what has been the usual size of deferral accounts maintained by NB Power? Just I guess to better explain my question, I think the annualized allotment is something like 28 million a year or something to that effect. Is that the largest equalized deferral account that NB Power has ever

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2 proposed, or are there some that are in fact larger?

3 A. I believe the generation equalization and the export
4 equalization accounts were larger amounts than that, but
5 perhaps the more relevant comparison is not prior deferral
6 accounts because they were of courser different purposes.

7 The more relevant comparison I believe is the fact that
8 the plant asset and the related debt are being charged to
9 your clients over 23 years, which is the logic behind
10 having the credit applied to the consumer over 23 years.
11 All the deferral account is doing is recognizing that in
12 year one and year two it is NB Power's desire to give back
13 more to the consumer than it is getting from Coleson
14 because it knows it can get it in the long run over the
15 life of the asset from the customer and be kept whole.
16 That's all the deferral account is doing.

17 Q.250 - Okay. Thank you. In fact you have I think partly
18 responded to my next question, but I will refer to -- the
19 actual cash -- the actual settlement includes about 115
20 million in cash payments of which only a small portion
21 would be delivered to the DISCO ratepayer under the
22 current tolling agreements. The proposed deferral account
23 in contrast offers more immediate relief in the first year
24 to the DISCO ratepayer. Can you state whether or not any
25 of the alternatives discussed by NB Power's board, such as

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treating the fuel settlement, as an example, as actual fuel for future year expenses -- would any of those alternatives have resulted in higher financial benefits to DISCO ratepayers in the next three years?

A. None of the alternatives would have done that that were at all considered feasible, because they would have led to much, much higher charges to customers after that three year period. It's like taking the vacation with your money instead of paying your mortgage. And it would have led to rate shock once the benefits in the three years of that settlement expired. The cost would still carry on for 23 years for the mortgage, the benefits would have been spent in three years and would leave the ratepayer in a very difficult position, and that was not seen to be reasonable.

So yes, a higher amount could have been applied in current years -- or in the next three years, but it was not seen as something that was fiscally sound or of benefit to ratepayers.

Q.251 - Some of this I think we can debate on a future date, but I think that one of my concerns with the deferral account option is that had some of the money be utilized for say more immediate rate relief, then that would give all of us in this room more time to deal with some of the

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2 very serious rate inequities --

3 A. Yes.

4 Q.252 - -- and presumably in future years because the rate

5 design would perhaps be more equitable, then would it not

6 be fair to suggest that even if rate shock were to come

7 four or five years from now if we had say a flat rate,

8 would not the ratepayer be better prepared to deal with

9 it, the low income ratepayer in particular?

10 A. I'm not really in a position to answer that, but I will

11 suggest, Mr. Peacock, that I think we are confusing two

12 issues. I think what you are having difficulty with is

13 not the deferral account, but the decision of the NB Power

14 board to apply the settlement in the way that it did, to

15 apply the settlement to reducing the fixed cost of the

16 plant and the mortgage, and therefore seeing the benefits

17 accrue over the long period of time. All the deferral

18 account is doing is just levelizing how that benefit is

19 given to ratepayers and the suggestion is that it be given

20 to ratepayers on the levelized way such that they get more

21 in the first three years, less in later years, and it

22 evens out over time. I think you are questioning the use

23 of the settlement, not the deferral account. Am I

24 correct?

25 Q.253 - You possibly could be, because my challenge I think is

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that a lot of these terms, say intergenerational equity, those sorts of things, in my mind are useful in a regulatory environment but not necessarily are very applicable to the many hundreds of households that our organization represents. They are having a hard time now. And for them to hear that 23 years from now a ratepayer will be treated fairly, it doesn't really help their situation a great deal. Obviously we are coming from two different points of view, so I guess we will have to leave it at that.

Perhaps I will just have one last question and I'm not sure even if you can answer this last question, but since you introduced the sell the house analogy I would like to return to yesterday's analogy of lotto tickets. Say you just won a \$300 million jackpot, which was offered to you in one lump sum payment, or promised to you in interest bearing equalized payments over a period of 23 years.

Which option would you wish to take?

A. Did the equalized payment provided with interest?

Q.254 - Yes. Yes. Interest bearing.

MR. MORRISON: Mr. Chairman, I don't know whether -- I know how I would answer it, but --

CHAIRMAN: Well, I think he did say this was his last question, so -- perhaps we won't take the answer as the

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2 view of the Applicant. It's a personal view.

3 MR. MORRISON: I think the answer is age-dependent, Mr.

4 Chairman.

5 A. Yes.

6 Q.255 - I may remind the Applicant's counsel that I think I'm

7 the youngest intervenor in the room, so --

8 A. No. I pretty much -- I would think about that hard.

9 Q.256 - Okay. Fair enough. Thank you.

10 CHAIRMAN: Thank you, Mr. Peacock. Mr. Theriault?

11 CROSS-EXAMINATION BY MR. THERIAULT:

12 Q.257 - Good afternoon, Ms. MacFarlane.

13 A. Good afternoon.

14 Q.258 - The advantage of seeing me throughout this process is

15 the end is near. Ms. MacFarlane, if I could I would like

16 to go back to a few questions on the beginning of the rate

17 case if I may, and if I may have the Board's indulgence.

18 Who made the final determination as to the figure that the

19 revenue requirement shortfall was \$113 million?

20 A. Who made the decision?

21 Q.259 - The final determination that that was the revenue?

22 A. It's a process that develops back. It's a process of

23 developing a budget. It goes through several levels of

24 scrutiny at different levels of management. It ultimately

25 goes to the executive, then the CEO and then the Board,

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2 before in fact it is determined that that is the budget and
3 therefore the revenue shortfall.

4 Q.260 - So it would be recommended to the Board by management?

5 A. That's right.

6 Q.261 - Are there minutes from the board of directors' meeting
7 to approve the figure of 113 million as the revenue
8 requirement shortfall?

9 A. Yes.

10 Q.262 - And are there minutes from a board of directors'
11 meeting to approve the increase in rates of 9.6 percent?

12 A. Yes.

13 Q.263 - And are there minutes from a board of directors'
14 meeting to approve the reduction in requested rate
15 increases from 9.6 percent to 7.1 percent?

16 A. Yes.

17 Q.264 - Now, Ms. MacFarlane, let's for a minute talk about the
18 financial statements, specifically NB Power's financial
19 statements. Have the financial statements for 2007 been
20 issued to the board of directors?

21 A. The draft financial statements have been reviewed by the
22 audit committee. They have not -- and certainly
23 management statements have been reviewed by the board, so
24 the board understands what the financial position is. The
25 reason why the financial statements for the year ended

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March 31st, the audited statements, have not gone forward from the audit committee to the board, was that this settlement requires disclosure of the subsequent event, and we are working through that disclosure now with our auditors. It will go to our audit committee August 31st and then subsequently to the Board. The legislative requirement for filing our statements is September 30th.

Q.265 - So do you have any idea when it may be issued to the board of directors?

A. There is a scheduled board meeting on September 27th. The issue may be handled by a special purpose meeting prior to that. But in any event they will be filed with the Minister before September 30th.

Q.266 - Ms. MacFarlane, let's talk about the \$47 million as mentioned in line 4, page 2 of exhibit A.

A. Yes.

Q.267 - Do you agree that \$47 million is a material figure?

A. Yes.

Q.268 - And where did this \$47 million come from?

A. It's a combination of two numbers. It is the write-off that was reflected as a line item on the financial statements for NB Power for the year ended March 31st, 2004. And it is the continuance of that as I spoke about earlier this morning, the clean-up of that in the

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2 following fiscal year amounting I believe to \$2.2 million that
3 because the amount was not material was included in OM&A
4 for the financial statements for the year ended March
5 31st, '05.

6 Q.269 - Thank you. Is the amount -- I may have missed it this
7 morning, but -- and I apologize if I did -- is the amount
8 previously written off?

9 A. Yes.

10 Q.270 - And I believe you said March of 2004?

11 A. 44 of it was -- 44-point-something was in March 2004, and
12 an additional 2-point-something was in March 31st --
13 pardon me -- the year ended March 31st, 2005.

14 Q.271 - What was the accounting entry to write this off?

15 A. It would have been -- as these expenditures were made they
16 would have been recorded in the fixed asset area as work
17 in progress. Our work in progress or our construction in
18 progress accounts are never capitalized and therefore
19 began accumulating or bearing amortization charges until
20 the project is completed. So they would have been
21 accumulated in work in progress, so the accounting entry
22 would have been debit expense for the write-off and credit
23 work in progress.

24 Q.272 - Now do you have an independent auditor's

25 recommendation or confirmation as to the original

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2 write-off and its timing?

3 A. Certainly it was part of the audit of that year and of the
4 subsequent year, yes.

5 Q.273 - And was there a recommendation or confirmation to do
6 it that way?

7 A. It would have been management's decision to do it that way
8 but the auditors would have concurred. They would have
9 audited it and made sure that it was appropriate.

10 Q.274 - But I guess my question is I am wondering was there a
11 recommendation by an auditor to do it that way and time it
12 that way?

13 A. No, there wasn't, but I don't believe we would have had
14 any option. You can't capitalize something that -- for
15 which there is no future revenue stream, and since there
16 was no physical asset there would have been no future
17 revenue streams. So CICA guidelines would not have
18 allowed us to keep it in this asset area. They would have
19 required us to recognize it as an expense.

20 Q.275 - Okay. Do you have again an auditor's recommendation
21 or confirmation as to the reversal of the write-off?

22 A. We have an accounting opinion on the treatment of the
23 settlement, and the fact that the \$47 million recovery
24 against that write-off will flow through NB Power's
25 financial statements in the current fiscal year as a

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2 recovery and then down through to net income and then
3 ultimately flow through to a reduction of our deficit, that is
4 the accounting treatment that they concurred with for the
5 47 million.

6 Q.276 - Well let's talk about how the write-off reversal was
7 accounted for. I'm assuming there would have been a debit
8 to an account called Coleson Cove or the station --

9 A. Excuse me. It isn't a write-off reversal.

10 Q.277 - Okay.

11 A. You can't reverse write-offs. Sorry.

12 Q.278 - What would you call it then?

13 A. It's a recovery against a write-off. This will show up as
14 a miscellaneous income amount in the current year.

15 Q.279 - So would that be a debit to an account called Coleson
16 Cove or the station?

17 A. No.

18 Q.280 - No.

19 A. It will be a debit to cash and it will be a credit to
20 income in the current year.

21 Q.281 - That's what I was getting at.

22 A. Yes.

23 Q.282 - Now would you agree, Ms. MacFarlane, subject to check,
24 that if the \$47 million flows through the current year's
25 income statement it reduces the revenue requirement

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increase from 113 million to 66 million, which in turn reduces the requested rate increase from 9.6 percent to 5.6 percent?

A. No, I would not agree with that, because our revenue requirement is designed to collect from customers ongoing costs that represent part of our cost base. This is a one time recovery. It is a recovery of a previous cost. It is not something that will continue into the future. It's not in recognition of a cost in the current year. So it is not in our opinion appropriate to include it as a reduction of the revenue requirement. If that were to be done again it would violate the rate stability because it would falsely reduce the revenue requirement and the rates when the costs for running the utility have not reduced. Those costs would stay at the same level the next year and would lead to just moving that revenue requirement right back up and an impact on rates. But more importantly if - more importantly is the fact that the ratepayer was never charged this 47 million. The write-off did not go to the ratepayer. It was done at the end of the year. It was never part of the revenue requirement consideration for that year. It flowed through the deficit which rose up to the province and therefore has been borne by the taxpayer. If this were taken off the revenue requirement

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2 it would be a windfall to the ratepayer because they never
3 paid the original cost.

4 Q.283 - Well that's something we will be able to see as the
5 process goes along.

6 A. Yes.

7 Q.284 - Now, Ms. MacFarlane, let's talk about where we are
8 going to ensure that the interests of the ratepayers are
9 protected as this settlement goes out over the next number
10 of years. First of all how does this settlement impact on
11 the economic dispatch order for generation?

12 A. It does not.

13 Q.285 - And why would you say that?

14 A. Because let's remember that the portion of the settlement
15 the consideration that is fuel, that consideration comes
16 into effect because we get market priced value for this
17 heavy fuel oil for a lower price. The difference between
18 the lower price and the market price is the consideration
19 and that is the amount that will be credited against the
20 fixed asset to reduce the amortization, and will be used
21 to pay down the debt.

22 So what that leaves us with is the equivalent of market
23 price fuel. So it will be treated just like every other
24 barrel of fuel that we buy in the market and it will flow
25 into dispatch in that way. So the fact that the

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2 barrel is reduced is because of the settlement, not because of
3 fuel expense.

