New Brunswick Board of Commissioners of Public Utilities

In the Matter of an application by the NBP Distribution & Customer Service Corporation (DISCO) for changes to its Charges, Rates and Tolls - Revenue Requirement

Delta Hotel, Saint John, N.B.
March 16th 2006

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CHAIRMAN:	David C. Nicholson, Q.C.
COMMISSIONERS:	Jacques A. Dumont
	Patricia LeBlanc-Bird
	H. Brian Tingley
	Diana Ferguson Sonier
	Ken F. Sollows
	Randy Bell
	David S. Nelson
BOARD COUNSEL:	Peter MacNutt, Q.C.
BOARD STAFF:	Doug Goss
	John Lawton
BOARD SECRETARY:	Lorraine Légère

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CHAIRMAN: Welcome to day 53. Could I have appearances for the record please? For the Applicant?

MR. MORRISON: Good morning, Mr. Chairman and Commissioners. Terry Morrison. With me at counsel table is Lori Clark and Michael Gorman.

CHAIRMAN: Thank you, Mr. Morrison. Canadian Manufacturers and Exporters?

MR. LAWSON: Good morning, Mr. Chairman and Commissioners. Gary Lawson. And I'm appearing with David Plante, expected to be showing up shortly, and Ron Nicholson.

CHAIRMAN: Thank you, Mr. Lawson. Enbridge Gas New Brunswick?

MR. MACDOUGALL: Good morning, Mr. Chair and Commissioners. David MacDougall for Enbridge Gas New Brunswick. And I'm joined today by Andrew Harrington, Shelley Black and Ruth York.

CHAIRMAN: Thanks, Mr. MacDougall. The Irving Group? Mr. Booker here? Yes.

MR. BOOKER: Good morning, Mr. Chair and Commissioners.

CHAIRMAN: Good morning, Mr. Booker. Municipals?

MR. GORMAN: Good morning, Mr. Chairman. Raymond Gorman for the Municipal Utilities. This morning I have Eric Marr and Dana Young with me from Saint John Energy.

And I anticipate before the day is out that I will have Charles Martin and Michael Couturier from Edmundston and Dan Dionne from Perth-Andover and perhaps Paula Zarnett with us as well.

CHAIRMAN: Good. Thanks, Mr. Gorman. Vibrant Communities here? No. Public Intervenor?

MR. HYSLOP: Thank you, Mr. Chair. Peter Hyslop with Mr. Knecht, Mr. O'Rourke and Ms. Power.

CHAIRMAN: Good. Thanks, Mr. Hyslop.

Mr. MacNutt, whom do you have with you today?

MR. MACNUTT: I have with me today, Mr. Chairman, Doug Goss, Senior Adviser, John Lawton, Adviser, Andrew Logan, Jim Easson and John Murphy, Consultants.

CHAIRMAN: Thanks, Mr. MacNutt. Any preliminary matters?

MR. MORRISON: Yes, Mr. Chairman. I have some undertaking responses to file. But before that there is an important matter came up out of Mr. MacNutt's cross examination yesterday. It appears that Mr. Hyslop isn't the only simple country lawyer in the hearing room. Mr. MacNutt is indeed on the rural rate. He is the only person on his street on the rural rate. And speaking to him this morning, he indicates that he wants to switch to the urban rate. So I want to put everybody on notice that will impact our 06/07 revenue requirement.

CHAIRMAN: Good, Mr. Morrison. Mr. MacNutt, you are going to have to mow your lawn now.

MR. MACNUTT: It appears so. Thank you.

CHAIRMAN: Go ahead with the undertakings.

MR. MORRISON: The first is undertaking number 6 from February 9th, Mr. Chairman.

CHAIRMAN: And that is A-156.

MR. MORRISON: The next one is undertaking number 7 from

February 9th 2006.

CHAIRMAN: That is A-157.

MR. MORRISON: The next one is undertaking number 3 from February 14th.

CHAIRMAN: That is A-158.

MR. MORRISON: And finally, Mr. Chairman, undertaking number 1 from February 21st.

CHAIRMAN: And that is A-159.

And those are all your preliminary matters, Mr. Morrison?

MR. MORRISON: Those are all mine. I believe Mr. Hyslop may have --

CHAIRMAN: Yes, he does. Mr. Hyslop?

MR. HYSLOP: Thank you, Mr. Chair. As indicated by Mr. Morrison yesterday, the issue relating to the admissibility of two documents that I wanted to put on the record relating to the Orimulsion issue is now resolved. I have given copies to the Secretary.

And they consist of two documents. One is the copy of Mr. MacPherson's prefiled evidence at the Orimulsion hearing. And the second is an excerpt from the Crown Corporations Committee hearings last fall.

And I would offer those two documents into the record as exhibits

CHAIRMAN: Okay. The excerpt from the Standing Committee on Crown Corporations dated November 24th 2005 is exhibit PI-21. That is PI-21.

And I take your word for it, Mr. Hyslop, that the next exhibit is a portion of the direct evidence of Mr. Stewart MacPherson before this Board. There is no date. But it is in reference to the Coleson Cove refurbishment as I understand it?

MR. HYSLOP: It would be the evidential portion but not the appendixes and schedules that would have been referred to in it, Mr. Chair.

CHAIRMAN: Okay. Thank you. That is PI-22.

And just as an aside, I really don't see any difficulty in something being introduced that was previously before this Board in another hearing. That is my personal opinion. I have no personal opinion I will express in reference to the other.

Any other matters?

MR. MACDOUGALL: Yes, Mr. Chair. David MacDougall for Enbridge Gas New Brunswick. You will recall yesterday Mr. Larlee made some comments with respect to his views of Dr. Rosenberg's evidence. And you offered us the opportunity to get a response.

I was able to catch Dr. Rosenberg before he headed to

Hong Kong for two weeks. And I have a response that I want to file and make a couple of comments on. I will give that to the Secretary and hand it out. And then I can speak briefly to it.

CHAIRMAN: Okay. Did you want to -- well, that should be an undertaking or something, shouldn't it, just an exhibit.

MR. MACDOUGALL: It is in the form of an undertaking.

CHAIRMAN: Okay. Great. That will EGNB-15.

MR. MACDOUGALL: And, Mr. Chair, in relation to that you will note there is a blank for the transcript page reference because we did not have the transcript at the time Dr. Rosenberg prepared it. The transcript page reference is actually page 5639. And I would also like to note for the record that Dr. Rosenberg's response is with respect to the GS II rate because that is how I had taken the notes down yesterday, but we didn't have the transcript. The transcript actually -- the question was in reference to the general service rates, so both GS I and GS II, but Dr. Rosenberg has confirmed to me that this response would be similar with respect to GS I. There is a numerical example in here but the numerical example would be different for GS I but would come to the same end result.

CHAIRMAN: Thanks, Mr. MacDougall.

MR. MACDOUGALL: Thank you, Mr. Chair.

CHAIRMAN: Any other matters? Well just before we go back to questioning by the Commissioners, Commissioner Sollows and I were chatting after the close yesterday and I had thought that there was an undertaking to provide certain information concerning the NUG contracts. And we then looked at the transcript and found that Commissioner Sollows and I got into an argument and we didn't elicit an undertaking. So I will ask Commissioner Sollows if he would set the background to it.

MR. MORRISON: Perhaps before you do that, Mr. Chairman, we certainly took your comments that day as an undertaking request, or at least an undertaking request. We have made inquiries which we think will respond to your question. We are in the process now of course of vetting that with Mr. Stewart because of the issues that you are well aware of. I have a preliminary -- we had a preliminary response from Mr. Stewart this morning. I have only had a chance to look at it very briefly and we have to circle around with them again at the break. So we certainly took it as a direction for us to provide information, and as we understand it is the ability of economically dispatching the NUGS. So it's not that -- we haven't ignored the issue. We have been dealing with it.

CHAIRMAN: Okay. That's great. It was not on the list of undertakings.

MR. MORRISON: We know that.

CHAIRMAN: But I appreciate the fact that you have got that information.

DR. SOLLOWS: It was not just the ability under the contract but the cost implications of moving them out of economic merit.

MR. MORRISON: Yes.

DR. SOLLOWS: Thank you. I think through this -- and it's a fairly long and rambling transcript reference, so I appreciate that it might have been missed. What we were really looking for was the exhibit that you have most recently filed as A-150, that there be some -- it's probably getting a little crowded, but the thought was there would be a column or a reference or an exhibit in the same format that gave the data for fully economically dispatched capacity on the system, or capacity dispatch for system security reasons.

MR. MORRISON: We -- I believe you put that question to Mr. Marois, Commissioner Sollows, about whether we could do it in this particular fashion.

DR. SOLLOWS: Yes.

MR. MORRISON: I think Mr Marois indicated that --

DR. SOLLOWS: He wasn't sure.

MR. MORRISON: Well we concluded that we can't do it in that format. But we did provide information in another undertaking response, and I think that one was marked yesterday, which refers to the undertaking response or the IR response. However, we are -- we do have two undertakings that will address the re-dispatch issue and the cost implications, and our only concern at this point because of the legal issues involved is getting Mr. Stewart to sign off. Otherwise what will happen is if he doesn't agree, then he will have to come down here and argue why it shouldn't be introduced. So --

DR. SOLLOWS: Thank you.

CHAIRMAN: Okay. Well the Vice-chair has an additional question. That's one thing about going over the evening, why things come up. Go ahead, sir.

BY THE BOARD:

MR. NELSON: Mr. Marois, just going back to I guess the vesting agreement, the hydro pole adjustment in reference to 6.12. Could you explain for us the difference between top of in-province firm versus top of dispatch?

MR. MAROIS: Top of dispatch includes also export sales. So it's really all the generation that includes both to serve in-province and to serve exports, while the top of

in-province only includes load to serve -- or generation to serve in-province. So that's why we were convinced that the right way to do the hydro adjustment is to use the in-province -- top of in-province curve because the hydro adjustment is really an adjustment of the vesting price initially set at the beginning of the year which is based on the in-province load, because the vesting price is to serve the in-province load. So it's totally consistent with how you set the price at the outset of the year.

MR. NELSON: So the top of dispatch is based on economic dispatch?

MR. MAROIS: They are both based on economic dispatch but one is only -- is for the load that is used to serve in-province. The other one includes all the load to serve in-province but also -- the total generation really. That includes export sales.

MR. NELSON: Okay. That includes export sales. So it's all the generation companies right in line versus you are only taking for top of in-province certain generation capacity.

MR. MAROIS: Yes. It's the same basic calculation, the same theory, the same approach. It's just one is how much generation did you use to show the in-province load, and that's what we are looking at here because the vesting

price is set to show the in-province load, and then you are adjusting that vesting price based on actual hydro. But the other one, the top of -- I forget the term -- top of dispatch is really all generation. So it includes both in-province and export.

MR. NELSON: Also I just want -- with the estimated billing procedures that you have put in place, and I was reading an article in the Times & Transcript last Saturday, and it said that you had over a thousand phone calls, complaints about the estimated billing.

MR. MAROIS: That sounds right, yes.

MR. NELSON: Have you looked at if there has been any costs incurred because of the estimating going to your customers? Have you looked at any, you know, compensation, credits, or something like that, whether it's because of late payments or interest charged on overdue accounts because of the -- we will say maybe the problems you had with the estimates?

MR. MAROIS: No, because for different reasons. I mean if somebody called with a genuine concern we were willing and able to adjust the estimate right then and there. That's one reason. The other reason is it gets corrected the following month once you do the actual reading. The other thing is the -- what we supplied to you this morning, the

additional undertaking -- the additional undertaking shows that really the estimate is neutral. So in other words there are going to be as many estimates that are going to be under-stated that are over-stated. So at the end of the day -- and that's unfortunately the reality of estimating. You cannot get it perfect. So some customers will have maybe an estimate that is somewhat high and other customers will get an estimate that is somewhat low. But I mean it's kind of something you have to accept. That being said this is a pilot and we are learning from this pilot and we have already identified certain things we can do better. For example, we will be able to take into account weather, actual weather. We are looking at modifying the system as we speak. So we believe we can get it more accurate. But there is always going to be discrepancies for things that are totally outside of our control.

MR. NELSON: Well what if there was some hardship, you know, a hardship situation where people were overcharged, you know, late payments, interest or anything else? I mean is anybody --

MR. MAROIS: We always take that into account. I mean each time there is somebody that raises a case of hardship we look at the case in a very humanistic fashion. So if

there is certain things we can do to assist the customers, we do.

MR. NELSON: So you have no program in place then to we will call it make amends for any issues --

MR. MAROIS: It's on a case by case.

MR. NELSON: So basically it's based case by case, if anybody comes in or calls in and complains or issues a complaint --

MR. MAROIS: Yes. We would look at the case and if it warrants an adjustment we will do it.

MR. NELSON: Okay. Thank you.

DR. SOLLOWS: Thank you. I would just like to follow up on Vice-Chairman Nelson's point -- or points. First with respect to the trial program that you are -- basically you have run an experimental billing program. Did you ask the customers if they wanted to participate? Was it voluntary?

MR. MAROIS: No.

DR. SOLLOWS: So these customers were really dragooned or co-opted or really had no option but to participate in this program that you have on the record said was experimental and a trial basis. So they have been not only not compensated for being guinea pigs, they have been in some sense penalized by the problems that have arisen

with the algorithm?

MR. MAROIS: Well all customers are being compensated because as I mentioned I believe during this process -- the reason we are doing this is to try to curb our costs. And if we were to stop this program tomorrow we would have to hire about 12 new meter readers, because I think I mentioned that because of our staff reduction we effectively reduced the number of meter readers by 12. And we saw that as an opportunity to try to keep those costs down and the only way we could do that in this point in time was to introduce meter estimating, because with that amount of people we cannot continue.

So customers are benefiting because if we do stop this we are going to have to introduce new costs. Naturally we want to make it as good as possible.

And the other thing too and it might not be much of a consolation, but I believe we still have to look at it that way, is it is interim in nature because we believe that within a certain number of years we will have automated meter reading. I mean, that's going to be -- I thing it is definite, the issue is when. But currently as we speak for example we do have other means that we are implementing to try to minimize the impact of such initiatives. For example this year we are adding a unit

in Fredericton to do drive-by meter reading, remote frequency meter readings.

So we are trying to read as many meters as we can with different technology, but it's really a balancing act in terms of cost benefits. But we are really caught between a rock and a hard place right now because again we are -- the staff reduction, but we are trying to make the best of it. And we really take seriously the comments we got from our customers and we are acting on it.

DR. SOLLOWS: Okay. When I looked in reference to this, exhibit 157, this is the information about the algorithm and your statistical rationale for it. Taking a quick look at it, and of course I have just had it for a few minutes, and if I understand it correctly it didn't -- you developed an algorithm that didn't use the actual weather, it simply assumed that the weather would be the long run normal, is that correct?

MR. MAROIS: Not really. It's not -- and this could get quite technical but in simplistic matter the way the estimating was done is it was based on the previous months.

DR. SOLLOWS: I see.

MR. MAROIS: So being based on the previous month it did take into account recent weather and that previous month's

actual reading was simply adjusted to bring it back into a more current estimate based on the time of year. In simplistic terms that's what we were doing.

DR. SOLLOWS: I guess my problem with that is all the energy estimating algorithms that I'm familiar with for companies like yours and other energy service companies, would use the actual weather for the billing period and feed that into -- the company that fills my oil tank gets the reports of the degree days through -- each day, each week, each month, and determines when they send the truck to my tank. They don't just take the estimate that I will use the same as I might use in the long run and send the truck on that basis.

But that seems to be what you have done in terms of sending your bills to the customers.

MR. MAROIS: Well we did talk to other utilities. We didn't talk to oil companies but talked to other utilities, and then it's not -- it's not every utility that has -- takes into account actual weather. So there seems to be different approaches.

But through our research and our discussion with SAP, our billing engine, we have determined a way to factor in actual weather. And to be honest -- I mean, I think what exacerbated the situation was January. January was I

think the mildest on record.

So what we did is the January estimate was based on December which was normal weather and that created overestimates unfortunately. But now by introducing a weather adjustment we should get rid of those. It doesn't mean we still have -- we will still have -- I believe our approach will be quite accurate on a class basis but then you are going to have certain cases that are going to be either over or under estimated for different reasons.

DR. SOLLOWS: Okay. I will leave that there and follow up on Commissioner Nelson's other point with respect to top of in-province versus top of dispatch.

And as you said it it occurred to me that one of the consequences of the change from moving of the top of in-province dispatch to the top of export dispatch or vice versa, is the way -- in effect the net compensation to Disco for I think the related issue of scheduling the natural gas plants out of merit, in that by scheduling the natural gas plants out of merit you have freed up capacity -- more economic capacity than would normally be scheduled in-province, you have freed it up to compete in a price sensitive export market and therefore increased your exports.

And to the extent that excess hydro flows caused the

same thing, I'm wondering if calculating it based on top of dispatch isn't in effect really fairer under the vesting agreements?

MR. MAROIS: Well I'm not totally certain I got your point because you are mixing the two -- the hydro and the -- but I'm convinced that doing it in-province is the right thing. Because again when you set the vesting price at the beginning of the year, you set it based on in-province load, because the vesting price is the price to serve your in-province customers. That vesting price set at the beginning of the year assumes average hydro.

The only thing you are doing is saying, okay, what would have been that vesting price if the hydro would have been at the level we now know, the actual.

So you do the exact same calculation after the fact, factoring in actual hydro. So you are comparing apples and apples. You are just saying one was with average hydro, one is with actual hydro, and the difference is X and that's your hydro adjustment.

So for me it's quite obvious that it's the right thing to do. If you use top of dispatch you are factoring in volume or generation that was not factored in to the setting of the vesting price initially. So now you are comparing apples and oranges.

And to boot, since this Disco shares in any variances due to export margin, then that's where there is the double counting. And that's why I said yesterday if we have an incorrect way of calculating the hydro adjustment we would have to develop an incorrect way of calculating the export margin calculation because then -- you would almost have to try to get two wrongs to make a right, which is not the right way to do it.

DR. SOLLOWS: I understand. The thing that's troubling me as someone who, you know, often does marking correct and incorrect is not black and white, it's often a judgment call. And while you might conclude that certain things are incorrect, I might conclude otherwise. And so that --

MR. MAROIS: That's why --

DR. SOLLOWS: -- that's why I'm not sure that it is as clear as you indicate, but I can leave it.

MR. MAROIS: But to get to the bottom of it though we did indicate in our response that we will get a third party to review it. So that will be really clear at the end of the day.

DR. SOLLOWS: Thank you. I do want to go on to a matter arising from question -- or it was a question in response to an undertaking provision. And I was musing over it last night and I want to make sure that the facts are

clear in my mind relating to interruptible sales and surplus sales.

Now as I understand it your interruptible sales are used essentially as a standby for combined heat and power producers, co-generators, that sort of thing and for all intents and purposes a equivalent of a standby rate, and until you develop a formal standby rate are really probably necessary, is that fair?

MR. MAROIS: Yes.

DR. SOLLOWS: Okay. But distinct from interruptible the surplus sales are more of an option for customers willing to take a risk on non-firm service, is that --

MR. MAROIS: That's fair.

DR. SOLLOWS: Okay. Now the capacity that serves that non-firm service is currently paid for by Disco's firm customers through the vesting PPA, isn't it?

MR. LARLEE: Well, at the time of peak there is really no capacity required to serve that load. Because they can be interrupted. At other times of the year it's served --

DR. SOLLOWS: But somebody paid for the capacity?

MR. LARLEE: -- it's served from the capacity that Genco has --

DR. SOLLOWS: So when it is served it is served through by capacity that is being paid for by Disco's customers?

MR. LARLEE: Yes. That's correct. And those are the same customers that are benefiting from the fact that it's interruptible.

DR. SOLLOWS: We are talking surplus not interruptible?

MR. LARLEE: Small i interruptible.

DR. SOLLOWS: Okay. Yes. Can you go on to explain how Disco's firm service customers are benefiting from the fact that it is small i interruptible?

I haven't seen any real evidence of that. Maybe I have missed it.

MR. LARLEE: Well, conceptually there is that piece of load that Disco doesn't have to have firm capacity reserve for or firm capacity to serve.

DR. SOLLOWS: But Disco does?

MR. LARLEE: That lowers -- that should lower Disco's costs overall. And that benefits all customers.

DR. SOLLOWS: I understand the concept. But I haven't seen any analysis to support that it actually carries through in fact. Is that in the evidence record?

MR. LARLEE: I don't believe it's in the analysis, no.

DR. SOLLOWS: Thank you. Now I also understand that there is some concern that the surplus customers -- and I'm talking about surplus, not big I interruptible -- surplus customers may want to become firm customers at the time of

the Point Lepreau outage. Is that right? And is that a concern for you?

MR. MAROIS: Well, it's a concern if the pricing of the surplus product gets out of line with the firm rate.

DR. SOLLOWS: Right.