4 Q.286 - But from a generation perspective will this alter the
5 economic dispatch?

6 A. No, it won't.

7 Q.287 - Okay. Now has this settlement been modelled using
8 PROMOD? I believe you said it was.

9 A. No. I was referring specifically to the expected delivery
10 schedule or the anticipated ability of us to receive and
11 burn this over the period of the fuel supply agreement,
12 and I said that we had used an operational -- we used
13 operational modelling to look at our ability to receive
14 that fuel over that period. It's not done through PROMOD.

15 It was done through a spreadsheet analysis with
16 operational people having knowledge of the plant, of the
17 port system and of the constraints of Coleson Cove. So we
18 did not run it through PROMOD.

19 Q.288 - Okay. And why not?

20 A. We didn't feel that it required that level of
21 sophistication.

22 Q.289 - Well how would you be able to quantify the benefits of
23 the fuel component in the settlement if you did not model
24 it?

25 A. We have a model of what the fuel requirements are for

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Coleson Cove and for Dalhousie. We were able to look at those quantities out of PROMOD and knowing that we have yet to buy those quantities our issue is we are going to displace future purchases by using this product instead. So it wasn't a matter of not understanding that we needed to use it in the plants, it was simply a matter of changing our purchasing program because it will be supplied from this source as opposed to from another source.

Q.290 - Now let's suppose that some of the fuel in this settlement is used to generate electricity for export thus producing windfall profits. To which entity in the NB Power group of companies would those windfall profits flow?

A. I want to start by making sure we are on the same definition of windfall. This fuel will flow into our system at market prices, because the value between market prices and the reduced price in the contract is the settlement which is going against the cost of the fixed asset. So this will flow into our dispatch system at market prices. And the difference between anything we export it at and market price, that margin will flow through the vesting agreement in the normal course. If it fits within the amount of credit in the vesting agreement,

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2 it will flow as part of that through to DISCO. If it is
3 within the band above or below that it will fit with GENCO
4 or DISCO, depending upon the amount. And then again if
5 it's beyond that band it will be shared between GENCO and
6 DISCO. But the issue of windfall, there is no windfall,
7 because this particular fuel is simply a consideration for
8 which value has been recognized elsewhere, and this fuel
9 is market priced.

10 Q.291 - So GENCO could receive a benefit from this?

11 A. GENCO receives no benefit from this undertaking. The
12 entire benefit -- the fuel is simply the type of
13 consideration. That consideration is turned into value
14 and the value is credited to Coleson Cove by reducing the
15 fixed cost of the plant and the mortgage. The fact that
16 that value comes from an in kind consideration called fuel
17 is irrelevant. It could come from an in kind
18 consideration called equipment, it could come from cash.

19 Q.292 - So how can you assure the Board that this will
20 continue to be the situation over the next 23 years?

21 A. That the deferral account will be used as --

22 Q.293 - The benefits will flow to the DISCO ratepayers?

23 A. The accounting for it will be transparent in NB Power's
24 financial statements, as the previous deferral accounts
25 were, and will be subject to discussion with the

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2 standing committee on legislation -- or on Crown corporations,

3 I'm sorry. But too, it may be that the Board will put in

4 place special reporting requirements on the deferral

5 account, that is not uncommon for regulatory bodies to do,

6 and we will comply with whatever orders are there.

7 Q.294 - So you would agree then that all of the costs

8 associated with the Coleson Cove refurbishment project

9 ultimately flow to DISCO's ratepayers?

10 A. That's correct.

11 Q.295 - Just so I am clear, there will be no transfer of

12 benefits from this settlement to GENCO, NB Electric

13 Finance or the government of New Brunswick?

14 A. The 47 million --

15 Q.296 - Aside from the 47 million?

16 A. That's correct.

17 Q.297 - Now, I think some reference was made to it with a

18 question from Mr. Peacock, but did the integrated NB Power

19 have deferral accounts?

20 A. Yes.

21 Q.298 - And what happened to them?

22 A. We discussed that earlier that at a point in time where

23 the NB Power legislation changed and the direction from

24 the owner changed to make it operate more like a

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2 private business, there was a decision taken that deferral
3 accounts were not in line with private sector accounting,
4 and a decision was taken to unwind those accounts over
5 three years and the balances in them were brought into the
6 revenue requirement over that period of time.

7 Q.299 - So were they written off in essence?

8 A. In essence they were written off, except the distinction
9 here is that that was done prospectively. So those
10 amounts over three years would have been considered in
11 setting the revenue requirement for the following year, so
12 they would have been in play in deciding on rate levels.

13 Q.300 - Now did NB Power at the time have the approval of the
14 Public Utilities Board before it wrote those accounts off?

15 A. No, it did not. I believe Dr. Sollows asked that.

16 Q.301 - I'm sorry. I missed that. And what assurance can you
17 offer the Board that history will not repeat itself?

18 A. Well as I say those issues predated me, but generally when
19 there are concerns like that there are certain guidelines
20 put in place so that things like that can't happen again.

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22 Q.302 - Now, I hate to say one final question, but I do
23 believe this is it. Do you know of anything in the
24 settlement agreement that prohibits NB Power group of

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- 622 -

2 companies from selling settlement fuel on the open market?

3 A. I have read the fuel supply agreement, but I have not read
4 it with enough care to know whether that is the case or
5 not.

6 Q.303 - Okay. I guess that would be another reason why it
7 should be disclosed. Thank you. That's all I have.

8 CHAIRMAN: Thank you, Mr. Theriault. Ms. Desmond, anything?

9 MS. DESMOND: No questions, Mr. Chair.

10 CHAIRMAN: Thank you. Mr. Morrison, any redirect?

11 MR. MORRISON: None, Mr. Chairman.

12 CHAIRMAN: Thank you. Perhaps we will take a short break
13 and I assume that Mr. Todd will then be sworn in as the
14 witness?

15 MR. MORRISON: That's my intention.

16 CHAIRMAN: Okay. Thank you. Sorry. I didn't give the
17 Panel members an opportunity to ask questions, so we are
18 not going to adjourn just quite yet. Mr. Barnett?

19 MR. BARNETT: Thank you, Mr. Chairman. I won't be very
20 long. Just two or three short questions.

21 BY MR. BARNETT:

22 Q.304 - First of all, maybe just define for the Board what you
23 mean by intergenerational equity? I have heard it talked
24 about, intergenerational principal. Perhaps you could
25 just explain what is meant by that, Ms. MacFarlane?

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2 A. I will defer to Mr. Todd to explain that with more clarity
3 than I can given that he I hope will be sworn as a
4 regulatory expert.

5 Q.305 - Fair enough. I will defer that to Mr. Todd. The
6 second question I guess relates to the \$47 million, which
7 is in exhibit A. During the course of deciding where that
8 was going to be applied was there consultation with the
9 shareholder during the course of that decisionmaking?

10 A. No, there was not.

11 Q.306 - So you just shoved up to Mr. Mallory's door and said
12 whoopie, I have got \$47 million for you. Very nice.
13 Final question. If the Board were to approve this
14 deferral account and then DISCO wished to make changes to
15 that deferral account, is it your opinion or your view
16 that you would be back to the Board to seek -- in order to
17 change the deferral account? I'm thinking of such things
18 as changing the duration and stuff like that?

19 A. That would be my belief.

20 MR. BARNETT: Thank you. Those are my questions.

21 CHAIRMAN: Any other questions from the Panel? All right.

22 We will take a very short adjournment.

23 (Recess - 3:00 p.m. - 3:15 p.m.)

24 CHAIRMAN: I guess before we resume, just for the benefit of
25 the parties, I just wanted to advise that the cross

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examination and direct examination of the next witness or two happens to be relatively brief. it is our intention to hear argument today.

We do understand the facility is available on Monday if necessary. And of course we will put it over till Monday if it is required.

So I'm certainly not looking to put any pressure whatsoever on the parties in terms of how long their cross examination might be, but simply to inform everybody that it is our intention to work through to see if we can get it done today. If not then we certainly will come back next week. Mr. Keyes?

MR. KEYES: Yes. Thank you, Mr. Chairman. I'm going to call John Todd to the stand.

JOHN TODD, having been duly sworn, testified as follows:

DIRECT EXAMINATION BY MR. KEYES:

Q.1 - Mr. Todd, you know how to work the microphone there?

A. I understand it's a little tricky.

Q.2 - Just don't speak too closely. State your name for the record?

A. John Douglas Todd.

Q.3 - And your address?

A. My business address is 34 King Street East in Toronto.

Q.4 - And what is your occupation, Mr. Todd?

2 A. I'm President of Elenchus Research Associates.

3 Q.5 - And in your role as President what type of work do you
4 do?

5 A. The firm specializes in regulation. For the last 15 years
6 primarily industry regulation. We are very involved in
7 rate hearings and other regulated matters with utilities,
8 intervenors, regulators and so on. We also do work in
9 Telecom and regulation generally.

10 Q.6 - And the Board has a copy of your curriculum vitae marked
11 exhibit A-15. Maybe if we could just refer to that. And
12 give us an idea of first of all your education?

13 A. I originally took a Bachelor of Applied Science,
14 Engineering specializing in Electrical Engineering. I
15 subsequently received an M.B.A. from the University of
16 Toronto. That was many years ago now.

17 Q.7 - Okay. And you mentioned that you got -- it is mentioned
18 on the first page in areas of expertise that you have had
19 experience specialized in government regulation for over
20 25 years.

21 You mention 15 in your work with the consulting company
22 that you are President of. I assume there was work before
23 that as well?

24 A. Yes. My business was set up in 1980. So I have been a
25 consultant in the area of regulation for, you know, 27

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years. I haven't updated my c.v.

Prior to that I worked as a Research Officer at the Ontario Economic Council specializing -- or handling research in the area of regulation. So my regulation expertise really goes back into the university days.

Q.8 - And looking at page 2 of your c.v. through the next number of pages, I will say, it appears that you have many retainers involving the electricity distribution markets, customers, companies, governmental agencies, consumer groups.

Maybe just give us a general overview of that, without going in detail, if we don't have to, through line by line of your resume.

A. In the interests of time I won't read the entire c.v. But just in terms of some recent work that would be relevant is the firm, and with myself as lead have done a number of projects for the Ontario Energy Board in the area of facilitation, of processes, development of cost of regulation, proposals for the Energy Board, items such as that.

This year in Ontario it is the first of three years where all of our local distribution companies, electric local distribution companies are coming in for rate cases. Our firm is handling 18 of 25 coming in this year.

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2 I also have been doing work currently for both Ontario
3 Power Generation and Hydro One in Ontario in the area of
4 facilitation with stakeholder groups.

5 I have done workshops in Vietnam for their regulator, the
6 Electricity Regulatory Authority of Vietnam, training on
7 regulatory methodologies and training on market design.

8 Also recently did some evidence for the Consumer Advocate
9 before the Newfoundland Board. And I have done projects
10 over the past year for energy associations such as the
11 Ontario Energy Association and the Electrical Distributors
12 Association on various topics.

13 Q.9 - And I see from your c.v. you have been involved in the
14 preparation and contribution to numerous papers and
15 research projects as well as giving presentations in the
16 area that you have just described. Would that be an
17 overview?

18 A. That's right. A number of papers and presentations over
19 the years.

20 Q.10 - And how would you describe your expertise in the
21 regulatory matters you have been called on to either
22 testify or work on?

23 I have got regulatory methodology. And if you could
24 explain that for a layman like myself it would be
25 appreciated?

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2 A. My speciality is around how we regulate the treatment of
3 matters within the regulated environment, regulatory
4 issues. We will get to intergenerational equity and
5 things like that, regulatory principles and how those are
6 applied within the regulated context.

7 My background and expertise cuts across industries. I'm
8 not specifically an electricity expert. Although as it
9 happens that was my original training. But I have dealt
10 with regulatory methodology in areas including the
11 securities industry and housing rental market.

12 MR. KEYES: Mr. Chairman, subject o any objections, I would
13 ask that Mr. Todd be declared an expert in regulatory
14 methodology for the purpose of today's hearing.

15 CHAIRMAN: Thank you, Mr. Keyes. Do any of the parties wish
16 to question Mr. Todd or have any objection to him being so
17 qualified?

18 Well, silence I guess is acquiescence. And you will be so
19 qualified then, Mr. Todd, as an expert witness is
20 regulatory methodology.

21 MR. KEYES: Thank you, Mr. Chairman.

22 Q.11 - I'm now going to turn, Mr. Todd to exhibit A-14 which
23 is a report I believe that you authored?

24 A. That's correct.

25 Q.12 - And could you advise the Board when you were retained

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to prepare this report approximately?

A. I was first contacted about two weeks ago in anticipation of settlements being reached and anticipating that there would be some issues in terms of the treatment for DISCO, and was retained immediately upon the settlement being reached early last week to complete evidence within the one-week time frame.