MR. MAROIS: That's a reality that --

DR. SOLLOWS: And it is out of line with the firm rate now?

MR. MAROIS: No, not right now. But it could get out of line during the refurbishment.

DR. SOLLOWS: Okay. So you are saying that the firm rate and the non-firm rate are the same now? What do you mean by out of line?

MR. MAROIS: Well, if during refurbishment the interruptible -- or the surplus rate gets more expensive for example than the firm, then what is the benefit of -- well, first of all there would be a benefit to go to the firm rate. First of all you get firm service. But also you get a lower price. So that is what I mean.

If the interruptible or surplus rate gets more expensive than the firm or gets close to the point where there is no benefit of staying on it, then I'm certain that customers will look at -- it's going to be a business decision on the customer's part to say well, should I stay on that rate versus going to the other one?

DR. SOLLOWS: Right. And I think if I were the business owner and I could buy firm service, the energy more cheaply, it is what we would call a no-brainer?

MR. MAROIS: Sounds like one.

DR. SOLLOWS: Okay. Now -- and from Disco's perspective, when they go onto firm service, you are actually getting someone that contributes now through the rate to pay the capacity costs that you are paying for under the vesting agreement?

MR. MAROIS: Yes. But we are advancing the time that we will need new capacity. And especially during the Lepreau refurbishment we anticipate capacity shortfall. So that's why we have to run the numbers.

We have to do an analysis to say what happens. If your firm customer -- if your surplus customer converts to firm, yes, you may be getting some contribution. But then all of a sudden you may need to buy new capacity. Because you already had a capacity shortfall.

DR. SOLLOWS: But you have indicated that they are probably going to want to convert to firm anyway because it is a no-brainer?

MR. MAROIS: No, no. Unless we do something about it. And that's what I mentioned --

DR. SOLLOWS: What could you do about it?

MR. MAROIS: Well, we have to look at the pricing options. What I believe I mentioned yesterday is we are doing an analysis right now. And we are trying to model what could be the surplus rate during the refurbishment compared to the firm rate.

And we will look at the pros and cons of making adjustments. And if we do determine that we should modify any of these rates, then we would come back to the regulator, the PUB and ask for changes in rates.

But that's the first thing we need to do. We need to understand where both of these rates will go during the outage.

DR. SOLLOWS: Well, perhaps. But I'm just left musing and wondering. I mean, as I understand this evidence -- and it seems that you have been offering this surplus rate for some time but don't have any formal economic justification for it other than it seems like it is a reasonable thing to do.

I'm wondering if Disco and Disco's customers wouldn't be better off just by having you wind up the surplus rate category as quickly as possible so to give those customers a choice in advance of the outage at Point Lepreau to determine whether or not they want to sign secure long-term contracts in the wholesale market, which seems to be

the legislative and White Paper intent for these kinds of customers or to take firm service from you which would benefit both Disco and Disco's customers by having them share in the cost -- recovering the costs of the capital plant that's used to provide their service.

So I'm wondering -- left wondering why we -- what evidence points to not doing that? It seems almost that conclusion is almost inescapable to me. And I want to make sure the facts are clear so that we can hear a good clear argument from counsel at the end.

MR. MAROIS: Well, I think the problem is the evidence you have in front of you is for 06/07. And what we are talking about here is for post 06/07.

So I mean, it's obvious from our rate proposal that we had not anticipated getting rid of the surplus rates for 06/07. And we are proposing to continue those rates. And those rates are -- the surplus rate is making a contribution to fixed costs.

I believe we indicated that with a $2 million correction it's making about a $1.4 million contribution. So there is some contribution to fixed costs, fixed generation costs.

But I think it would be premature to determine if we want to abandon that rate or not. Because again it might

be detrimental to Disco's customers overall. Because we know we are going to have a capacity shortfall during the Lepreau outage.

If we make the decision now that we should no longer offer surplus products then we have just made a decision to increase that capacity shortfall by a couple of hundred megawatts.

And we are going to have to make a decision -- we should analyze that first to see what is the cost of getting that replacement capacity? Is that something we want to do? And I don't know. We are doing that analysis as we speak.

DR. SOLLOWS: I guess I will close off by simply saying I think you should have analyzed this a long time ago. But I want to carry on with my prepared questions now.

And so I just want to make sure that my understanding of the facts are clear. And we will let counsel deal with it in argument.

So I would like to go on to my prepared questions. And I want to -- I have a fairly long series of questions here. But I want to talk about residential rate design.

Now I understand that Disco's corporate policy goal with respect to residential rates is to move from the current declining block rate to a flat rate and thereafter

to an inclining block rate.

The rate proposal that is currently before us increases the block size from 1300 kilowatt-hours per month to 1400 kilowatt-hours per month.

And the question I have is am I right to infer that the size of the first block of the inclining block rate that you ultimately envision is equal to a larger than 1400 kilowatt-hours?

MR. LARLEE: Can I ask you to repeat the question?

DR. SOLLOWS: You have been told by your Board of Directors to move towards an inclining block rate, first flat then inclining. And in this proposal you have moved your block size from 1300 kilowatt-hours per month to 1400 kilowatt-hours per month.

I infer from that that your ultimate goal for the block sizing and inclining block rate is greater than 1300 kilowatt-hours. Am I right?

MR. LARLEE: No. I wouldn't think that that inference would be correct.

DR. SOLLOWS: Okay. That is fine.

MR. LARLEE: One of the reasons that we went in the cost allocation study to split out electric heat and non-electric heat was that so when we get to a point in time where we might consider an inclining block rate that we

would have that analysis available to us to look at what the best break point would be for any inclining block.

DR. SOLLOWS: Okay.

MR. LARLEE: Because once you go to a flat block then really you can put your inclining block anywhere.

DR. SOLLOWS: Right.

MR. LARLEE: The customers are paying the same price for all energy, so --

DR. SOLLOWS: So you say when you get to that point in time. If I recall, your Board's instruction was to develop a flat block by 2007. And this is setting a rate that is at least partially into 2007 year.

So aren't we at that point in time? No. It was inclining by 2010. Or no, that was a ratio of 1 for 2010.

MR. MAROIS: Yes. Well, I think like I mentioned before, I believe the Board's directive is somewhat work in progress especially following the ruling of the Board.

I mean, the ruling of the Board made it clear that we should eliminate the declining block rate within five years. And so once that's done then definitely it's going to create opportunity to look at introducing an increase in block rate.

DR. SOLLOWS: So I guess my next question is what is the target for the first block size when you get to the

inclining block rate, given that you must have worked on it, because your Board directed you to be flat by the coming year or at latest the year after and inclining a few years later. I'm wondering where you think the first block size, the target would be?

MR. LARLEE: Yes. I mean, I have done some preliminary analysis on what it would look like and where the rates might go.

And my thinking at this point is that somewhere around sort of the baseload usage level, the average baseload usage level for residential customer, which is between 8' and 900 kilowatt-hours a month, would be reasonable.

DR. SOLLOWS: Thank you. That is interesting. Because it is about the same number that I came to when I thought about it. That will make what proceeds fairly easy. Because what proceeds from here works from a first block size assumption of 800 kilowatt-hours.

So the prelude to this question may be a little long. And you may want to take some notes of the numbers as we work through it.

But the evidence seems to indicate that Disco's ultimate goal is to adopt an inclining rate block structure. I haven't heard much opposition to that as an ultimate goal from any of the Intervenors as long as

issues like equity and rate shock are dealt with appropriately. Is that a fair characterization of the evidence?

MR. MAROIS: Well, just one thought that came to my mind when you were saying that is I guess the other thing that preempt introducing a declining block rate is a seasonal rate. I mean, the Board has asked us to introduce -- to make a proposal in the next rate application I believe. Well, I mean, my personal view is if you have a flat block and then you get seasonality, it's either that or an inclining block rate if not both.

DR. SOLLOWS: And I understand the Board's order. And if you recall, there was a different opinion expressed at the time of that order.

MR. MAROIS: But I guess what I'm saying is if we do introduce seasonal rate then I think it takes away the need to introduce an inclining block rate. It's one or the other.

DR. SOLLOWS: I guess to just follow up on that point before I go to my prepared questioning, I think the concern that I would have with a seasonal rate, based on my understanding of the data that you filed is that it would be very difficult for you to develop a fair and equitable seasonal rate with the current customer classifications

that you have.

Because many of your industrial customers are in fact seasonal in nature and exhibit seasonal behavior that is indistinguishable from residential customers. And so that is why I think that maybe we might disagree.

But I want to carry on with my own line of questioning if that is okay.

I find it useful to separate the issues of rate design and revenue requirement so that I come to a clearer understanding of the issues. So I wanted to examine the impact of restructuring your residential rate on a revenue-neutral basis.

I took the 2005 invoice -- year invoice records for the residential classes from the data you filed and calculated the revenue generated by applying your July 7th 2005 rates. And I didn't make any adjustment for weather or anything else, just tried to get a rough estimate here. When I did that I generated a base revenue of 451 million for the residential classes. And that was split equally between urban and residential customers at 49 percent each, and had seasonal customers providing the remaining 2 percent of revenue. Does that sound like a reasonable outcome?

MR. LARLEE: Yes, it does.

DR. SOLLOWS: Okay. The split between rate features indicated that 15 percent of your revenue under the current rates came from the monthly service charge, 59 percent came from the first energy block and the remaining 26 percent came from the second or the runout block of energy.

Is that sounding like -- I was looking for a check here. These are the numbers that I got. And I just want to be sure that they are somewhere in the right ball park?

MR. LARLEE: Yes. I'm just looking at what we call our rate calculations in response to IR EGNB-11, IR-11 that we filed on February the 9th. And yes, those numbers are correct.

DR. SOLLOWS: Sounds good. Thank you. So -- now taking the 451 million as a revenue target, I -- to try -- just as you have indicated there are an infinite set of rates that you could come up with to satisfy your requirements, so I picked another one as a test. And I took the 451 million as the revenue target, I set a monthly service charge at $23 for all three residential classes, because I didn't really see anything in the cost allocation study that would allow me to differentiate.

I put the first block size at 800 kilowatt hours per month based on my own review of the consumption data by

knowledge that the block size would result in most of your customers being exposed to the second block price for their marginal winter consumption, which is I think what you had in mind when you said the base consumption was around 800, and it also -- it -- sort of in my mind was the notion that it represented a reasonable upper ground for monthly consumption of a residential customer that uses electricity for other than space heating. And that's from my own bill. I have a few electric baseboards but I'm largely in an old farmhouse that's nominally heated by oil but largely unheated, and I use 5' to 600 kilowatt hours in the -- 700 in the summer months and 1100, 1200 in the winter time. So that's how I arrived at the 800.

When I -- having done that, I looked at the extra revenue that I got from increasing all of the monthly service charges to $23 and I took that increment of revenue and reduced the first block rate from 8.37 cents to 7.71 cents to compensate for that increased revenue.

I simply said, well normally, I would anticipate that the first block rate would be higher because it's making up for any shortfall in the cost recovery from a lower than necessary service charge, so having put the service charge to cover 100 percent of its estimated cost I reduced the first rate down to 7.71 cents per kilowatt

hour.

Then I simply calculated the second block or the run out rate so that the $451 million would be generated. And I arrived at 7.21 cents per kilowatt hour.

When I checked the results I got the same revenue split between classes. I got 49 percent from urban, 49 percent from rural and two percent from seasonal customers. And the split between rate features showed a little more revenue coming from the service charge, 18 percent versus 15 percent under the current rate.

First block revenue fell substantially. It fell from 59 percent down to 40 percent of total revenue. And the second block revenue increased from 26 percent to 42 percent.

Now I would like you to leave aside the Board's December order which I understand prohibited you from doing what I have done, and I understand that, and leave aside for now the need to increase revenue and rate shock because we are going to deal with that a little later. And just answer the next question. Subject to checking my arithmetic, do you agree that this prototype rate design would be a reasonable option for Disco?

MR. LARLEE: It's not unreasonable given that you have asked me to leave aside considerations, the Board's ruling and

rate shock and --

DR. SOLLOWS: Yes.

MR. LARLEE: -- revenue requirement.

DR. SOLLOWS: Okay. And as I say there is nothing you can do about the Board's ruling.

MR. LARLEE: I guess the only comment I would have, because I do try to keep familiar with what other utilities are doing in their residential rates, is that the service -- this would be among the highest service charges in the country.

DR. SOLLOWS: That's absolutely clear, and I understand that. But I do want to --

CHAIRMAN: We will take our break.

(Recess - 10:15 a.m. - 10:35 a.m.)

CHAIRMAN: Any preliminary matters?

MR. MORRISON: No, Mr. Chair.

CHAIRMAN: Panel, I want to reassure you, as Commissioner Sollows has reassured me, that he is not putting this example in front of you to write a new dissenting opinion, but rather doing something that the Panel supports which is to try and get the best ideas out on the table and that you folks consider them and give us your opinion.

Go ahead, Commissioner.

DR. SOLLOWS: Thank you, Mr. Chair. Now I would like to

turn your attention to the impact of this prototype rate on the customers. To examine that I calculated the dollar amount by which each customer's annual electricity cost would change. And I rounded that dollar amount to the nearest $10.

I did that so that I would have in a statistical sense I would call a bin variable, and I got 206 different bin variables in that way, ranging from negative to positive. And the distribution was interesting to me and I want you to comment on some summaries -- as I summarize it here. And of course all your comments subject to checking, because this is the results of a calculation going through -- I don't know -- 300,000 customers times 12 invoices or something like that.

When I looked at that distribution I found there were basic groups under the new -- or the prototype rate. There was one group that I would probably call the winners and they totalled about 44 percent of all the customers. They would see their annual cost of electricity decrease by an average of $29 per year.

I found a group that I will call the losers. They were about 40 percent of customers. They experienced an annual cost increase of about $34 per year. And that's average for the whole group.

And the remaining 16 percent of customers who we would call -- I might call the indifferent. Probably they are indifferent to the two rates. Their costs would change by less than $5 either way.

What I am wondering is would you agree with me that the only customers that experienced cost increases, which I have called -- the 40 percent of customers that are going to see an increase in costs -- they would be the ones that are at risk of what we would call rate shock? Is that fair?

MR. LARLEE: Yes. I think I would agree with that. Just sort of looking at the rate and the way it is laid out, you really have two customers that are going to see significant increases.

You have got the very, very low-consuming customers because you have increased the service charge by $6 for your urban customers. And then you have got the very large customers.

DR. SOLLOWS: Right.

MR. LARLEE: So sort of at both ends of the spectrum. And the very large customers, just rough calculations, would be in the order of 9, 9 1/2 percent.

DR. SOLLOWS: Yes. Okay.

MR. LARLEE: So you have a got a revenue-neutral adjustment

with some customers seeing almost a 10 percent increase. I would say that you are approaching rate shock.

DR. SOLLOWS: Okay. So you think that a 10 percent increase does -- that this proposal would be rate shock?

MR. LARLEE: Well, keeping in mind sort of the criteria that Mr. Marois laid out yesterday, where your overall rate increase is zero. And then you have got some customers with 10 percent.

I think that's quite an extreme -- quite an extreme impact. You are telling customers well, we are not going to change your rates, but you may see 10 percent. I think that could qualify as rate shock.

DR. SOLLOWS: Okay. I think we probably have a very different definition of rate shock. But we will carry on. And I think you have sort of come to the point -- my next question was the urban customer with no energy use at all sees a fairly large percentage rate increase. I found it is $5.26 per month or just under a 30 percent rise in their bill. Does that sound right?

MR. LARLEE: Yes.

DR. SOLLOWS: Now I know that you have your view of what rate shock is. But I'm still struggling with the issue. And I'm struggling with the notion of whether that 30 percent rise is or is not rate shock.

Certainly on one hand it represents a 30 percent increase in the customer's cost for service. But on the other hand the customer used no energy. It derived no -- he derived or she derived no energy utility from the service. And the service actually cost 30 percent more than they paid under the old rate.

And on top of all of that, 30 percent rise is still only $63 per year for that customer.

So you have commented already that you think for the big customer it would be rate shock. Do you think that it would be rate shock for the small customer, that $63 per year?

MR. MAROIS: You probably appreciate that we are going to be very cautious and qualify anything as rate shock or not rate shock. I mean, that's why judgment comes into play. I mean, you have to apply judgment in terms of the circumstances.

And I guess where I'm struggling a little bit is you seem -- if I understand your argument, is that you are factoring load percentage increase and then absolute increase.

DR. SOLLOWS: Pardon me?

MR. MAROIS: What I understand you saying is when you look at the customers with little or no consumption, that the

absolute increase or dollar value increase is relatively small.

DR. SOLLOWS: Right.

MR. MAROIS: And you mentioned 60' --

DR. SOLLOWS: $63.

MR. MAROIS: Yes.

DR. SOLLOWS: That is 30 percent rise. But it is $63.

MR. MAROIS: I mean, if your criteria is absolute numbers -- maybe it is not. Maybe it is depending if you are looking at a small apartment for a low-income person. It could be significant or it could not be. So I guess it almost depends on your criteria.

But from a percentage increase it would raise eyebrows. And I mean, that's something we would take into account considering the circumstances at hand.

DR. SOLLOWS: Okay. As an example of those circumstances, perhaps the situation for Vice-Chair Nelson who -- I think he mentioned in passing that he used a few hundred kilowatt-hours a year at his cottage or his trailer at his vacation lot. He would be facing quite a substantial cost increase for that. He would be pushing the 25 or 30 percent range.

Is that in your judgment something that we would want to mitigate through some extraordinary measure? Or do you

think he should pay the full cost of service?

MR. MAROIS: That's a tough question. I mean, typically there would not be programs for a situation like that. Because I just got my tax bill for my cottage. And I don't like it at all. But I don't think I'm going to get any assistance, so --

DR. SOLLOWS: And so really when we come to mitigating rate shock I guess we are probably on the same wavelength here, is that we can't just look at the percentage rise. We have to look at the absolute amount, the affordability and a number of other factors, sort of the utility of the supply to the customer?

MR. MAROIS: Yes. And I mean -- and when we talk about circumstances, I mean, the theoretical exercise we are going through right now is a revenue-neutral adjustment. But usually when you look at rate increase, it's not in a revenue-neutral circumstance. So that --

DR. SOLLOWS: We are going to get there, yes. Thank you. So at the other end of the spectrum I found a residential customer with an annual electricity bill totaling $338,000 under the old or existing rate. That customer would experience a rise to 368,000. And that is about 8.7 percent.

Now if I understand you correctly, 8.7 percent rise

for that customer is rate shock. But a 10 percent rise for everybody is not rate shock.

Is that -- am I interpreting your interpretation -- have I got your interpretation of rate shock correct?

MR. MAROIS: I don't want to contradict Mr. Larlee. But I guess that's my -- I would stay away from qualifying anything as rate shock or not rate shock.

I believe yesterday my discussion with the Chairman was that when I personally look at gradualism or concern about rate impact it's really versus the average increase. I mean, if the average increase is legitimate, because you have to recover your cost, that is an increase you have to live with.

DR. SOLLOWS: But in this case there is no average increase. It is rebalancing the rate to achieve an objective that was set by your Board as part of your policy?

MR. MAROIS: Exactly. So that's when -- in that case, I mean -- and I believe that's what Mr. Larlee was getting at is 8, 9 percent, 10 percent increase, when you have a zero increase really overall, because it's a revenue-neutral adjustment, it raises questions. Is it rate shock or not?

But it's a significant increase for an adjustment that is overall revenue-neutral. Because I believe that -- and

these comments were not made by us, but they are part of evidence on the record, that some people seem to define gradualism or acceptable gradualism or acceptable impact as increases that are within 1.5 times to 2 times the average increase.

DR. SOLLOWS: Yes.

MR. MAROIS: And so I guess what makes it difficult in a revenue-neutral situation is your average increase is zero. So 2 times that is --

DR. SOLLOWS: Right. So that is the problem with the formula, isn't it?

MR. MAROIS: That's a problem, yes.

DR. SOLLOWS: Okay. So we agree that it is debatable. And it is really subject to judgment.

MR. MAROIS: I agree with that.

DR. SOLLOWS: Yes. And finally when I looked at the customers that were grouped by their change in annual costs rounded to the nearest 10, I found that the customers paying an extra $40 per year experienced the highest percentage change in their cost.

And that amounted to about a 10 percent increase. And again on the formula basis by definition, that is rate shock if you are comparing it to a zero change.

But would you agree with me that it -- it may be

reasonable to look at this and look at an overall goal of developing a flat or an inclining rate and say that a 10 percent increase, since that is really less than the average increase you are asking for, from a customer's perspective the reason you do it is less important than the fact that they will pay 10 percent more.

And therefore it might be reasonable to conclude that 10 percent increase wouldn't be rate shock?

MR. MAROIS: Well, I guess that's where personally I'm struggling. Because I have got difficulty detaching myself from the current situation where we know we have an average increase of --

DR. SOLLOWS: I understand.