Q.13 - And by all means refer to your report if you have it there in front of you. I think you do.

Could you tell us specifically what you were asked to do?

A. As it says on the first page, line 20, I was asked to provide my expert opinion regarding the appropriateness of the proposed deferral account from a regulatory perspective.

Q.14 - And in providing your opinion can you advise and tell the Board what it was that you had to do in order to give us this opinion?

A. Essentially looking at the treatment, as to whether it was appropriate, from the perspective of regulatory principles and whether there would be an alternative approach which would be more consistent with traditionally accepted regulatory principles.

Q.15 - And what was your conclusion?

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A. My conclusion was that -- which does appear on the last page in bold -- I go through a bit of the background in my conclusion -- the approach is consistent with regulatory principles.

In particular I done it by four there, intergenerational equity, rate stability, maintaining financial integrity and cost of service recovery. The latter two are -- you can ensure those principles are adhered to in almost any way.

The intergenerational equity in the rate stability issues were key in my consideration. Intergenerational equity being, since the question has been asked, being an issue of -- the term comes from myself and my kids. I'm not going to take from my children to enrich myself.

Alternatively I'm not going to take from myself to enrich my children.

Intergenerational equity now in the regulatory context really means looking from one year to the next. Are the ratepayers in different years treated equally?

And where that principle comes into play in my view in this case is that if it had not been sort of but for the Orimulsion contract, a different decision would have been made in 2002. There would have been a refurbishment of Coleson Cove for purposes of making it an upgraded,

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refurbished oil-fired generating station.

Because of the expectation of being able to use Orimulsion, the costs ended up being significantly higher.

There were some additional benefits through the process, primarily in the environmental front. But essentially there is higher costs. Those higher costs compare to the alternative of just refurbishing for being an oil-fired plant. All appear in the capital cost category.

If they had built an oil-fired plant, the cost of fuel would be exactly the same as what it is now. The difference that is being carried through to customers through the tolling agreement is the higher capital costs.

And those higher capital costs are being borne for the 25 years or 23 years left that the plant is in operation.

So the principle, as I apply it in terms of intergenerational equity is saying that it is just consistent to take the benefits of the settlement and apply them in a way that it matches the costs associated with the problem that arose.

Higher capital costs were borne because of the initial decision which is driven by the Orimulsion contract. That failure led to a negotiated settlement which provided benefits. All the ratepayers through all the remaining 23 years will get equal benefit from this settlement. In

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other words they will have their higher costs -- the higher capital costs will be defrayed by an equal amount.

You could, of course, try to stack those benefits early on. You could try to stack those benefits later on. That would not be consistent with the principle of intergenerational equity. Because you would either be, you know, robbing some of the later customers to benefit the earlier ones or the other way around. That is the concept of intergenerational equity in this concept, everybody treated equally in terms of costs and benefits.

The rate stability issue is also important here. One of the effects of levelizing is that it's not going to have an impact on there being a large rate increase a few years down the road because you have deferred the recognition of higher costs through time in rates.

One doesn't know where rates are going to go in future years. But a levelized approached minimizes the risk that you are going to be depressing rates in early years, and then having a big rate increase.

More importantly in this case what it's doing is it's actually bringing some of the benefits that are being realized later by DISCO into the first two years.

Bringing down the rate increases now by building in a flat cost every year so it would have absolutely no rate

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impact.

This particular settlement would have no rate impact in future years. So that minimizes any risk of a problem being created by this settlement because of -- in regard to rate stability.

Q.16 - So in summary you would agree from your report that the establishment of the deferral account as proposed by DISCO is an appropriate way to deal with the benefits of the settlement?

A. Yes. The most consistent approach that I can think of with those regulatory principles.

MR. KEYES: Thank you, Mr. Chairman. Those are all my questions.

CHAIRMAN: Thank you, Mr. Keyes. Mr. Lawson?

MR. LAWSON: Thank you, Mr. Chairman.

CROSS-EXAMINATION BY MR. LAWSON:

Q.17 - I have only a couple of questions. First of all, just out of curiosity, and it may be just a misunderstanding, on page 2 on the bottom, in your footnote -- footnote number 3, there is reference to an amount of \$619 million.

And on page 3, line 5, there is reference to \$497.

And my quick reading suggests it would have been normally the same number but they aren't. So what is the difference?

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A. The 619 refers to at the time the decision was made. The costs that were expected for the two alternatives, the Orimulsion alternative and the oil-fired alternative of refurbishment.

The number on page 3, the 497 refers to the differences between the actual capital cost, not the projected capital cost and the alternative of refurbishing for oil-fired.

Q.18 - So it had been projected at \$619 million and it really came in at only a mere \$497 million?

A. Yes. That was referred to this morning, that the number was lower in fact because all the work didn't have to be done. Part of that was the savings around the facilities to receive Orimulsion.

Q.19 - Right.

A. And the 47 million, as well as what was spent, was left out of the second number, because that was never capitalized.

Q.20 - So it wasn't the same project where they came in way under budget. It was a different project?

A. No. The actual project was the actual project, which ended up with a plant which has higher environmental standards being met than the oil-fired plant would have been, and more flexibility in terms of what it can burn.

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2 Q.21 - And just on page 4 of your report, I guess it is line
3 11, starting on line 11, the paragraph, "The primary
4 alternative to implementing a deferral account would be to
5 include the revenue requirement of DISCO and the actual
6 cash flowing under the tolling agreement."

7 This -- I presume this conclusion, because where you are
8 talking about an alternative, is premised on the
9 allocation of the settlement funds all going to the
10 capital account, is that right?

11 A. Well, you are talking about Coleson Cove, what is
12 happening in Coleson Cove. I mean, in terms of --

13 Q.22 - That is right I am.

14 A. -- DISCO, the only thing that's happening is that there is
15 a reduction in charges under the tolling agreement to them
16 on a year-by-year basis.

17 Q.23 - Right. But if in fact it was dealt with differently by
18 Coleson Cove and not dealt with by attributing the
19 settlement funds to capital monies, but some of it to say
20 capital funds and some of it to savings down to DISCO and
21 fuel costs in the year in which it is incurred for example
22 over the next 18 months or two years, that would be
23 another alternative?

24 A. I don't think that's actually another alternative.
25 Because what you are referring to is changing something in

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2 the way that the nonregulated company acts.

3 Now I think that what you are getting at is if the Board
4 were to want to look through that reality and say we are
5 going to deem this to be -- we are going to recognize all
6 the income within the regulated company DISCO in the first
7 year, regardless of what's happening in the tolling
8 agreement.

9 Q.24 - Or a part of it.

10 A. I'm sorry?

11 Q.25 - Or a part of rather than all, as you said --

12 A. Whatever. If what you are suggesting is that a different
13 recognition be made for the regulated company DISCO -- and
14 if you go to the spreadsheet, attachment number 1, and
15 while there are benefits of 13.5, 24.4 and so on being
16 recognized, but instead you are recognizing say 50 million
17 in the first year, you could create a deferral account
18 that does that.

19 And instead of having an amount to be recovered in the
20 deferral account you would have a surplus in the deferral
21 account, or whatever you are going to do.

22 That is a conceptual alternative that totally violates the
23 regulatory principles that I have laid out.

24 Q.26 - And the principle, this intergenerational equity --

25 A. And rate stability, are the two keys ones that I said.

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2 You could -- you could do that other thing in a way that meets
3 the other regulatory principles, like cost recovery.

4 Q.27 - So just -- I mean, you heard the evidence this morning.

5 I understand -- you were in attendance I believe were
6 you?

7 A. Yes. That's correct.

8 Q.28 - An so you did hear my line of questioning I assume with
9 respect to the concept that some of the \$2.2 billion
10 claimed was in fact for extra costs incurred for fuel
11 because Orimulsion wasn't cheaper, wasn't available? The
12 cheaper fuel wasn't available?

13 A. Well, I think -- I think that's looking at the -- that's
14 looking at the contract in isolation from the projects.
15 The higher costs -- I look at it from the perspective, the
16 customer's perspective, what are the costs, what are the
17 benefits?

18 And in the absence of the Orimulsion alternative the fuel
19 costs would be exactly the same as they are today, the
20 cost of oil. That was the alternative to Orimulsion --

21 Q.29 - Right.

22 A. -- from the get-go.

23 Q.30 - But the settlement, which is what we are dealing with,
24 how is the money going to be dealt with that comes from
25 this settlement?

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2 The settlement was of a claim that included a very
3 substantial portion of being extra fuel costs as a result
4 of replacing Orimulsion with a more expensive fuel. Is
5 that your understanding?

6 A. That's my understanding. But that was only part of the
7 equation in the decision that was made.

8 Q.31 - I recognize that.

9 A. Yes.

10 Q.32 - But it was part of the equation. And you -- just very
11 quickly, it was a \$2.2 billion claim as at least
12 identified in the press that was being made, of which the
13 capital costs are, I'm not quite sure, some \$500 million,
14 \$400 million.

15 I'm not quite sure what number is the correct one. I
16 presume by mathematics the rest of it was probably extra
17 fuel cost. But I don't know.

18 That extra cost is an extra cost that is being occurred by
19 customers today, yesterday and tomorrow, isn't that right,
20 of Coleson Cove, or DISCO customers through Coleson Cove's
21 extra costs?

22 A. Well, first of all, I have been involved in a number of
23 lawsuits, unfortunately not as a litigant but as an
24 expert.

25 I have yet to be involved in a lawsuit where it is

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being claimed by the lawyers up front was not a dream. So I don't take that 2.2 particularly seriously as a meaningful number. And I don't know what's behind it.

What we do know is that there was a settlement. There was a recognition that there was costs. And we do know that the incremental costs borne by Colesonco, which get reflected in the tolling agreement, are the higher capital costs.

Relative to the alternative, which is what I would have based the negotiations on, the alternative is here is what our company and our customers have suffered. We have suffered an increase in capital costs compared to what we would have done if we didn't have this contract with you.

And that difference was higher capital costs.

If you go partway down the road and split the original arrangement in two parts, the original Board decision in two parts, higher capital costs versus lower fuel costs, if you look just at the fuel costs, then yes, you are now paying higher fuel costs than you would have been.

But those higher fuel costs would offset higher capital costs. So I don't see how you can split them.

Q.33 - The higher fuel costs would have offset the capital cost?

A. The reason -- the reason that the decision was made in

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2 2002 to go with the refurbishment, to use Orimulsion, was
3 because that alternative was both environmentally superior
4 and less costly than just refurbishing the plant to run on
5 oil.

6 The reason why it was less expensive overall was that
7 despite the significantly higher capital cost, which is
8 the amount referred to in my footnote, the --

9 Q.34 - 619'?

10 A. -- 619', despite that higher cost there was going to be
11 significantly lower fuel costs over the lifetime of the
12 fuel contract.

13 So the net effect of that was to leave the overall project
14 being less expensive. The decision would not have been
15 made if it weren't for the combination of those two
16 factors, the higher capital costs and the lower fuel cost.
17 At the end of the day, since the contract wasn't
18 fulfilled, you are paying exactly what you would have been
19 for fuel, if the alternative plant had gone ahead, but you
20 would end up incurring a lot more capital costs.

21 Q.35 - How much more today are the customers paying for
22 Coleson Cove power than they would have been paying under
23 the deal if the Orimulsion project had proceeded,
24 considering both capital cost component amortized and the
25 extra fuel savings?

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A. That's exactly what my prime consideration was. And that's -- the 497 million is the additional capital cost that is being recovered, both through amortization and interest, in the tolling agreement over the 25 years, 23 years left.

So I haven't done the calculation. But it would be the amortization and interest associated with that. Now --

Q.36 - Have you factored in the fuel cost savings that might have in fact been greater than the capital cost recovery?

A. In the alternative scenario you would have had an oil-fired plant. And there would be no fuel cost savings. Because you would be paying for oil just as you are paying right now for oil to fire that plant. So there is no difference in the oil cost under the two scenarios.

Q.37 - I'm not going to pretend to play this game. I'm sorry. Okay. Thank you.

CHAIRMAN: Thank you, Mr. Lawson. Mr. Baird?

MR. BAIRD: Just one question, Mr. Chairman.

CROSS-EXAMINATION BY MR. BAIRD:

Q.38 - Mr. Todd, you talked -- one of the analogies for justifying the treatment of the rate over the long period of time was that -- and I may have misunderstood you -- is that you shouldn't take from your children's wealth to

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2 enhance your own, and your children shouldn't take from yours
3 to enhance theirs. Was that a correct assumption on my
4 part?

5 A. That's correct. What you are doing is giving equal
6 treatment to customers in all 25 years over which the
7 Coleson Cove facility will be in operation.

8 Q.39 - I don't think there is a parent in the room would agree
9 that they haven't had to enhance their child's wealth?

10 A. I would agree with that. But personally I do not apply
11 the regulatory principle of intergenerational equity in my
12 personal life. I violate it every time I pay out some
13 allowance.

14 Q.40 - So it was just an analogy, not a --

15 A. Yes. Fortunately I once attempted to use regulatory
16 principles in our household. And I failed miserably. So
17 since then I don't do it.

18 CHAIRMAN: Anything further, Mr. Baird?

19 MR. BAIRD: No. That is it.

20 CHAIRMAN: Thank you. Mr. Wolfe?

21 MR. WOLFE: No questions, Mr. Chairman.

22 CHAIRMAN: Thank you. Dr. Sollows?

23 DR. SOLLOWS: Thank you, Mr. Chairman.

24 CROSS-EXAMINATION BY DR. SOLLOWS:

25 Q.41 - Mr. Todd, two questions I think, I hope. You have

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referred repeatedly to the alternative to the Orimulsion conversion as being the Coleson Cove conversion to continue to burn oil and put in environmental controls. When I go back to the evidence that was filed before the Board that made the recommendation to proceed with the project, the ranking was number one for the Coleson Cove Orimulsion conversion.

The second-ranked project was a Coleson Cove combined cycle new unit. And it was ranked based on levelized life cycle annual cost.

So I'm wondering how you can premise your decision on the notion that the alternative to the conversion was a project that really was ranked number 4.

It was ranked well below the second rank which would have been -- without Orimulsion availability they would have, according to the information they filed, constructed a Coleson Cove -- a combined cycle plant, a new unit at Coleson Cove.

A. I was advised that if the refurbishment had not taken place, that the oil-fired alternative would have been alternative.

Q.42 - So you have not reviewed the evidence that it had originally filed before the Board?

A. In the couple days I had, I reviewed -- complete

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2 sections of the evidence and in particular the summary of
3 option parameters, which included data but did not have
4 the ranking.

5 Q.43 - So if you now knew that, in the case of the Orimulsion
6 conversion and the levelized fixed costs were 1.51 cents
7 per kilowatt-hour and the second ranked alternative was
8 1.73 cents per kilowatt-hour --

9 A. Sorry. Can you repeat those numbers?

10 Q.44 - 1.51 cents per kilowatt-hour for the Orimulsion
11 conversion levelized fixed and levelized a variable 2.85
12 cents per kilowatt-hour.

13 And the second ranked alternative was the combined cycle
14 unit at 1.73 cents per kilowatt-hour fixed cost and 3.45
15 cents per kilowatt-hour total cost.

16 A. And what was oil?

17 Q.45 - The oil was .73 levelized fixed cost and 4.62 cents per
18 kilowatt-hour levelized variable, for a total of 5.35
19 versus 5.18 for the natural gas combined cycle.

20 So I guess my question is how would your conclusions be
21 different based on that comparison? And why -- what you
22 say are the same, why would they be the same? And if they
23 are different why would they be different?

24 A. Well, first of all, where it came from, the key -- the
25 only thing I was worried about was the capital cost

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higher than the value of the settlement that's flowing through
to DISCO?

My concern was that if there was a windfall here, i.e. if
the settlement exceeded the incremental cost of going the
Orimulsion route and ending up with an oil-fired plant,
that a portion of the settlement could be treated as a
windfall and you wouldn't have a rationale for saying we
have got to counterbalance the higher cost with the higher
benefit. And therefore whatever was a windfall would --
could be disposed of in any way.

Regular principles wouldn't apply to that. At least
intergenerational equity wouldn't apply to that. The
margin is sufficient that we are not in a windfall
situation. You are recovering a portion of the
incremental costs.

And that is true. I mean, all of these scenarios are
close enough that there is not a significant difference.

What you have ended up with is an oil-fired plant which is
largely similar to the oil-fired alternative, which is
what I was looking at, but at a much higher cost.

As we have seen, the estimate for the oil generation
blended HFO with NOX controls was shown as 158, which is
the figure I have used. And what you have ended up with
is something which is environmentally superior to that, as

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2 I understand it.

3 Q.46 - Yes.

4 A. But essentially that plant with better emission controls
5 built in. And in addition some more flexibility in terms
6 of what could be burned in the future.

7 Q.47 - So in your view, the fact that the second alternative
8 was not the oil, enhanced oil, blended oil option, but was
9 instead the combined cycle unit, it makes no difference
10 from the -- to your recommendation --

11 A. No.

12 Q.48 - -- or your advice?

13 A. What we ended up with was the oil-fired conversion, not a
14 gas-fired conversion.

15 Q.49 - That is true. But had we known that we had not -- we
16 are not going to get Orimulsion, we would have done the
17 natural gas-fired conversion?

18 A. That may be the case.

19 Q.50 - And the question that I want to be sure is clear on the
20 record is would that influence any of the recommendations
21 as to how to handle this, the fact that the actual
22 alternative was not a Orimulsion or fuel, it was
23 Orimulsion or combined cycle natural gas with slightly
24 higher fixed costs and slightly higher variable cost?

25 A. The actual cost of 665' minus, from the chart I have,

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2 shows the gas-fired with 393'. So the difference is --

3 Q.51 - Which chart are you looking at?

4 A. This is -- sorry. In the evidence filed in November 1,

5 2001 --

6 Q.52 - Yes.

7 A. -- of comparing the alternatives.

8 Q.53 - The one that I was looking at was labeled, Table 3,

9 "Three power cost comparisons, the levelized costs."

10 A. Okay. The table I'm looking at is from the save evidence

11 I expect, Table 3-1, Summary of Option Parameters.

12 Q.54 - Okay.

13 A. Which shows a capacity capital cost expected life --

14 MR. KEYES: Mr. Chairman, just before you go on, the

15 evidence he is referring to is evidence that was in a

16 previous Board hearing I assume. I don't know what --

17 DR. SOLLOWS: That is correct.

18 MR. KEYES: I don't know what Mr. Sollows is referring to.

19 CHAIRMAN: I'm having some difficulty hearing you. I don't

20 know if our technician can get my microphone working.

21 Q.55 - What I'm trying to establish is whether Mr. Todd --

22 he has repeatedly has said that his advice was based on

23 the fact that the alternative to the Orimulsion conversion

24 was the oil-fired choice. And that is not back at the

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2 decision point what the alternative was.

3 So if you are going to make the comparison it should be
4 clearly to what the alternative choice would have been if
5 you did not have Orimulsion fuel available. And that was
6 the second ranked, number two.

7 Now you are looking at Table 1, you are looking purely in
8 terms of capital cost, right, capital cost dollars per
9 kilowatt? Table 3-1, is that the one you are looking at?

10 A. Capital cost dollars per kilowatt, yes.

11 Q.56 - Yes.

12 A. Yes.

13 Q.57 - I think you really have to look at the levelized costs
14 over the plant, which is where the rankings are made.

15 If you go down to page -- table 3-3 on page -- it is page
16 56 is where we find the rankings?

17 A. Okay. I don't -- I don't have that table.

18 Q.58 - All right.

19 A. I brought the table that I was using. So the issue is --
20 I'm not trying to revisit the decision. And if the
21 decision were looked at today with current knowledge of
22 prices, we would have a very different decision.

23 The point I was trying to make was what we have ended up
24 with is an oil-fired plant. That was an alternative.

25 Q.59 - Yes.

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2 A. The oil-fired plant was one of the options considered in
3 the original hearing.

4 Q.60 - It was not the option that would have been selected if
5 -- I guess really it's just a matter of semantics here.
6 But I certainly got the impression from your words -- and
7 I would have to wait to read the transcript -- that your
8 decision was premised on the fact that had they not done
9 the Orimulsion conversion they would have done the oil,
10 the blended oil operation. And that doesn't seem to be
11 consistent with the historical evidence.

12 A. Okay. Your question was if natural gas was second choice
13 would that change what I have to say?

14 Q.61 - Right.

15 A. Okay.

16 Q.62 - So why?

17 A. So that question. What we have ended up with is the
18 oil-fired alternative, whether it was second, third or
19 fourth.

20 Q.63 - Right.

21 A. Based on the original cost estimates, that alternative
22 would have cost 158 million capital cost.

23 Q.64 - Yes.

24 A. Fuel cost for that alternative and what we have today is
25 no different. It's oil. So it would be the same

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2 reality.

3 Q.65 - Right.

4 A. The plant that was built cost 497 million more than the
5 estimate at the time of the hearing.

6 Q.66 - Right.

7 A. 497 million is much more than the settlement benefit
8 that's flowing through to customers.

9 Q.67 - Okay.

10 A. Therefore, it is appropriate for the benefit to be used to
11 offset the capital cost.

12 Q.68 - That is irrespective of whether a second choice was --

13 A. Absolutely.

14 Q.69 - -- by that time. That's what I wanted to make sure was
15 clear.

16 A. Yes.

17 Q.70 - Thank you very much. The second question is, I see
18 your summary decision here. "The proposed approach is
19 consistent with the regulatory principles of
20 intergenerational equity and rate stability."

21 What is the point of stabilizing a rate that we know is
22 wrong, that is not recovering the cost of service to
23 customers? Why would we want to stabilize that?

24 A. Are you referring to the rate that was the result of
25 government intervention?

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2 Q.71 - No. I'm referring to the declining block rate that
3 general service and residential customers pay. I'm
4 referring to rate not revenue.

5 MR. MORRISON: Mr. Chairman, with all due respect to
6 Dr. Sollows -- and I know that he has a soft spot in his heart
7 for rate design issues -- I think we are going to -- the
8 evidence that is going to be filed -- there is rate design
9 evidence going to be filed.

10 I'm sure there will be lots of questions on rate design as
11 we go through the hearings in the fall. And I'm not sure
12 if it has any direct bearing on the establishment of the
13 deferral account.

14 But if Dr. Sollows can demonstrate that it does then I'm
15 happy to withdraw my objection.

16 CHAIRMAN: Mr. Morrison, I think that I would agree with
17 your comments.

18 Dr. Sollows, perhaps you could indicate how this is
19 relevant to today's proceedings. I understand the
20 relevancy of your questions with respect to the overall
21 hearing.

22 But with respect to the issue that we are dealing with
23 today, perhaps you could clarify as to what the relevancy
24 is?

25 DR. SOLLOWS: Well, I guess I was looking at this. And it

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2 says that part of the decision is based on that it does
3 provide rate stability.

4 And I guess I just don't really understand the value of
5 that in the context of this particular company at this
6 particular time.

7 Had this company been subject to ongoing regulation and
8 had its revenue cost ratios close to 1 and had all of its
9 rates designed to recover costs and fairly apportionate,
10 then I think the notion of rate stability is very weighty.

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12 But absent those conditions I'm wondering why we should
13 give it much consideration.

14 CHAIRMAN: Well, perhaps if you would pose it as a question
15 to the witness then we can move forward?

16 DR. SOLLOWS: Okay.

17 A. I think I understand the question. First of all, there
18 are two, in a sense, aspects to concepts of rate stability
19 that I think you are combining in that question. One is
20 the level of rate increase in average rates from one year
21 to the next, the rate increase that the company is talking
22 about in its motion.

23 The other concept of rate stability is there is stability
24 in the rates of individual classes of customers, when you
25 are adjusting to get their revenue to cost ratios

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2 closer to 1, and the impact on any of your customers when you
3 change the rate design.

4 So individual customers, individual classes can have rates
5 that are not stable, even though the rate increase on
6 average may be stable.

7 The only thing being affected by the proposed deferral
8 account is the overall cost and therefore the overall
9 level of rate increase from one year to the next. It's
10 not dealing with instability caused by rate design issues.

11 The approach being taken will have a benefit in terms of
12 rate stability, in terms of increases in rates from one
13 year to the next on average.

14 Q.72 - That is fine. Thank you.

15 One last question. Do you know if these required
16 intergenerational equity rate stability?

17 Put it this way. If instead of consulting you after the
18 decision had been made to do this, if DISCO had -- or NB
19 Power group of companies had approached you well in
20 advance of making the decision, what are the options that
21 you might have proposed?

22 A. There is two levels to that question. I was approached
23 with respect to DISCO, with respect to DISCO's treatment
24 of a decision that had been made, DISCO's decision with
25 respect to the treatment of the costs

2 flowing through to it.

3 Under the tolling agreement it had not been decided. And
4 in fact we discussed that. And I gave them my advice.
5 And my advice was exactly what they had done and exactly
6 what I would recommend.

7 If what you are saying should be done in terms of the
8 broader scope, which is actually -- you are talking about
9 unregulated companies and treatment there. Again the
10 principles underlying on my evidence is a matching of the
11 costs and the benefits.