MR. MAROIS: -- over 11 percent. And then if you add to that a 10 percent adjustment, now you are into 20 percent. I mean, if I understand your question is if the change you are trying to make is a right one, and really at the end of the day has merits, and if you were facing a zero overall increase, would 10 percent be acceptable? I would almost have to agree, yes.

DR. SOLLOWS: Okay. Thank you. Now I would turn you to a comparison between this prototype rate and the existing one. Now I understand neither rate is designed to deliver the revenue requirement for the test year. But again to

keep things clear I want to deal with that a little later.

The difference between energy price in the first and second blocks of the current rate is 1.74 cents I think, isn't it?

MR. LARLEE: Yes. That's correct.

DR. SOLLOWS: In the prototype rate the first block is price at 7.71 cents. And the second block is priced at 7.21 cents per kilowatt-hours, the difference being a half a cent a kilowatt-hour.

Would you agree with me that the prototype rate would make greater progress towards the goal of eliminating the declining block rate structure than the one you have proposed?

MR. LARLEE: Oh, absolutely. The one we have proposed is in compliance with the Board ruling.

DR. SOLLOWS: Fair enough. Thank you. Now I want to consider Disco's need for additional revenue for the test year. Assuming that we find there is a need for revenue over and above that which the prototype rate would provide, do you agree that increasing only the second or runout block energy price by up to .5 cents per kilowatt-hour would increase Disco's revenue and close the gap between the first and second block rates?

MR. LARLEE: Yes, it would do both those things.

DR. SOLLOWS: And if the second block was increased by more than .5 cents per kilowatt hour, either all at once or in a series of smaller steps -- do you agree that an inclining block rate would result?

MR. LARLEE: Yes.

DR. SOLLOWS: Okay. Now when I looked at it, the second -- or the run out block of the prototype rate contained about 2656 gigawatt hours for the 2005 fiscal year. And half a cent a kilowatt hour is $5,000 per gigawatt hour so my rough calculation is that increasing that run out rate by a half a cent reveal an extra $13.3 million in revenue for Disco. Subject to check, does that sound about right?

MR. LARLEE: Could you repeat the revenue number again?

DR. SOLLOWS: 13.3 million. That is 5000 times 2656. And again, of course subject to check that I have done the sums right.

MR. LARLEE: Sure. Subject to check that looks about right.

DR. SOLLOWS: Now, Mr. Marois, your evidence indicates you proposed to need an extra 59.2 million from residential customers to move your residential customer class from revenue cost ratio of 84 percent to 95 percent. And that is a total of 11 points. Is that right?

MR. MAROIS: Yes, that is correct.

DR. SOLLOWS: Thank you. So if my arithmetic is correct and

assuming that you don't use any of your -- what I am going to call waterfall profits from this year to offset the rate shock -- an extra 2.22 cents per kilowatt hour added to the second block price would meet your revenue target for residential customers. And we are going to talk about rate shock and I certainly understand that this would induce rate shock. But you accept that that number, subject to check, would meet your revenue target? That basically the 56 million divided by 13.3?

MR. LARLEE: So just so I have it clear in my own mind, how much energy did you calculate you had in the end block?

DR. SOLLOWS: In the end block it turned out to be 2656 gigawatt hours. And when I added I did it on the basis of a half cent, the difference between the two rates, I got 13.3 million in revenue. And when I divided that into 59.2 I got about 2.22 cents. MAybe I am wrong.

MR. LARLEE: I just can't do that much math in my head so --

DR. SOLLOWS: I didn't either.

MR. LARLEE: Yes, 2.2 cents.

DR. SOLLOWS: Thank you. So to summarize, this would leave us with an inclining block rate with a service charge of $23 per month, a rate of 7.71 cents per kilowatt hour for the first 800 kilowatt hours of monthly consumption and a second rate block or a run out block rate of 9.43 cents

per kilowatt hour for energy in excess of 800 kilowatt hours per month. Now do you agree with me, subject to check, that this rate will probably deliver your revenue requirement but will also raise the problem of rate shock for some of your residential customers?

MR. LARLEE: Yes.

DR. SOLLOWS: Okay. Now just for the purposes of this question leaving the rate shock aside, assuming we can address it in some manner, is this prototype inclining block rate design practical from an implementation perspective for the company?

MR. LARLEE: When you say practical, are you referring to would Disco be able to actually bill it?

DR. SOLLOWS: Yes. Would you be able to implement this if we could find some way to emoliate the issue of rate shock for those customers that would face real hardship by implementing such a large increase -- as you have seen the big -- after this the big increase would be for large users and they would be very large increases for the largest users. So assuming that we could find some way to deal with that, would this type of design be a reasonable thing or a practical thing for you to implement?

MR. LARLEE: Well it would certainly be practical to implement it. I mean, there is no -- there is nothing

here that our billing engine couldn't handle. And as far as reasonableness of it, again I go back to this idea is one of the reasons why we did that segmentation cost allocation study is I think we would want to look at sort of directionally where that takes the electric heat and non-electric heat customers from a cost recovery basis just to make sure that we're getting reasonable results there.

DR. SOLLOWS: And I understood conceptually the 800 kilowatt hour base does a lot to segregate the two customers so really what this would do would shift revenue collection from smaller customers to higher customers, higher usage customers and those tend to be electric heat customers?

MR. LARLEE: That's correct.

DR. SOLLOWS: So now rate shock. If we wanted to implement this design, what are the various options available to us to mitigate rate shock. And the understanding that I have is that the largest customer that we are talking about would see a huge increase. I mean, they would be I am guess 30, 40 percent increase, which by anybody's definition is rate shock. But there aren't very many of these really large customers so the cost of dealing with it might not be prohibitive with this particular rate design. Again because the basic rate design started by

decreasing half the people's rates by a little bit. So I'm wondering if any of these would be possibilities in terms of -- well, I guess first off what could we do with this rate design to mitigate the rate shock?

MR. LARLEE: I think the first thing that you would do to get to this type of rate is you would do it gradually. And the Board's order in eliminating the declining block rate by one-third in this particular rate proposal gets us on that road to getting it obviously.

You know, I think you should get to a flat rate before you get to an inclining block rate. And the Board's order certainly gets us a long ways to some type of rate structure similar to this.

DR. SOLLOWS: Okay. So basically move to this more gradually would be one way of dealing with it?

MR. LARLEE: Yes. That's correct.

DR. SOLLOWS: One way of moving to it gradually would be to move more slowly towards a revenue-cost ratio of .95. I'm thinking back to your own Board's order to move to a revenue-cost ratio of 1. But they gave you five years to do it.

So I'm wondering if we could perhaps move -- instead of moving from .84 to .95, if -- would it tend to eliminate the rate shock if we moved you from .84 to --

oh, let's say .9?

MR. MAROIS: Well, I guess what would have been my opening comments to your question was it's communicating -- I mean, if you try to minimize rate impact to one rate class, with the example you just gave, you have got to look at, okay, who else is going to pay more?

DR. SOLLOWS: Right.

MR. MAROIS: And that is where you start into the balancing.

DR. SOLLOWS: Yes.

MR. MAROIS: And that's -- and I think I stressed that our rate proposal tried to do just that, is balance. And I mean, right now we are in a situation where it's tough because of the average increase.

The balancing, you don't have that much flexibility. So if you reduce the overall increase to the residential rate class because you are doing rate design changes, another rate class will have to bear --

DR. SOLLOWS: I understand.

MR. MAROIS: -- the cost.

DR. SOLLOWS: But nonetheless the subject of that consideration, moving more slowly towards the target of 100 percent, would be one way of addressing issue of rate shock for this class?

MR. MAROIS: Yes. But then you are defeating the purpose.

Because you are redesigning the rate to have really better pricing.

DR. SOLLOWS: Yes.

MR. MAROIS: But then you are recovering a smaller amount of cost. So you are getting faster to better rate design. But you are recovering less cost. So which one is better?

DR. SOLLOWS: Yes. I guess from a purely -- you know, from a more abstract perspective that I would bring to this would be -- I'm wondering if it isn't better to get the rate design correct because that is the information that you are going to transmit to the customer in the long term to affect their consumption. So if we get that design right you might see sufficient changes in customer behavior that your costs go down. And it might make further progress towards the revenue cost ratio of one, by their adaptation.

So that is one of the reasons why I would say I'm looking at the pricing side rather than the revenue cost side.

MR. MAROIS: There is always two sides to every coin. And I guess I would potentially argue that -- true, but the pricing though that you have just described, if you are not recovering the right amount of cost, is really an intrarate pricing.

But if the overall residential rate class is at least recovering more of their cost, i.e. like at 95 percent, at least the overall pricing of the residential rate class is better. So which one is better?

DR. SOLLOWS: Certainly it is a judgment call. And I certainly wouldn't propose leaving the revenue-cost ratio where it is. But we could move more slowly to deal with rate shock.

If the customer -- if the shareholder felt that rate shock was an issue, do you suppose a shareholder holding this kind of monopoly should be asked to maybe invest some equity in eliminating or muting rate shock, as long as we are transitioning to a goal that is consistent with their goals?

MR. MAROIS: Well, I'm not certain I understand you are talking about -- equity. But my understanding -- and again this is based on publicly available information -- is what the government is looking at right now is notwithstanding even doing an adjustment to raise the way you are mentioning it, but just to help offset some of the impact of the rate proposal as proposed by us, is they are looking at their own measures.

DR. SOLLOWS: Okay. So we can perhaps have some confidence that even if we adopted a rate like this, the largest

customers that were subject -- in the class that were subject to the worst rating cases, they might well be taken care of by government.

MR. MAROIS: I don't know if we have some confidence. But it's definitely a possibility.

DR. SOLLOWS: Okay. Thank you. Is there any merit to allocating some of the windfall or waterfall revenue that you have got from the high water flows and low and unusually warm winter -- warmest on record I guess according to Meteorological Service of Canada -- is there any merit to taking some of what is essentially a windfall or waterfall profit and using that to mute the rate shock or ameliorate the rate shock for these customers with extreme increases?

MR. MAROIS: Well, I think it's a tough question for me to answer. Because I mean, I don't think we have conceded by any means that it would be appropriate to take money from one year to help offset.

DR. SOLLOWS: I understand. And I would be reluctant --

MR. MAROIS: But in theory, I mean, in theory if that money was to be used to offset rate increase then it creates more flexibility, flexibility we don't have right now. But I mean, a word of caution I want to give right now is even if everybody would agree that the Board has

authority to create variance accounts for hydro for the current fiscal year, and if the conclusion was that the Board is able to create those accounts and is able to take that money to help offset costs, what the Board has just done is implemented a means that we can recover any shortfall from hydro.