12 Therefore, I would come to exactly the same result where I
13 say the costs that are ultimately flowing through to
14 customers is an increase in capital-related costs which
15 flow through to customers on a levelized basis over the
16 full term of the operation of the plant in 25 years.

17 And therefore the benefit should flow back to them in a
18 way that gives equal treatment to customers in all years
19 and defrays some of that higher cost in each of those 25
20 years.

21 Two years have already passed us by. You can't go back
22 and compensate those customers. That would be retroactive
23 ratemaking. That would be making retroactive payments.

24 So instead we have squeezed that 25 years of benefit

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2 into 23 remaining years and spread it equally across those, so
3 that all future customers will benefit equally from those
4 benefits.

5 DR. SOLLOWS: Thank you. I have no further questions.

6 CHAIRMAN: Thank you, Dr. Sollows. Ms. Newman?

7 MS. NEWMAN: No questions. Thank you.

8 CHAIRMAN: Mr. Peacock?

9 MR. PEACOCK: One very, very brief question. It draws from
10 part of Dr. Sollows' questioning.

11 CROSS-EXAMINATION BY MR. PEACOCK:

12 Q.73 - The concept of intergenerational equity, can it be
13 fairly applied if say within two decades you have vastly
14 different rate design? Say in the original generation you
15 have a rate design that includes, for example, a declining
16 block rate. And 20 years out you have an inclining block
17 rate. Can the concept of intergenerational equity still
18 hold under that scenario?

19 A. The precondition for intergenerational equity is that the
20 other principles of regulation hold in the sense of full
21 cost recovery.

22 If -- and I'm sure this will be the case, with the Board
23 as a regulator, subject to the occasional government
24 intervention I understand.

25 But if in each and every year the company is

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recovering its costs within that year and it's meeting the cost of service standard, then if there is an incremental cost, such as we are talking about in this case, which is being visited upon customers through all those 25 years, and that is an extra cost on top of what would have been the otherwise full cost of service, then the intergenerational equity applies that everybody should receive an equal share of that benefit.

If you were to -- certainly it would be very attractive to low income people to -- and if you look at my c.v. you will see I have had many poverty groups as clients over the years.

It would be very attractive for them to receive, you know, all of the benefit now. But to do that it would mean that you would be saying that today's low income people, as a portion of the total customer base, deserve help.

And therefore what we will do is we will take the 25 years of benefits and squeeze it into the early years, and help all customers, high income or low income, by squeezing all the benefit into the early years. And as a result they are better off. But we have taken the benefit away from other customers in the latter part of the 25 years.

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I can see that that would be attractive to your client group. But it would violate the principle of intergenerational equity. And it does apply because we have got cost of service being covered in every year.

MR. PEACOCK: That is all, Mr. Chair.

CHAIRMAN: Thank you, Mr. Peacock. Mr. Theriault?

MR. THERIAULT: Yes. Just a few questions, Mr. Chairman.

CROSS-EXAMINATION BY MR. THERIAULT:

Q.74 - Mr. Todd, would you consider your report a statement of opinion on the reasonableness of establishing a deferral account?

A. It's a statement of the reasonableness of establishing this deferral account, yes.

Q.75 - In this situation?

A. Given the circumstances. I mean, every deferral account is established for a reason. And each one is in some sense unique.

Q.76 - Were you given any access to any of the so-called background documents, specifically the settlement agreement?

A. Not the settlement agreement complete. I don't think it was complete when I was first contacted in fact. What I had was the summary, the same information that the chartered accountant for the Board had to review.

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2 Actually I think he may have had more than I did.

3 But it was the summary information which explained what

4 was in the settlement agreement, which he has verified as

5 being correct.

6 Q.77 - Did you do any of your own mathematical analysis for

7 your report?

8 A. I was not retained to check the numbers. That was being

9 done by the staff's consultant. I was retained to look at

10 the principles of the approach.

11 Q.78 - Now were you able to confirm any of the figures you

12 quote in the body of your report or in the footnotes?

13 A. No. That's not -- those are numbers that are from the

14 record or given to me just in terms of some basic facts so

15 that I could make my determination on principle. But I

16 cannot speak to those numbers.

17 Q.79 - So Mr. Todd, we could conclude that you are offering an

18 opinion on an approach to a deal with the settlement

19 without offering any opinion on the veracity of the

20 figures given to you or contained in your report?

21 A. Yes. I was looking at the principle of the deferral

22 account, not at the numbers.

23 MR. THERIAULT: Thank you very much.

24 CHAIRMAN: Thank you, Mr. Theriault. Ms. Desmond?

25 MS. DESMOND: No questions, Mr. Chair.

2 CHAIRMAN: Mr. Keyes, any redirect?

3 MR. KEYES: No. Thank you.

4 CHAIRMAN: Any questions from the Board? Thank you, Mr.
5 Todd.

6 Mr. Morrison, I take it that that is all of the witnesses
7 that you wish to call in this proceeding?

8 MR. MORRISON: That is correct, Mr. Chairman.

9 CHAIRMAN: Thank you. We have one other expert's report
10 that has been filed, which is Mr. Logan's report, NBEUB-1.

11 Ms. Desmond, what is your intention with respect to that
12 document?

13 MS. DESMOND: Mr. Chair, we are prepared to have Mr. Logan
14 speak to his report if any of the Intervenors or the
15 Applicant wish to question Mr. Logan on his document.

16 CHAIRMAN: I might suggest that perhaps Mr. Logan come
17 forward and be sworn, and at least perhaps by way of
18 direct examination swear to the truth of the contents in
19 his report.

20 ANDREW LOGAN, having been duly sworn, testified as follows:

21 DIRECT EXAMINATION BY MS. DESMOND:

22 Q.1 - Sir, could you provide your name for the record?

23 A. My name is Andrew Paul Logan.

24 Q.2 - And Mr. Logan, could you give the Board please a summary
25 of your education and qualifications?

2 A. Received an undergraduate degree in business from the
3 University of New Brunswick. I articulated with the
4 chartered accounting firm of Deloitte & Touche, receiving
5 my CA designation in 1989.
6 Spent several years in public practice. A couple of years
7 with a private firm. And then rejoined public practice in
8 the late '90s. And currently I'm a partner with Teed
9 Saunders Doyle & Co. here in Saint John.

10 Q.3 - And you are a qualified chartered accountant, sir?

11 A. That's correct.

12 Q.4 - Okay. And do you have an expertise or an area of
13 concentration with respect to your practice?

14 A. Not necessarily. Our firm is a general practice. If
15 there is a focus for my particular practice it would be in
16 the area of auditing and review engagements for various
17 non-profit and profit organizations.

18 MS. DESMOND: Mr. Chair, the Board would like to offer
19 Mr. Logan as an expert and qualifying him as a chartered
20 accountant with an expertise in the area of auditing.

21 CHAIRMAN: Any objection from any of the parties? Okay. He
22 will be so qualified.

23 Q.5 - Now Mr. Logan, you prepared a report at the request of
24 Board Staff?

25 A. That's correct.

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2 Q.6 - And can you confirm that that report and the contents
3 therein are accurate?

4 A. Yes, they are.

5 Q.7 - And that is dated August 16th 2007?

6 A. That's correct.

7 Q.8 - And Mr. Logan, as a result of our hearing yesterday you
8 were asked to review a number of source documents. And
9 prior to reviewing those documents what if any agreements
10 did you sign?

11 A. I signed a confidentiality agreement earlier that week
12 with DISCO.

13 Q.9 - And just generally could you speak to what your
14 understanding was of your mandate on this project?

15 A. Yes. I was asked by the Board to review and verify the
16 mechanical accuracy and supporting documents that went
17 into the calculation of the regulatory default account
18 that's being proposed by DISCO.

19 Q.10 - Mr. Logan, perhaps I could take you to page 1 of your
20 report. And if you could just walk through the scope of
21 the assignment and what exactly you did do in reviewing
22 those numbers?

23 A. Certainly. As noted beginning at line 27 of my report on
24 page 1, I reviewed the settlement agreement that was
25 signed and executed by the parties involved to ensure that

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the underlying amounts that form the basis for the settlement calculations were in fact input correctly into the model.

I also recalculated and verified the inputs for the regulatory default calculation that's shown in exhibit A-13.

On page 2 beginning at the top I performed a recalculation of the various savings from the settlement that would flow through to DISCO, including the interest cost reduction and the amortization expense reduction, which would be found in Table A of exhibit A-13.

I verified the receipt of the cash settlement to external banking records and the conversion amount to Canadian dollars, did a recalculation on the in kind estimated fuel cost savings model.

I also reviewed the inputs and the substance used in that model including the methodology used to determine the fuel delivery schedule, verification of the conversion factors, verification of prices that were forecasted and also verification of foreign exchange rate used to convert the savings into Canadian dollars.

Q.11 - Mr. Logan, as a result of that review -- and perhaps you could walk through what if any results you came to in your conclusion with respect to that review?

A. Certainly. Again on page 2 beginning on section --

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line 19, all of the amounts that were in the settlement agreement were found to be correctly applied in the model as inputs in determining the savings. I was able to verify the cash settlement and corroborate the amounts. The in kind fuel cost saving settlements were also correctly applied in terms of the contracted quantities of fuel and the negotiated settlement price calculation methodologies. All of the calculations that I checked were found to be without error.

In my review of the fuel cost savings model, all inputs were reviewed for reasonableness, the supporting documentation. The calculations were verified.

In my notes on page 3 you will note that I had a comment regarding the price forecast that was used to determine the ultimate savings. An annual average was used in the model over the expected fuel delivery period.

And there was quarterly price information available in the supporting documentation that I observed. And given that the fuel delivery schedule is not equally distributed over the period, I felt that the quarterly prices would provide a more accurate estimate if you will. In all other cases there were no issues.

Q.12 - Could I clarify just for the Board, on page 2 under item (f), you do reference a review of the inputs and

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assumptions. But are you able to express an opinion as to the reasonableness of any of those assumptions or forecasts?

A. No, certainly not. In terms of fuel delivery schedules and things of those natures, no. My review was entirely to ensure that the supporting documentation agreed to the model and that the inputs were correctly input.

MS. DESMOND: Thank you, Mr. Logan. No further questions.

CHAIRMAN: Thank you, Ms. Desmond. Mr. Morrison, do you have any questions?

MR. MORRISON: No questions, Mr. Chairman.

CHAIRMAN: Thank you. Mr. Lawson, any questions?

CROSS-EXAMINATION BY MR. LAWSON:

Q.13 - You do mention on page 2 of your report under item (f) a review of the inputs and assumptions. And you reference in Roman Numerals III and IV a verification of forecasted prices and verification of foreign exchange rates.

What did you do to verify those things?

A. In the information that I reviewed there were various price forecasts that were developed by DISCO from various sources, some external, some internal.

I ensured that the numbers that were in those supporting documents agreed to the model used to establish

2 the fuel cost savings estimate.

3 Q.14 - So you didn't actually look to see whether or not the
4 information they provided was reasonable or there might
5 have been other sources to use?

6 A. No, I did not.

7 Q.15 - And just on the one exception that you referenced,
8 using the annual versus quarterly prices forecasts, I know
9 that you do indicate time didn't permit you to do an
10 analysis of the result.

11 But do you have a sense of -- can you express an opinion
12 as to the materiality if any of that difference?

13 A. I would be uncomfortable doing that, since I haven't had
14 time to verify my calculations.

15 MR. LAWSON: Thank you.

16 CHAIRMAN: Thank you, Mr. Lawson. Mr. Baird?

17 MR. BAIRD: No questions, Mr. Chairman.

18 CHAIRMAN: Thank you. Mr. Wolfe?

19 MR. WOLFE: No questions, Mr. Chairman.

20 CHAIRMAN: Thank you. Dr. Sollows?

21 DR. SOLLOWS: No questions, Mr. Chairman.

22 CHAIRMAN: Ms. Newman?

23 MS. NEWMAN: No questions, Mr. Chair.

24 CHAIRMAN: Mr. Peacock?

25 MR. PEACOCK: No questions.

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CHAIRMAN: Mr. Theriault?

MR. THERIAULT: None, Mr. Chairman.

CHAIRMAN: Panel? Any redirect? Okay. Thank you.

I take it that there is no other witnesses today, other evidence to be filed, is that correct? Then I guess the next phase would be for us to move to argument. And we are little bit later in the day than we had anticipated. It's I guess quarter to 4:00 now.

Perhaps I will just canvass the parties as to whether or not they feel it's possible to move to argument today.

It's -- I don't think that we really want to go much beyond 5:00. And quite frankly we haven't checked with our translators or our court reporter or others as to whether or not that's possible.

But Mr. Morrison, I will start with you. What would your preference be?

MR. MORRISON: Well certainly my preference, Mr. Chairman, to wrap up today if at all possible. I can't speak for the other parties, of course, but I suspect my final argument will be less than 10 minutes.