So next year, if we come back with the exact reverse, we are going to go out to the market and say we need a 10 percent rate increase because our water is too low.

So what's important here is our costs, our revenue requirement, the rates we are going to set are ongoing. Unless something changes we need those rates every year. Like you mentioned, the additional hydro profit of last year is a one shot deal.

DR. SOLLOWS: Yes.

MR. MAROIS: So you have to be really careful not to correct a long-term problem with a nonrecurring one-time --

DR. SOLLOWS: I agree.

MR. MAROIS: So that's why I'm very nervous, but --

DR. SOLLOWS: I tend to make people nervous.

MR. MAROIS: If you could find money -- the problem we have right now, and usually it's the case when you do rate design or you set rates, is you don't have much flexibility.

I mean, if you had the flexibility of increasing one rate quite a bit more to help address the problem in another rate, then you can have all sorts of flexibility.

But in this case in particular we have very small flexibility. So that's why the balancing act is --

DR. SOLLOWS: I understand.

MR. MAROIS: -- so difficult.

DR. SOLLOWS: Okay. I think I would like to just leave that there and go on to another line of questioning if that is okay.

I'm going to talk now briefly about small industrial rates. And by now you know that I have spent some time crawling through the database that you provided.

And when I examined the billing data for small industrial customers it revealed 22 customers for whom the recorded actual demand was less than zero and the largest of which was about minus 290 kilowatts. And this is again small industrial customers, not the large ones. How does a negative demand arise in the billing data?

MR. LARLEE: I don't know. I would have to look at those particular accounts and see what is happening.

DR. SOLLOWS: Okay. It just seems like an interesting anomaly to me. Could you undertake to do so?

MR. LARLEE: Yes.

DR. SOLLOWS: Okay. Thank you. The same examination also revealed 252 customers for whom the load factor was greater than 100 percent, and who had not recorded any purchases of surplus or interruptible energy.

My question from that is how do load factors above 100 percent arise?

MR. LARLEE: Again on those customers I don't have the details but I can look into it.

DR. SOLLOWS: I would appreciate that. Thank you. When I eliminated those two groups for purposes of my analysis I then examined the load factors of the remaining, and it sort of grouped into three different groups that comprised about 84 percent of your energy sales. So I think the resulting analysis, even though I have had to eliminate these ones, probably captures most of your -- most of your small industrial rate customers.

I found that there were three groups when I grouped them by load factors. I had one group that had a load factor of 19 percent plus or minus nine percent. I had another group that was 36 percent plus or minus 20 percent. And I had a third group that was 41 percent plus or minus 15 percent. And just for the sake of completeness there was another group with a seven percent load factor but it used less than two percent energy, so I

left it off the consideration.

There was also a small group of outlyers that consumed less than one percent of the energy and 60 percent load factor. So again really leaving those aside, I want to focus on the main three groups.

Have you examined your rate design regarding intra-class equity to ensure that the revenue cost ratios for these three subgroups, which are not unlike subgroups that you found in the residential rate, are the revenue cost ratios for these three main groups within a reasonable range of values, or is there some intra-class subsidy from the high load factor group -- higher load factor group to the lower load factor group?

MR. LARLEE: No, I haven't, but I think it's important to note that because this is a two part rate, a demand charge and an energy charge, that customers with lower load factor, in other words have a higher demand relative to their energy consumption, pay a higher cents per kilowatt hour rate.

DR. SOLLOWS: I understand that and I guess what I'm looking -- asking and if you haven't done it I'm just wondering if you could do it and report at some future date, not as an undertaking in this hearing -- undertake the analysis to see whether you have struck the right balance in the

demand charge and the energy charge in order to eliminate any -- to the degree that you can with the rate structure you have eliminate any subsidy from the high load factor customers to the low load factor customers, or to limit that subsidy to an appropriate value, if you think it should be one?

MR. LARLEE: I think I mentioned yesterday that the best way to do that would be to just examine the costs that are coming out of the cost allocation study, and when I say the costs I mean the customer costs, the demand related costs and the energy costs, and compare those to the rate. And then based on that make sure that the rate is in line with those costs.

DR. SOLLOWS: So you could do that?

MR. LARLEE: I think that's something that could be readily done.

DR. SOLLOWS: Thank you. Now prior evidence in the hearing that led me to believe that industrial customers had characteristically high load factors, but these results seem contradictory. The highest load factor group is 41 percent, plus or minus 50 percent, that represents 49 percent of your sales to the class.

Now the difficulty I'm having is 41 percent load factor is somewhat like the load factors we had for

residential, is it not?

MR. LARLEE: Yes, it is. But unfortunately I think when we -- a lot of times when we talk about industrial, depending on the context, we are really talking about the large industrial customers, those 40 or so customers that are on the transmission system, and most of them, not all, but most of them do have quite high load factors.

DR. SOLLOWS: Okay. So I will accept that. And I did just want to note though that there is a difference between these load factors in that these are monthly load factors, or the average monthly load factors, and under your cost allocation study you are looking at annual load factors. And so I guess you would agree with me that for a given customer their annual load factor -- the upper limit value it could be would be the average of the monthlies, is that right?

MR. LARLEE: Yes, that's true.

DR. SOLLOWS: So really this is a -- this is -- it's a conservative comparison, but what you have clarified is when you referred to high load factor loads you are really talking about large industrial loads?

MR. LARLEE: Yes.

DR. SOLLOWS: Thank you. So I can eliminate that. Now I haven't done this calculation and I propose that I will do

it, but are you fairly confident that if I just sort of looked at the overall load factor that I found for your small industrial customers and compared it to the number that you have used in your cost allocation study that it would be the same?

MR. LARLEE: Well it wouldn't be the same as you pointed out that you are looking at monthly load factors and in the cost allocation study.

DR. SOLLOWS: Okay. I will -- what I will do is actually calculate the annual for each customer and average that. Would I get then a number that's comparable to what you have used in your cost allocation study?

MR. LARLEE: You should get a comparable number because we based those estimates on our billing analysis which is essentially what you have been doing.

DR. SOLLOWS: Perfect. Thank you. Now large industrial rates. When I did the analysis of large industrial rates I also found three groups of customers. I found a group consisting of 26 percent of your customers that together consumed five percent of the class energy and had a load factor of 46 percent. I found 45 percent of your customers consuming little more than half of your energy, 54 percent of your energy, with a load factor of exactly the same actually, 54 percent, plus or minus seven.

And I found that 26 percent of your customers, or about a quarter of them, consumed 41 percent of the energy, and they had a load factor of 84 percent.

Now I guess based on what you said so far you would agree with me that the third group, the one with an 84 percent load factor, represents a high load factor group of customers?

MR. LARLEE: That's correct, yes.

DR. SOLLOWS: And the small standard deviation, it was 84 percent, plus or minus seven percent, that's also something that makes this a collection of pretty good customers, right? It's not only a high load factor, it's a fairly constant load factor?

MR. LARLEE: That's the function of their load. It's a constant load. Most of them are continuous process operations running 24/7.

DR. SOLLOWS: So they are better customers in this respect than the first group which had a 46 percent load factor and was 26 percent of your customers, about the same percentage of customers but a 46 percent load factor. Those -- that quarter of your customers -- the high load factor group is certainly better than the low load factor group.

Again have you examined the rate design to ensure that

the large ones with the high load factors aren't subsidizing the ones with the low load factors?

MR. LARLEE: And again the rate -- it's a two part rate. So as a result low load factor customers pay a higher cents per kilowatt hour --

DR. SOLLOWS: Yes.

MR. LARLEE: -- so that there is basically the rate -- a two part rate is designed to track the cost, and the cost is a relation of demand cost and energy cost. So no, I haven't done that.

DR. SOLLOWS: Could you put the revenue cost ratios on the record for those three groups?

MR. LARLEE: I'm not sure that I would be able to segregate the cost allocation study along the lines that you have described.

DR. SOLLOWS: Well I can give you the identity numbers that are on the data base for the group members.

MR. LARLEE: I think really -- and what I was proposing before is is that we can look at what the cost allocation study tells us the costs are on a demand basis in dollars per kilowatt, and in energy basis. And we can compare those to what the rate is and that would give us --

DR. SOLLOWS: So if I gave you then the average demand and average energy of each of these groups you could do a

revenue cost ratio on that basis?

MR. LARLEE: Essentially I guess what you are saying is if you had the billing determinates --

DR. SOLLOWS: Yes. Which we do.

MR. LARLEE: -- then -- but I'm still not clear on what you would be using as a segregating point? I guess what I'm trying to get at is that -- I mean, a two part rate you are already taking into account variations in load factor. So all that's important is that your demand charge and your energy charge actually track cost.

So there is no reason then to do a segregation upon load factor because your rate design is already taking that into account.

DR. SOLLOWS: And I guess all i'm looking for from the point of view from an auditor is a check and that the check would be since your customers have these different characteristics in their groups, I would want to be sure that these groups are covering their own costs and there is no intra-class subsidy from say the high load factor group to the low, and it would be just a check on the rate design.

So I guess that's my reason for asking and I'm wondering if we gave you the numbers you would be able to do it?

MR. MORRISON: Excuse me, Mr. Chair. I have no problem with the information request. Mine is more a practical concern in that I don't know how long it is going to take to do whatever it is required to be done, and the record will close here soon, so --

DR. SOLLOWS: I guess I'm not -- the same as I had for the small industrial. This wasn't really for this record. It was for, you know, a report at a future date.

MR. LARLEE: My only concern is I guess from the revenue side it doesn't sound like there would be an issue, but it's the cost side that there may be some difficulty in doing this segmentation.

I mean, I would propose really what we would look at again is examining the demand and energy costs, compare that to the rate components, and if they are in balance then they are, and if they aren't they aren't.

DR. SOLLOWS: Okay. So we will perhaps leave this for a later working group or something.

Now that's the extent of my questions. Thank you very much.

CHAIRMAN: Those are all the Panel's questions. Mr. Morrison, do you have any redirect?

MR. MORRISON: No, Mr. Chairman. Thank you.

CHAIRMAN: Okay. Well thank you gentlemen for your

testimony and you are excused.

MR. MAROIS: Thank you.

CHAIRMAN: Mr. MacNutt, while the witnesses are standing down could you refresh my memory as to where we go from here?

MR. MACNUTT: It's my understanding, Mr. Chairman, that EGNB has a witness Panel of two persons who would be sworn and give evidence, to be followed by a cross examination, et cetera. Then Mr. Knecht would be sworn on behalf of the Public Intervenor.

CHAIRMAN: Thank you, Mr. MacNutt. You can move up, sir, once the stand is vacated.

SHELLY BLACK and ANDREW HARRINGTON, sworn:

DIRECT EXAMINATION BY MR. MACDOUGALL:

MR. MACDOUGALL: Good morning, Mr. Chair, Commissioners. I believe the panel has just been sworn by Ms. Legere. What I would do is just introduce the panel to you, then we have some direct examination. As part of the direct examination there will be a couple of references to some of the graphics or the charts in the written testimony of the panel. So I think it may be useful for the panel to have EGNB-4 in front of them during the direct, which is the written direct testimony of Andrew J. Harrington and Shelly L. Black. There is only a couple of times that the

witness will reference it, but there are a few graphics that are useful for the panel to go to.

Also as part of our direct examination we will be doing a little bit of rebuttal, primarily in response to questions raised I believe by Commissioner Dumont and the Chair which were addressed to Dr. Rosenberg regarding incentives, and you will recall we had suggested that -- I believe Dr. Rosenberg himself had suggested that this panel would be better prepared to answer those questions. So we will try to address some of that issue in our direct examination.

CHAIRMAN: You are probably going to have to remind me what those questions were, Mr. MacDougall.

MR. MACDOUGALL: Sure. They were in relation to incentives available for conversion, Mr. Chair.

Q.1 - Mr. Harrington, your curriculum vitae is attached at Schedule I of EGNB-4, correct?

MR. HARRINGTON: That's correct.

Q.2 - And could you just for the record indicate your position with Enbridge Gas New Brunswick?

MR. HARRINGTON: I am the general manager of Enbridge Gas New Brunswick.

Q.3 - Thank you. And, Ms. Black, your curriculum vitae is attached as Schedule II to your direct evidence, correct?

MS. BLACK: Yes, that's correct.

Q.4 - And could you just indicate for the record your position with Enbridge Gas New Brunswick?

MS. BLACK: I am mthe anager of regulatory affairs and gas supply.

Q.5 - Thank you. And, Mr. Harrington, was this evidence prepared together with Ms. Black under your direction and control?

MR. HARRINGTON: That's correct.

Q.6 - And, Ms. Black, you also assisted in the preparation of this evidence?

MS. BLACK: Yes, I did.

Q.7 - And there is no changes or revisions to the evidence, correct?

MS. BLACK: No, no revisions.

MR. HARRINGTON: No.

Q.8 - And, Mr. Harrington, do you adopt this as your evidence in this proceeding?

MR. HARRINGTON: Yes, I do.

Q.9 - And, Ms. Black, do you adopt this as your evidence in this proceeding?

MS. BLACK: Yes, I do.

MR. MACDOUGALL: Thank you very much. Mr. Chair, we will now just go to the direct and as I say we do raise some

questions in -- along the lines of rebuttal and response to certain issues which will just be part of the direct examination. I believe Mr. Harrington will probably be responding primarily in direct with the ability of the panel as a whole to be dealt with in cross examination.

Q.10 - Mr. Harrington, could you please explain to the Board the general reason why you have filed your evidence in this proceeding?

MR. HARRINGTON: EGNB's evidence first profiles the implications of Disco's proposal from an inter-fuel competitiveness standpoint. It then discusses broader societal implications and makes very specific suggestions as how to limit these implications.

In the final analysis we are here to ensure that proper price signals are being sent and that competitiveness is being encouraged, both of which goals we believe are consistent with the government's Energy Policy and in the general public interest.

Disco's proposal unfortunately continues to send incorrect price signals to the market, which adversely impacts the competitive energy suppliers in New Brunswick.

Electricity customers, the New Brunswick Power Corporation, including Disco and the New Brunswick taxpayers, as well as the environment.

Q.11 - Mr. Harrington, why is sending correct price signals in your view so important?

MR. HARRINGTON: Price signals motivate customers to alter behaviour. Disco's current price signals encourage New Brunswick residents and businesses to choose electricity for 100 percent of their energy requirements. Additionally there is little incentive to conserve as the price signal indicates that the more you consume the lower the average electricity rate. Correct price signals would motivate electricity customers to conserve and possibly even convert part of their electricity requirement to a more efficient energy source. This would result in positive impacts to the environment and foster a competitive energy market in New Brunswick.

Q.12 - Could you please explain the environmental impacts of sending inappropriate price signals?

MR. HARRINGTON: The generation of electricity to meet the heating demand in New Brunswick is an inefficient use of fossil fuels. This has serious negative environmental consequences both from an efficiency and emission intensity perspective.

From an efficiency perspective, and considering a residential electric heating customer as an example, 70 percent of the primary energy used to generate electricity

on a high heating demand day is lost before it reaches the home. Only 30 percent of the primary fuel reaches the home in the form of heat. Compare this to natural gas, where on average more than 92 percent of the energy is converted to heat. This results in not only more fuel being consumed than necessary, but higher emissions as a result of the type of fuel being consumed. This same home using electricity to meet its heat and hot water requirements, will generate 20 tons of greenhouse gasses annually. Converting one home from electricity to natural gas reduces the emissions by 15 tons, a 75 percent reduction, and the achievement of 15 one ton challenges for New Brunswick. These improper price signals are actually discouraging conservation and efficient energy usage by continuing to incent New Brunswickers to use electricity for their space and water heating requirements. This price signal makes no sense from a policy, conservation, efficiency or cost perspective.

Q.13 - Mr. Harrington, could you now please describe the possible impact on a GS II customer who decides to switch some of their load from electricity to natural gas?

MR. HARRINGTON: A GS II or all-electric customer who converts a portion of their energy requirements from electricity to natural gas will be penalized by being

switched to the higher-priced GS I rate for the remaining electricity requirements.

Using the real life example of an office building found in EGNB exhibit 4 on page 5, and you don't have to turn there right now, this type of customer is one we can easily understand.

If this customer could convert their heat to natural gas without the perverse impact of having the rate applied for the rest of their electricity requirement increased to GS I levels, they would actually enjoy a savings of $36,100 annually or 22 percent of their energy requirements for heating.

Instead due strictly to the promotional nature of the GS II rate and the fact that it penalizes customers who do not use electricity for 100 percent of their energy requirements, this customer will find that their overall energy costs would increase by $7,600 or 6 percent annuall if they switch.

This is due to the fact that their remaining heating requirements for electricity, lights, fans, et cetera has increased to $43,700 or 8 percent annually because they haven't switched to the GS I rate.

Due to this penalizing price signal this customer will choose to continue using electricity for 100 percent of

their energy requirements, and as a result continue emitting 938 tons of greenhouse gases to our environment annually.

Q.14 - Mr. Harrington, could you now indicate why you believe it is important to close the GS II rate to new customers at this time?

MR. HARRINGTON: EGNB is unable to determine any public interest being served by the continued availability of this rate. The GS II rate results in the avoidance of all of the benefits to the end users, Disco and the environment.

EGNB cannot stress enough the importance of removing the penalty in combination with closing the GS II rate to new customers to sotp the bleeding.

Closing the GS II rate to new customers has a transition phase. And removing the penalty for customers who seek alternate fuel sources will eliminate future discrimination.

Q.15 - Could you now please explain the consequences with respect to new construction in the residential and GS classes of sending an incorrect price signal?

MR. HARRINGTON: The implications for new constructions are even more problematic. There are three additional impacts that must be considered with respect to the new

construction market.

First some prospective commercial customers, due to the nature of their operation or circumstance, are not able to take advantage of the promotional all-electric rate for their entire energy needs. So this rate is discriminating against customers without any cost of service differentiation.

Second, the availability of both the GS II rate and the continuance of the declining block residential rate promotes the continued cross-subsidization of heating customers by non-heating customers within their own respective classes.

Finally, these incorrect price signals are creating permanent barriers in the market by the continued use of electric baseboard heaters.

The majority of new construction clients, either residential or commercial, who build to use electricity for heating, use electric baseboard heaters due to their low initial installation cost and the existence of the GS II rate and the declining block feature of the residential rate.

Future retrofit cost to switch from electric baseboard heating to an alternate fuel are high and may prevent these customers from moving away from electricity in the

future.

If proper price signals are not introduced the impact on the new construction market will most likely be permanent. And future development in new construction will not change.

Q.16 - Could you now please explain the impact of the price signals that Disco is creating with its proposal in your view?

MR. HARRINGTON: Disco's proposal will result in the following five impacts. 1) Disco will face increasing demand for electricity which will require further investment in its infrastructure and additional cost to ratepayers. 2) Disco will face continued underrecovery from rates to meet the heating requirement, resulting in revenue deficiencies or more pronounced cross-subsidy. 3) investments made in incremental transmission and distribution infrastructure will make insufficient contribution to the New Brunswick economy unless Disco is allowed to earn on a commercially appropriate capital structure. 4) no distributed generation or any private generation will be undertaken as developers will quickly realize that they cannot compete with the subsidized rates. 5) energy providers will continue ignoring market segments dominated by electricity.

In addition to these points, please refer to the illustration on page 9 of EGNB's evidence, that is EGNB exhibit 4. This chart illustrates the end use cost faced by consumers as a function of their increasing heating requirement using existing and proposed residential rates. As a customer consumes more electricity for their heating requirements, the price of the electricity per unit actually decreases. The price signal being sent through both the current and proposed Disco rates is not one which promotes efficiency or one which encourages electricity customers to conserve and/or displace part of their electricity requirement with alternate energy choices. In fact it promotes quite the opposite behaviour. The price signal to encourage heating with electricity remains.

Q.17 - Could you now please comment on the impact of Disco's proposals for competitive energy suppliers?

MR. HARRINGTON: Energy providers will continue ignoring market segments dominated by electricity. In EGNB's case, we will be less likely to expand in the neighbourhoods with a preponderance of electrically heated homes. As a result, three obvious implications will occur.

One, there will be limited investment. There will be less economic growth from private return on equity. Less

of the same from the related industries and there will be corresponding impacts to employment and trade development. Two, there will limited choice. When and if the proper electricity price signals do exist, customers will not have the choices as the investment necessary for alternate energy providers to service them have not been expanded. Three, there will be increased costs. Costs for alternate energies will remain higher than otherwise, because economies of scales could not be achieved, placing an unwarranted burden on those end users who cannot or choose not to use electricity to meet their energy requirements.

Q.18 - Nr. Chair, the next couple of questions, as I say, go to the issues of incentives that were raised with respect to conversion.

Mr. Harrington, in your experience, what are the key factors considered by customers when contemplating conversion to natural gas?