CHAIRMAN: Well, I will just canvass the other parties then.

Mr. Lawson?

MR. LAWSON: I to would like to see us proceed today.

And I would be certainly less than 10 minutes.

2 CHAIRMAN: Mr. Baird?

3 MR. BAIRD: I have no summary and comments to make, Mr.
4 Chairman.

5 CHAIRMAN: Mr. Wolfe?

6 MR. WOLFE: I will be very short also.

7 CHAIRMAN: Dr. Sollows?

8 DR. SOLLOWS: I will try to be short, no problems going
9 today.

10 CHAIRMAN: Ms. Newman.

11 MS. NEWMAN: We will be very brief. Less than five
12 minutes, Mr. Chair.

13 CHAIRMAN: Mr. Peacock?

14 MR. PEACOCK: About five minutes.

15 CHAIRMAN: And Mr. Theriault?

16 MR. THERIAULT: Five minutes or less.

17 CHAIRMAN: All right. By my calculations, except for Dr.
18 Sollows, who wouldn't give us an estimate, we should be
19 able to do this within half an hour or so.

20 Are you prepared to start now or do you want a short
21 break?

22 MR. MORRISON: No, I am prepared to proceed, Mr. Chairman.

23 And I am going to try to beat my estimate.

24 Quite simply the focus of today's hearing, as everybody
25 knows is the establishment the deferral account.

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2 And DISCO is before this Board seeking the approval of this
3 deferral account and for one reason and one reason only.
4 And that's to enable DISCO to pass the benefits of the
5 PDVSA settlement to customers as soon as possible by
6 facilitating an immediate reduction in the interim rate.
7 That's why we are here.

8 However, as set out in my notice of motion and
9 subsequently explained by my letter of August 15th, for
10 the reasons that I set out in that letter, it is
11 impossible to reduce the interim rate until the Board has
12 issued a final order approving the deferral account. And
13 I think it is also important to note as proposed by DISCO.

14 And I will get to that in a little bit -- in a moment.
15 There is a fundamental issue which the Board must
16 understand before we can move forward with any
17 consideration of the deferral account. And that is -- and
18 I know it was raised earlier about I guess where you draw
19 the line with respect to the settlement of the lawsuit.
20 The decision to have the benefits of the lawsuit flow
21 through reductions in the tolling agreement. I would say
22 that is one side of the line. And then there is the
23 treatment by DISCO. How DISCO deals with that reality.
24 And that brings us to the deferral account.
25 It's my submission that the Board can only deal with

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the benefits that flow to DISCO under the settlement structure. What flows to DISCO is a reduction in the fixed charges under the tolling agreement over the life of the tolling agreement. That in my submission is all the Board can and should consider.

In the July 16th decision, the generation cost decision I guess it's for more of a better term, the Board stated it would expect DISCO to explain why its costs under the PPAs are reasonable. But the Board went on to say that the Board stated that it does not regulate the New Brunswick Power Generation Corporation. So I think a distinction has to be -- you have to look at it from DISCO's perspective.

The structure is a reduction in the fixed costs under the tolling agreement. What we are dealing with here is how does DISCO deal with that reality and hence the discussion of the deferral accounts. As I said what flows to DISCO is a reduction in those fixed charges.

Now there have been some suggestions here today -- some intervenors have raised it to suggest that all benefits or a large portion of the benefits be taken into account immediately or over some shorter period of time than what DISCO has proposed.

In my submission that does not reflected the reality

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that you can only deal with the costs that DISCO gets and that again is a reduction in the fixed costs flowing to DISCO under the tolling agreement. And I would also like to point out that Mr. Todd has just said, if my comments aren't enough, that the approach of escalating that transfer you violate the regulatory principles that he outlined.

Now, I would like to talk a little bit about what tests you should use. Just as an interim rate was established on a prima facie basis, it's my submission that the establishment of the deferral account and the variance in the interim rate can and should be done on a prima facie basis. And as I explained in my opening comments this morning that allows the Board to move on with the decision on the deferral account today and leave all of the other questions and issues, and all of them valid, but which require a little bit more consideration than time allows us to give them in this hearing. Those issues can all be dealt with and fully explored during the full hearing of the application in November.

So I am suggesting that the appropriate approach for the Board to take is has DISCO established a prima facie case for the establishment of the deferral account, which if approved as DISCO proposes will then result in your

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ability to reduce the interim rate by what we have proposed.

And we recognize that the intervenors have only just received the information that was filed in confidence yesterday. And by proceeding on the basis that I am suggesting to the Board, it would allow the intervenors to research this information, to study it and to have more meaningful questions when the Board convenes for the full hearing in November. And it can test the actual number that actually goes into the deferral account at the end of the day.

As I just said, I submit that the appropriate evidentiary basis for varying the interim rate and approving the deferral account is a prima facie case. The question is has the prima facie case been met? Ms. MacFarlane has explained the structure of the settlement. The Board's independent consultant has verified the values of the benefits, which DISCO has calculated and has said that they are indeed accurate.

The expert witness, John Todd, has provided his expert opinion that a deferral account, which levelizes the settlement benefits over the term of the tolling agreement, is the most appropriate mechanism in a regulatory perspective. It has in his expert opinion, the

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deferral account proposed by DISCO is consistent with the regulatory principles of matching the benefits of the settlement to the costs which the settlement addresses. And he goes on to say that the proposal was also consistent with the regulatory principles of intergenerational equity and to a lesser or secondary extent, rate stability. Some intervenors have suggested, and again I may be repeating myself, but when you escalate this in some fashion, and again I refer you to Mr. Todd's evidence, where he said that's inappropriate from a regulatory point of view. And again -- and I will make this more clear before I finish in a moment or two. The Board can only deal with the reality that DISCO -- of the costs that DISCO gets or the benefits that DISCO gets under this settlement structure. And that is the reduction in the fixed costs flowing to DISCO under the tolling agreement. And that is important, again harkening back to the reasons that I set out in my letter of August 15th, why the establishment of the deferral account as proposed by DISCO is a pre-condition to the reduction in the interim rate. If, for example, this Board were to second guess the settlement structure and say you know that \$47 million that really should have gone to pay off debt or instead of

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\$29.1 million coming in the first year, that really should be a different or a higher number or some should be allocated to fuel. If the Board looks at that then -- and then at the same time you reduce the interim rate by 2.5 percent DISCO cannot recover that reduction.

So when I say that I request the reduction in the interim rate is conditional on the establishment of the deferral account, it is the establishment of the deferral account specifically as proposed by DISCO.

And it is also very important -- actually it is essential that the establishment of the deferral account be a final order. In other words, if you choose the mechanism in November and DISCO has foregone by a reduction in the interim rate, there is going to be an under recovery of revenue and that's a risk, as I said on my letter of August 15th that DISCO is not prepared to take. And indeed as a regulator, I wouldn't expect that you would wish DISCO take such a gamble.

So, Mr. Chairman and Members of the Board, I submit that a prima facie case has been established. And it is in order for you to issue an order that the deferral account, as specifically proposed by DISCO be approved upon establishment of the deferral account as proposed by DISCO that the interim rate be reduced by 2.5 percent.

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2 In the event that the Board does not approve the deferral
3 account as specifically proposed by DISCO including that
4 the settlement structure is a reduction in the fixed
5 charges under the tolling agreement over the term of the
6 tolling agreement, then I would ask that the Board make no
7 reduction in the interim rate. Thank you.

8 CHAIRMAN: Thank you, Mr. Morrison. With respect to your I
9 guess point that the Board should make this a final order
10 for -- and I guess this kind of jumps out at you, it's
11 establishment of the deferral account, as opposed to a
12 deferral account. By a final order are you referring to
13 the final order with respect to the form of the deferral
14 account, that is a 23 year model, but that subject to
15 verification through the process, interrogatories and the
16 full hearing that the actual inputs might be subject to
17 change, but that it's the model itself that you --

18 MR. MORRISON: Absolutely. It's the model itself. The
19 structure of the deferral account. It's just that you
20 can't expect DISCO to absorb a 2.5 percent reduction in an
21 interim rate, which is based on a deferral account that
22 may change at sometime in the future. So it's -- we know
23 that the numbers that -- the amounts that go in the
24 deferral account are subject to the scrutiny of the Board
25 and all the intervenors as we go through the process, as

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is the revenue requirement in general. And I am sure there will be all kinds of questions on what does the revenue requirement is 83.1? Whether the fuel futures forecasted were used to -- for the estimates for the deferral account are appropriate? All those questions are legitimate questions. And at the end of the day, the Board will approve the number that will be in the deferral account. But the establishment of the deferral account has to be a pre-condition for a reduction in the interim rate.

CHAIRMAN: And I have one other question for you. If in fact the Board did not approve the establishment of the deferral account, how would the settlement monies be treated in the test year? What would be the -- what would the effect be? I appreciate you have asked it that if we don't approve the deferral account, we make no order. But sort of in the long run, if you will, what would the impact be?

MR. MORRISON: I had some discussions with my client about this, Mr Chairman. And I suspect that we would have to come back to the Board with some alternative -- to have the Board order something other than what it is. An alternative that I would suspect would be is that the benefits of the settlement as they flow through

2 unlevelized, if you will, would be taken into the revenue
3 requirement as they come in.

4 CHAIRMAN: Sure.

5 MR. MORRISON: And I don't know, I think the ultimate
6 reduction in the interim rate would be in the order of 1.1
7 or --

8 CHAIRMAN: That is my recollection of Ms. MacFarlane's
9 evidence. And is that really -- is that your position
10 then that that would be essentially what would happen if
11 there was no deferral account or --

12 MR. MORRISON: It's the only way that DISCO could avoid the
13 risk of under recovery. And it's the only way that the
14 benefits could be passed through. So it would result in a
15 significantly smaller reduction in the interim rate in the
16 test year.

17 CHAIRMAN: Thank you, Mr. Morrison. Any questions from the
18 Members of the Panel? Thank you. Mr. Lawson?

19 MR. LAWSON: Thank you, Mr. Chairman. I guess I would first
20 start by saying that I find it a bit uncomfortable to be
21 looking at us having had a span of less than two weeks, us
22 -- including the Board, to deal with a matter that really
23 we are being asked to deal with that is going to have in
24 impact for 23 years to the ratepayers after having had
25 what I will say a very short time for preparation or

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reflection on the issue.

More importantly, we haven't had an opportunity, time didn't permit it. We are all in a hurry. And would all agree we would like to have a rate increase or rate decrease take effect as soon as possible. But they get sort of another opinion, for example, like Mr. Todd's to be able to help the Board come up with another view if there is another view. I feel very uncomfortable with that. But that being said, this is the time that we have to do it. But we do -- the Board has to consider when they are doing this that they are at least being asked by DISCO to bind this Board from a regulatory point of view, for all intents and purposes, for a 23 year period. And I think that's pretty significant.

As I say, the concept itself of the deferral account, sort of a levelizing, which is a word I didn't know existed until a few days ago, the levelizing of these things -- of the benefit is not unacceptable to CME. But the first question becomes is how much do you levelize? Do you levelize all of it? And secondly, over what period of time do you levelize it? As to how much, for example, we heard evidence, as I understood it at least, that with respect to the \$47 million that none of the benefit of that part of the settlement will flow to DISCO. We have

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heard why? At least 2-point some odd million of that it appears as though has in fact been expensed by -- and paid for by DISCO customers, as I understood it. The part that was put into the following year, which appeared in OM&A, I assuming would have been a rate -- included in the rate amounts for the subsequent year.

We also -- and I may not have understood this correctly as well, but I believe that there was reference to the \$6 million, and I think that was the amount in legal fees incurred in recovering this has also been expensed. And I would again assume -- and I am only assuming here that that in fact also would have been incurred and paid for as part of the rate by DISCO customers. So it seems to me at least those amounts should paid back on an immediate basis to the customers and it shouldn't be spread over a 23 year period.

And then I move to the next part, which is obviously the much bigger question of this -- there was a claim for \$2.2 million -- billion dollars, small slip of the tongue -- \$2.2 billion. And the vast majority of that was for extra costs incurred as a result of not having Orimulsion.

So there was a capital cost recovery component of the claim, plus the extra fuel costs. So I would submit that

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2 at least some part of the settlement amount should be in
3 recognition of the fact that the customers today and
4 tomorrow in the near future should have more accelerated
5 than 23 years, some part of that settlement for in the
6 next few years rather than waiting the 23 years, because
7 it's all been attributed by NB Power to capital costs.
8 DISCO basically has had imposed upon it by Holdco the fact
9 that it is all going to be attributed to capital cost. I
10 mean we submit that that's something, like it or not in
11 the regulatory environment, Holdco has to recognize that
12 when they make these kinds of decisions, that you as a
13 regulatory group may think that's not the appropriate way
14 to do it. You have to look and see is that's a reasonable
15 way for Holdco to allocate those costs, and if not, I
16 submit you have the jurisdiction to decide what is a
17 reasonable way of doing it.

18 So the deferral account concept, no problem. How long a
19 period of time should that be? I submit that really
20 depends on how much is allocated. The Board decided that
21 a significant component of this should be recovered in
22 terms of fuel costs over the next few years and reduced
23 costs to the customers of the day for the next three years
24 transfer some of that savings in fuel costs down to DISCO
25 in operating costs and therefore reduce their rates. Then

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all of it could be attributed and spread over 23 years.

Perhaps the more appropriate way is to take some small part of that capital amount or the amount allocate it to operating costs and give the recovery immediately. Put the balance of it into a -- into the deferral account, but don't spread it over the full 23 years. Spread it over some shorter period. I submit not -- perhaps depending on how much it is, maybe 10 years or something of that nature. I know some would prefer it much sooner. I am sure I have some clients who would prefer to have it all given the day after tomorrow. Whether that's reasonable is another issue. But the reality is is that it should be a shorter period of time. Part of the fuel price contract expires in about 17 or -- was to expire in 17 or 18 years.

If the Board does decide though that it should put in a deferral account of some sort, I guess a couple of comments. One is that the -- we would submit that the Board should in fact require because DISCO is not regulated, its rates are, but it itself isn't regulated, that they should attach condition for reporting to this Board on an annualized basis, the adjustments that take place in the deferral account and make that available for the public to be able to comment on so that there is sort of an accountability on the accounting of the deferral

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account.

Secondly, and I alluded to this in argument this morning in cross-examination this morning, and that is the question of who should bear the risk of something going wrong, because we have all known deals that looked like a good idea at time, but they don't always come to fruition as planned. And what happens if something goes wrong?

I submit that Holdco has decided that they will made the decision as to what the settlement is. They will impose how the settlement is going to be dealt with, which is by allocating it all to capital costs. And I submit that they should bear the risk of anything going wrong with that and it should not in turn be passed down through to DISCO. So that if is in fact something goes wrong with this, and heaven forbid that it should happen, but if the petroleum company decides it's not going to honour this agreement, then DISCO would receive little or no potential benefit on the fuel savings component. We would submit that that should be born not by the ratepayers, not by DISCO, but by Holdco.

Those are all the comments I have. Thank you.

CHAIRMAN: Thank you, Mr. Lawson. If I can perhaps just attempt to summarize your position. You are in agreement with the approval of the establishment of a deferral

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account, just not the deferral account that's been proposed.

Is that your summary?

MR. LAWSON: I don't think it's unreasonable that some form of a deferral account would be established. As to how much goes into the deferral account and the duration of it are the issues that we would have.

CHAIRMAN: And you did speak somewhat at length about the duration and you did -- I guess you threw the number 10 years about, but I wasn't sure that was sort of cast in stone. Is that your proposal or do you think it should be just something shorter than the 23 years that's been proposed by DISCO?

MR. LAWSON: I, without even having even discussed it with my client, it seems to me that 10 year period may be a reasonable balance between sort of the immediate and the 23 year period. But again it really does depend on how much is actually going into that deferral account. If all of the amounts going into the deferral account, I say the shorter the better. If some part of it's going to be sort of given in the next few years by way of a flow through benefits of operating costs and therefore savings in the years, then it could be a little longer.

CHAIRMAN: And I guess thirdly, Mr. Lawson, one of the issues you raised was the \$47 million as a recovery

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2 against the cost of the fuel delivery system previously
3 written off. And a question to Mr. Morrison with respect
4 to that, just to kind of go out of order here. Is that --
5 Mr. Morrison, would that be your understanding if the
6 deferral account that's put forward is approved, that
7 would be one of the numbers that would still be up for
8 argument by the parties?

9 MR. MORRISON: I am sorry, Mr. Chairman. I was consulting
10 with Ms. MacFarlane on another matter. Could you repeat
11 that, please?

12 CHAIRMAN: I certainly could. One of the arguments that Mr.
13 Lawson makes is that the \$47 million as a recovery against
14 the cost of fuel delivery previously written off, I mean
15 perhaps it isn't fair that it's being paid back to the
16 government, is that -- is part of the deferral account
17 that's being proposed by DISCO, is that an absolute part
18 of it that that \$47 million be paid or is that something
19 that would be discussed at the general rate hearing as we
20 go forward?

21 MR. MORRISON: No, that would be a condition of the deferral
22 account, because it is part of the settlement structure.
23 And if that changes then we have to come back here with
24 some other proposal.

25 MR. LAWSON: Thank you.

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CHAIRMAN: Thank you, Mr. Lawson.

MR. JOHNSTON: Mr. Lawson, if I understand your position correctly, you have referred to the fact that the claim that was presented in the underlying litigation contained a claim, among other things no doubt, but one portion of the claim was for recovery of the capital outlay for the cost of Orimulsion. And another portion of the claim was the loss that had been suffered because the lower cost Orimulsion fuel was not available and a higher cost fuel had to be purchased, is that correct?

MR. LAWSON: Yes, I believe, Mr. Vice-Chair, that Ms. MacFarlane's evidence confirmed that.

MR. JOHNSTON: What I am not clear on is how that causes that deferral account to be over a shorter period of time, because I would think that the loss on the fuel cost side would also be projected out into a fairly long term into the future similar to the life of the plant, perhaps a little bit shorter, but similar. Could you just clarify that for me, please?

MR. LAWSON: No, I would agree that while it would a shorter period of time if it were just spread over that contract, it would not be a short period of time, because I would submit that as is being proposed that the -- as to the capital, it would be only for balance of the amortization

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2 period, the tolling agreement, which the amortization period,
3 or the capital asset, if you spread it over the balance of
4 the supply contract, I understand it may have been around
5 17 or 18 years less on the basis that it was a 20 year
6 contract. So, yes, it would shorten it up, but not to the
7 10 years that I am proposing.

8 MR. JOHNSTON: Thank you.

9 CHAIRMAN: Any other questions from the Panel? Mr. Baird?

10 MR. BAIRD: No questions or comments, Mr. Chairman.

11 CHAIRMAN: Thank you. Mr. Wolfe?

12 MR. WOLFE: I guess at the outset, it's fair to say that we
13 have no problem with the deferral account. The problem we
14 do have is with the 23 years. I don't know of anybody
15 that could predict Canadian dollar exchange, predict fuel
16 prices, predict the markets for 23 years from today with
17 any kind of accuracy. Christ, we can't even do it for two
18 years. But it's very uncomfortable though to hear Mr.
19 Morrison say it's either that or nothing because that
20 makes it a very difficult thing.

21 MR. MORRISON: That's not exactly what I said, Mr. Chairman.

22 CHAIRMAN: No, I understand that Mr. Morrison said that he
23 would prefer the Board not make an order and they would be
24 back perhaps with an alternative, is that correct, Mr.
25 Morrison, did I -

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MR. MORRISON: That's correct, Mr. Chairman.

MR. WOLFE: Okay. When I talk about the 23 years, I don't -
- I am not an accountant so -- but I don't know, but I
wouldn't think there is any requirement the deferral
account must meet the length of the depreciation time.
And that's why I say if 23 years for me is just too long a
time for a deferral account.

Now if it is necessary to meet the depreciation period,
then I say we accelerate the depreciation. Part of Ms.
MacFarlane's testimony was that that money was spent for
equipment that really truly wasn't needed, so if it truly
wasn't needed it can be accelerated. And we will just
accelerate it and meet the -- and do a different deferral
at the time. But 23 years in my guess is way too long.
If you think back 23 years ago, the NB Power of 23 years
ago is no where near what it is today.

On the other side, Ms. MacFarlane's answers I think the
ratepayers have paid over the last two or three years
several charges just like Mr. Lawson said. There was the
legal fees of \$6 million that the ratepayers have been
charged. There is that 2.9 or 2.2 million whatever it is
on the write off of the fuel handling system that went
into direct costs one year.

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2 Mr. Baird talked about the extra fuel costs that would
3 have occurred at Coleson in the last two years when the
4 Orimulsion wasn't there. That's another factor that
5 should be looked at for extra costs that has gone to the
6 ratepayers in the last two years that could be -- that
7 could be recovered now.

8 If you take those amounts directly to DISCO, plus the
9 proposed savings from the deferral account, you get a
10 little larger decrease in the rate this year and you get a
11 slightly lower rate over the next few years. But it would
12 take a new calculation for sure.

13 Another thing that kind of concerns me is that this
14 settlement is going to result in a huge volume of oil
15 flowing to Coleson Cove starting in November. As I
16 understand it they buy all their fuel ahead of time, so
17 they know what they need. How you are going to use this
18 huge amount of fuel and not incur extra costs is hard to
19 understand, but we need to understand that as well, so
20 that we don't run a deficit on the other side. And if it
21 does turn out there is a lot of export sales and do make a
22 lot of money, then under the agreement today, they only
23 share with DISCO. If they truly are going to make money
24 off of this settlement on export sales, then that
25 shouldn't flow through to DISCO as well for the

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ratepayers, if we want to be consistent.

And the final thing I had is that I think the Board should require that DISCO report at least annually on this deferral report and compare with the budget that they put together. Thank you.

CHAIRMAN: Thank you, Mr. Wolfe. Any questions from the Panel? Dr. Sollows?

DR. SOLLOWS: Yes, thank you, Mr. Chair. I guess when I look at this, I start with the -- the starting position is almost the same. How would this be treated under generally accepted accounting principles, if this was a non-regulated company? Can we live with that treatment? If we can't, then you should consider a deferral account. How far you should go in terms of amortization periods and the extent to the -- really it should be determined as much as anything by your confidence in the reality of the benefits and the longevity of the benefits. And I guess basically that. So if I -- I would look at it first with respect to if we treated this under normal GAAP, would we -- could we live with it? What would be the implications? If we can't do that or if we are willing to live with those implications, then certainly I would suggest that a deferral account would be a reasonable decision for this

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2 Board to come to, subject to consideration that it's not
3 entirely clear that DISCO is a rate regulated company and
4 you have already decided that it's not a public utility.
5 So given that these kinds of accounts are normally
6 available to rate regulated public utilities, you want to
7 I would suggest come to the more -- be somewhat modest in
8 your expectations as to the longevity of this deferral
9 account. Given the -- what appear to be the trends in
10 accounting to a relentless pressure to begin to clean up
11 balance sheets and eliminates these things, again I wonder
12 whether a very long period for the deferral account is
13 reasonable.
14 When I look at the -- looking at the agreements, the power
15 purchase agreements between DISCO and Holdco and see that
16 for the coming eight years, this year and the following
17 eight years, the capital costs are the highest and they
18 begin to fall there after, to me that creates the natural
19 length of for this account. If you are really interested
20 in the levelizing costs out over time for customers as a
21 whole, make the deferral period the eight years. And
22 those are the sum of my comments.

23 CHAIRMAN: Thank you. Any questions from the Panel? Ms.
24 Newman?

25 MS. NEWMAN: Thank you, Mr. Chair. The Utilities Municipal,

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they have no objection to the establishing -- or the Applicant establishing the deferral account in the manner applied for. And neither do they have any objection to the 2.5 percent reduction to take effect as soon as possible. Their only -- their only wish, if you like, would be that the Board hasn't -- keep the -- have the ability to scrutinize the operation of the deferral account on an ongoing basis. Thank you.

CHAIRMAN: Thank you. Any questions? Mr. Peacock?

MR. PEACOCK: Given the hour, Mr. Chair, I will be brief.

If we are here to pass the benefits of NB Power's recent settlement onto DISCO ratepayers, then I think there must be a better way to do this than with the Applicant's proposed deferral account.

We are principally concerned with the fact that NB Power's Board has decided how this settlement is best directed towards DISCO ratepayers. Obviously, we feel that this public Board, the Energy and Utilities Board should have a greater say as to how over \$300 million should be directed towards N.B. ratepayers. And we think that Friday afternoon arguments over settlement documents only recently released into the public realm offer insufficient opportunity to fully discuss the significance

2 of this economic windfall.

3 Now, I don't know much about intergenerational equity, but
4 I do know that the low income consumers of this province
5 require much more rate relief than that which is offered
6 by the Applicant. And while we may be biased against the
7 needs of electricity consumers 23 years from now, we feel
8 today's consumer should merit more rate relief resulting
9 from this settlement than anyone consuming two decades
10 hence.

11 In short, Mr. Chair, we are moving to ignore the concept
12 of intergenerational equity, because a heck of a lot can
13 happen 20 years. Today, N.B. -- New Brunswick has a lot
14 of low income consumers punished by an unjust rate
15 structure. And many of them inhabit residences that are
16 old and inefficient. These consumers need rate relief.
17 20 years from now our province's residential rate
18 structure may in fact be inclining. And our province will
19 have benefited from 20 years of residential efficiency
20 upgrades. Those consumers will be less likely to be hit
21 by rate shock. Whether or not the economic burden of
22 Coleson Cove's upgrades will be severe 23 years from now,
23 I will leave it to the economic forecasters. What I can
24 say is that there is a real economic burden now and it is
25 born by an awful lot of ratepayers currently struggling to

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get by.

For all of these reasons, we had asked that if the Board agrees to the Applicant's motion, that it take a significant oversight role over any potential deferral account. We would also ask that the Board request that any account lifetime be significantly shortened. We similarly request if possible that a larger portion of the cash settlement that was announced earlier in the hearing be applied to this year's revenue requirement. If need be, let's hold onto the cash until the full rate hearing.

We need the benefit from this settlement to be applied now and not drawn out to some date 23 years from now. If we are to reduce rates, let's do it right.

CHAIRMAN: Thank you, Mr. Peacock. Any questions from the Panel? Thank you. Mr. Theriault?

MR. THERIAULT: Thank you, Mr. Chairman. This has been an interesting and challenging two days and I don't intend to take up much of your time with my final argument. However, at the outset, I wish to say that I just want to submit to the Board that this is your interim rate relief decision that's being affected, and you as the Board have the right to adjust it in anyway you deem appropriate. I have just two points to bring before the Board. First, the concept of a deferral account is an appropriate

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way to treat the benefits arriving from the settlement negotiated with PDVSA.

Second, the Board lacks significant information on several key aspects of how the deferral account will work. These aspects I submit include verification of the calculations that support the amounts that go into the account, verification of the data that goes into the calculations, lengths of the amortization periods, methods of amortization, and most importantly, ongoing monitoring of the deferral account to ensure that the full benefits of this settlement flow through to the ratepayers of this province.

Accordingly, Mr. Chairman, Members of the Board, I ask the Board for the following rulings and orders. The Public Intervenor requests the following rulings and orders from the Board.

Rulings

1. That the Board has jurisdiction over the Deferral Account to be set up as part of the Board order in this matter.
2. That said jurisdiction includes, but is not limited to the following:
 - a. Verification of the calculations that support the amounts that go into the account.

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2 b.Verification of the data used in the calculations.

3 c.Verification that the data sources are appropriate.

4 d.Approval of the amortization period over which the account
5 will be written down.

6 e. Approval over the amortization method used to write the
7 account down.

8 f.Ability to adjust either the amortization period or method
9 upon application by any part to this proceeding,
10 or on its own motion.

11 3.That only the Board can authorize any reductions in the
12 Deferral Account.

13 4.That only the Board can terminate the Deferral Account.

14 5.That said jurisdiction shall last for the duration of the
15 Deferral Account.

16 Now I would submit the following Orders. I would ask the
17 Board to consider the following Orders.

18 Orders

19 1.That DISCO establish the Deferral Account in a manner
20 consistent with the objective of reducing the
21 requested rate increase from 9.6 percent to 7.1
22 percent.

23 2.That DISCO be ordered to reduce the Interim Rate

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increase from 9.6 percent to 7.1 percent effective August 24th 2007.

3. That DISCO be ordered to provide all of the documentation related to the settlement with PDVSA to all of the registered intervenors by September 1st 2007. As part of this documentation, DISCO be ordered to provide in Excel Spreadsheet format, all calculations that went into Confidential Attachment #1 of Exhibit A.

4. That all other matters related to the Deferral Account, including, but not limited to, the amounts credited to the account, the timing of the amounts credited to the account, the amortization period, the amortization method, and the manner of oversight on the account be reserved until these matters can be thoroughly canvassed during the upcoming hearings.

Now, Mr. Chairman, at this time, Mr. O'Rourke will hand out -- he has copies for all the parties and for the Board of my request. And that's all the comments that I have.

CHAIRMAN: Thank you. Any questions from the Panel?

MR. JOHNSTON: Mr. Theriault with request -- with respect -- excuse me, it's late in the afternoon for all of us, but with respect to your request for disclosure of the

2 underlying documentation, I am wondering and Mr. Morrison
3 might want to address this as well, is whether this may be
4 an area where there is going to be some dispute. Perhaps,
5 Mr. Morrison, will tell me he has no problem with it, but
6 perhaps we should think about what other alternatives
7 there are for looking through that process, whether it be
8 through the IR process or through some separate Motions
9 Day. Mr. Morrison, perhaps you want to comment first?

10 MR. MORRISON: I was speaking to Mr. O'Rourke, but I believe
11 you are talking about verification of -- oh, the release
12 of the settlement agreement. I am almost loathe to say
13 it, but the contractual obligations have not gone away
14 since yesterday. The Board has made a ruling with respect
15 to certain documents. I am cognizant of the legal
16 obligations that are on my client with respect to
17 confidentiality. As DISCO has said from the outset, it's
18 bound by those. I suspect that the Board may have to make
19 yet another ruling with respect to the confidentiality.
20 As far as supplying it by September 1st, I don't
21 anticipate that would be a problem, but it would be filed
22 with Board requesting the protection of Section 34.

23 MR. JOHNSTON: The reason I raised this Mr. Theriault and
24 Mr. Morrison, is that Mr. Theriault in his submission has
25 made certain requests that I think the Board would have it

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2 -- and I guess I speak only for myself -- we might have some
3 difficulty in dealing with without proceeding through a
4 full process. And I just inquire as to whether either of
5 you or any other parties have specific suggestions as to
6 how to best move into that process. Mr. Theriault?

7 MR. THERIAULT: Thank you, Mr. Vice-Chairman. First of all,
8 the argument that my friend just posed is the same argued
9 that was yesterday and that's why I have requested that it
10 be considered an order of the Board to release that
11 document as part of the filing. But it would also go to
12 answering a lot of the questions that the intervenors have
13 raised here this afternoon. It would give people the
14 ability to go back to check that documentation. And as I
15 suggest in item number 3 or 4 of my requested orders that
16 these matters could be then dealt with in a reasonable
17 fashion. But at the same time the ratepayers of the
18 province of New Brunswick would get the immediate relief
19 and the deferral account would be set up.

20 CHAIRMAN: Thank you. Mr. Morrison, any rebuttal?

21 MR. MORRISON: I do, Mr. Chairman, but quite frankly I would
22 like to have five minutes or 10 minutes. I am just
23 looking at the Public Intervenor's proposed Order. A
24 quick glance, there are probably some items there that we
25 probably don't have any difficulty with. There may be

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others that we do. If I have 10 minutes --

CHAIRMAN: We will take a 10 minute adjournment.

MR. MORRISON: Thank you.

(Recess: 5:00 p.m. to 5:15 p.m.)

CHAIRMAN: Mr. Morrison.

MR. MORRISON: Yes, Mr. Chairman. I will be brief. I will deal first with some of the comments made by the Public Intervenor, particularly in this -- in his draft proposed Orders and Rulings. When I look at, I don't know if you have a copy in front of you, but --

CHAIRMAN: I do not have a copy in front of me. I thought it was being distributed, but --

MR. MORRISON: And it doesn't have to be marked as an exhibit. I am just using it for talking notes. But I will start with the first one. He is asking that the Board has jurisdiction over the deferral account. Obviously, we don't have any problem with that. The next item is the said jurisdiction includes, but is not limited to the following; verification of the calculations is number 1, that support the amounts. Verification of the data used in the calculations is number 2. Verification that the data sources are appropriate. We don't have any problem with those subject to the confidentiality concerns that I have raised yesterday and today.

2 The third items that he asked is approvals of the
3 amortization period over which the account will be written
4 down. And approval over the amortization method needs to
5 write the account down. And I believe this was raised by
6 Mr. Lawson as well, and I could be wrong, it may not have
7 been Mr. Lawson. Let me put it this way, the deferral
8 account to accumulate the benefits flowing through to
9 DISCO through the tolling agreement, the deferral account
10 itself collecting those amounts, if you will, has to be
11 for 23 years, because that's how the benefits flow to
12 DISCO under the tolling agreement. It's a 23 -- it's a
13 balance of 23 years left in the term. However, if the
14 Board chooses to disburse those benefits to ratepayers
15 over a shorter period of time, you certainly can do that.
16 In our view, it violates the principles of
17 intergenerational equity. I think parties should be aware
18 that in the end you are going to have higher rates at the
19 end of that period and there is going to be higher
20 interest costs. But DISCO for its part, the amortization
21 -- the amortization -- the period over which you disburse
22 the benefits from the deferral account, it can be 10
23 years, it could be five years, it could be 15 years. It
24 doesn't matter to DISCO. It does have an impact, and I
25 think the intervenors should be aware of

2 this, that it will have an impact in terms of what the rates
3 will be at the end of that payout period and there will be
4 additional interest costs, because obviously it is going
5 to spread out over a longer period. But the collection
6 aspect of the deferral account does for our purposes have
7 to be the 23 years.

8 As far as, he has a couple of other Rulings that the Board
9 can only -- that only the Board can authorize any
10 reductions in the deferral account. No problem with that.

11 And only the Board can terminate the deferral account.
12 We have no problem with that. That the said jurisdiction
13 shall last for the duration of the deferral account.

14 Again we have no problem with that.

15 He has asked for a number of Orders. The first one is
16 that DISCO establish a deferral account in a manner
17 consistent with the objective of reducing the rate from
18 9.6 to 7.1. Of course, that's essentially what we are
19 asking for. But his fourth order is that all other
20 matters related to the deferral account, including, but
21 not limited to, the amounts credited to the accounts, the
22 timing of amounts credited to the account, the
23 amortization period, the amortization method, and the
24 manner of oversight on the account be reserved until these
25 matters can be thoroughly canvassed during the upcoming

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hearing. Those are all legitimate concerns. But the problem is, as I have mentioned earlier, I said in my letter of August 15th, that creates tremendous risk for DISCO in terms of unilaterally reducing the interim rate by 2.5 percent if you don't have the deferral account that supports that reduction in place. They don't co-exist. They don't live together very well.

He has two other Orders that he has requested. That DISCO be ordered to reduce the interim rate increase from 9.6 percent to 7.1 percent effective on August 24th 2007. I think our order was whenever the Board issues its decision that's when the effective date of the reduction would be. And finally orders that DISCO be ordered to provide all the documentation related to the settlement with PDVSA. Basically the underlying documents, the settlement agreement, Excel Spreadsheet format and so on, again that relates to the confidentiality issue, which unfortunately I don't see any other way around that the matter is going to be back before the Board with respect to those specific documents. So that's all I can say about that.

I would like talk -- just a couple of comments that come up from other intervenors. Mr. Lawson talked about if something goes wrong with this fuel supply agreement

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that the risk should -- of that should lie with Holdco. If something goes wrong with the fuel supply agreements or the numbers, the benefits aren't what we think they are, basically it's not a risk. It just means that the benefit is lower. It's a lower benefit. And so that would flow through as just a reduced benefit. So it wouldn't -- it's not like there is an increase cost. It's just a reduced benefit.

Mr. Baird in his comments talked about how this -- again he talked about the \$47 million. And unless I misunderstood his remarks, I still believe from what he said that he believes that that \$47 million somehow ended up in DISCO's rate base and was charged to the customers.

Ms. MacFarlane was very clear about that. The \$47 million didn't end up in the rate base. It was never charged to customers. That \$47 million was never collected from customers. So -- and she said it would be a windfall to return that to customers, would in my submission be akin to the legal term of unjust enrichment.

But to address Mr. Baird's point, it just was not ever included in the rate base being collected from customers. The only other item I want to address is Dr. Sollows talked about the role of general accounting principles. Regulators make rate decisions. I am advised that the

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Canadian Institute of Chartered Accountants has no business in this whatsoever. And so GAAP has no application to whatever it is that you do with respect to setting up regulatory accounts.

Those are all of my submissions, Mr. Chairman. Thank you.

CHAIRMAN: Thank you, Mr. Morrison. I guess just before concluding, I want to thank all of the parties for working diligently today to complete this hearing. I know it's a matter that everybody is very interested in and certainly looks forward to an early decision. So thank you to everybody for sticking with this. I guess it's 5:30 now.

So it has been a long day. And I do want to thank the Board Staff and our court reporter and our audio people who let us down for about 10 minutes earlier today, but are here at this late time, our translators.

The Board will consider all of the arguments that have been put forward today and all of the evidence that it has heard. I don't know whether or not we will issue an oral decision or a written decision. But we will most certainly endeavour to have our decision rendered just as quickly as possible understanding the importance of this issue. So again thank you to the parties.

(Adjourned) Certified to be a true transcript of the proceedings of this hearing, as recorded by me, to the best of my ability.