MR. HARRINGTON: Customers typically consider two main factors. The capitol cost of converting existing equipment or purchase of new equipment and the ongoing operating cost.

Several types of incentives exist, such as private

incentives. Those from EGNB, for example. In addition to provincial, federal and even in some cases, municipal incentives are available to help customers convert their hot water and space heating requirements. These incentives are designed to help customers manage their costs to convert or purchase new equipment and may additionally include rebates or long-term financing.

When comparing the operating costs of natural gas heating equipment versus electric heating equipment, the current price signal is clear. Heating with electricity costs less than natural gas or oil, particularly when a customer qualifies for the anti-competitive GS II rate.

In the absence of proper price signals, incentives aimed at reducing or managing the capital cost will not be effective. To the extent that these prices signals are not corrected, it will limit the opportunities for energy providers, such as Enbridge Gas New Brunswick, and the choices available for New Brunswick.

Q.19 - Now, Mr. Harrington, your evidence speaks a lot about sending adequate price signals and the consumers will modify their behaviour in accordance with these signals. How realistic is it that consumers will be able to respond to price signals and convert from electric usage since that response involves capital costs to convert to another

energy source for heating?

MR. HARRINGTON: It's very realistic. First, people will respond in a variety of ways, not all of which require high capital costs, but will have the joint benefit of lowering costs for both Disco through lower generation costs, and for the consumer through lower end use consumption.

For instance, the U.S. Department of Energy has indicated a homeowner in a climate similar to New Brunswick's could reduce their energy requirement for heating by up to 10 percent through the simple installation of an Energy Star thermostat. This would have a capital cost of less than $100 and would be paid back almost instantly.

Second, let's talk about price signals that end users cannot respond to, increases to the monthly charge and increases to the rates applied for the first few hundred kilowatt hours per month. Sending price signals here has no market effect at all. There are measures like Energy Star appliances and compact florescent lighting that customers can install to reduce energy in the front block. Although it's important to note that all of these measures have less effect in electrically heated homes.

The point here is where there is discretion increases

should be directed toward those aspects of the rates where end users will be able to adjust their behaviour, such as in their heating requirements, as opposed to those aspects of a rate where they will not. This will result in benefits to all electricity end users.

Third, let's be really clear. Capital costs or other customer concerns are only a barrier once the proper price signals are in the market. If the argument underpinning the question is that perspective capital costs incurred by an end user to respond to price signals will prevent conversion, therefore there should be no price signals, then I would say you are putting the cart before the horse. From the outset, Disco said it was an objective to send the correct pricing signals into the market. EGNB agrees completely.

Finally, pricing signals will and do work. This is undeniable. Markets do respond. A few examples will illustrate this.

Under EGNB's proposal for Disco residential rate, end users would be able to save enough annually on their heat and hot water if they switched to natural gas to pay for the conversion out of savings. If there was additional certainty about the progressive elimination of the declining block, EGNB would immediately be able to

penetrate the residential central heating retrofit segment, illustrating a better than 7 year pay back period. An all year cost of conversion would be paid out of savings. Under Disco's proposal this would not happen.

For the second example, I want to talk about my experience in the Ontario market. When I first started working in the gas industry, one market opportunity which was being worked on was the elimination of all electric areas. These were geographic areas where home builders were forbidden to use other forms of energy in the homes they built. The homes were built using electric baseboard exclusively. During a very rare spurt of prudence, Ontario Hydro adjusted its residential rates up significantly and removed this all electric barrier for these areas. At very high initial capital costs to the homeowners, these homes were almost immediately converted to natural gas. While very historic now, I would venture to say that these homes and there were large numbers went from being 100 percent electric heat to 100 percent natural gas within a year or two. The demand was absolutely incredible.

For the final example, which really isn't an example, more of an example in weighting. I will profile a joint initiative between Enbridge Gas New Brunswick and the

provincial government, wherein together we approached the federal government under a national program called the Opportunities Envelope. EGNB and the Province successfully acquired $4.4 million, more than any other applicant, for a number of off electric programs aimed at reducing greenhouse gases. EGNB and the Province are unable to spend the vast majority of these dollars because of NB Power's anti-competitive rates.

For example, there are programs worth $1 million aimed at commercial customers. Unless the penalty aspect of the GS II rate is eliminated, this will not get spent. To be really clear, even if you provide conversion for free to an end user, they will not convert if the ongoing cost implications are negative.

There are multiple points here. First, this application, the one to the Opportunities Envelope was so successful, and as a blueprint I believe for the future, because Disco's winter electricity is so dirty from a greenhouse gas perspective, the federal government will invest heavily in end users who reduce the demand for this dirty electricity. I believe there is no opportunity like this anywhere else in Canada.

Second, if these programs do not get used by March 31st 2007, the investment opportunity will be lost and

40,800 tons per year will still be emitted.

Finally, I guarantee that 100 percent of the funds for this program reference will be spent as soon as the penalty is lifted because customers will respond to the price signals and EGNB, the provincial and federal government will be there to assist them.

Q.20 - And Mr. Chair, just before -- a couple of wrap up questions. There was one question I want to raise in response to remarks made by Mr. Marois. One of EGNB's recommendations is to allow existing GS II customer, who switch part of their energy requirement away from electricity to another energy source to remain on the GS II rate for their remaining electricity requirements. On direct Mr. Marois stated that Disco could not support this for equity reasons, citing that if this recommendation were accepted there could be two identical non all electric customers who are paying different rates. Did this equity concern raised by Disco cause EGNB to reconsider its request?

MR. HARRINGTON: Absolutely not. Let's be practical. First, the equity concern that Mr. Marois raised, that of identical non all electric customers paying different rates already exists. There are customers who pay the GS II rate who do not meet 100 percent of their energy

requirements with electricity. I would go as far as saying this is a wide spread occurrence. Disco is apparently aware of this, as well as came out in Mr. MacDougall's cross. Disco at various points in its cross has indicated that they are completely unable to manage this aspect of the GS II rate.

Second, if there is an equity concern, it is the fact that the GS II rate exists at all. This rate was obviously implemented historically for the purposes of promoting electrification and was inherently and undeniably inequitable. The policy reasons that allowed the introduction of this rate are long gone. It is undeniably inequitable to allow the perpetuation of an aspect of a rate which is anti-competitive and benefits no one to continue.

Third, Disco and all intervenors have said that the general service rate must be merged as quickly as possible. It is a practical fact that merging of these two rates will require the elimination of the penalty aspect of the GS II rate.

EGNB's recommendation is to do this immediately as opposed to some uncertain date in the future.

Finally, this is a transitional measure as Disco moves to ultimately merging the GS rates and as such is

particularly appropriate in the current circumstances.

Q.21 - Mr. Harrington, could you now just briefly list what specific recommendations Enbridge Gas New Brunswick is making to the Board?

MR. HARRINGTON: Yes. EGNB makes the following requests, as Dr. Rosenberg also set out. 1) close the GS II rate immediately to new customers. 2) eliminate the penalty when a GS II customer converts part of their energy requirements to an alternate fuel. 3) apply a larger increase to the GS II rate than the GS I rate to effect as much conversion -- convergence as possible through this rate requirement. 4) in accordance with the Board's ruling, apply the largest adjustment possible to the residential tailblock.

And in addition to these requests, EGNB strongly encourages the Board to approve a competitive market based net income for Disco which reflects a capital structure and return on equity for Disco to ensure it is placed on a level playing field with alternate energy providers. And finally, EGNB cannot stress enough the Board's attention to removing the abberation of the GS II class and to provide an opportunity for these customers to choose alternate fuels without penalty.

Q.22 - And finally, Mr. Harrington, do you believe your

recommendations are in line with the Provincial Energy Policy and the Board's CARD ruling?

MR. HARRINGTON: Yes, most certainly. EGNB was retained by the Province on very clear policy objectives. To deliver natural gas at the lowest possible cost to as many customers as possible in as quick a timeframe as possible. These objectives continue to be frustrated by the continuance of the anti-competitive electricity rate structures. Further, while EGNB is the only alternate energy provider represented at this proceeding, we do represent the interests of our rate payers as well as, we believe, the interests of other energy providers. Alternative energy providers and their customers do not want to continue to subsidize electricity rates through their tax dollars. There is no doubt that sending the correct price signals is in everyone's interest, particularly in these times of generally higher overall energy costs. Doing so is the only way to optimize our energy usage, reduce overall costs, encourage conservation and benefit the environment.

MR. MACDOUGALL: Thank you very much, Mr. Harrington. The panel is now available for cross examination, Mr. Chair.

CHAIRMAN: All right. I think we will take our luncheon break and come back at quarter after one.

(Recess - 12:00 p.m. - 1:15 p.m.)

CHAIRMAN: Good afternoon, ladies and gentlemen. The Board has one preliminary matter and that is you responded I believe yesterday to a question from Commissioner Ferguson-Sonier with A-152, and that was the organizational chart.

We would like you to go further, in other words, down so that one gets a sense of how many employees, at what level and whom reporting, et cetera. You don't have to put names or anything.

MR. MORRISON: Mr. Chairman, there was some discretion on our part exercised in how far down we go, and -- is that only for Disco that you want the deep organizational chart, or --

CHAIRMAN: They would like to have it for all the companies.

MR. MORRISON: Okay. And do you have --

CHAIRMAN: Just think, Mr. Morrison, of a chain of title on the wall.

MR. MORRISON: Oh, I understand chains of title very well. The question we had of course is do we go down to the director level, manager level, you know? Where do we cut it off?

CHAIRMAN: Right down to the folks who go out and climb the poles.

MR. MORRISON: That's fine.

CHAIRMAN: Okay. Mr. Lawson, do you want to go next?

MR. LAWSON: I will go next but I don't have any questions.

CHAIRMAN: Okay. That's the way I like it.

MR. MORRISON: Mr. Chairman, I do have one preliminary matter. It's an undertaking response.

CHAIRMAN: Sorry. Yes.

MR. MORRISON: This is the undertaking response with respect to -- you will recall there was a settlement surrounding the precipitator upgrade. This is -- we are going to be filing this in confidence because the settlement provisions agreement have very strict confidentiality provisions, but it is undertaking number 3 from February 22nd.

CHAIRMAN: We will do the same with this as we did with -- previously, and that is the expunged version shall be exhibit A-160 and the pink paper in confidence version will be A-160(c).

MR. NELSON: Mr. Morrison, was this under the Crown Construction Act, this contract?

MR. MORRISON: I don't know, Commissioner. I'm assuming it was but I don't know. I could find out and advise you.

MR. NELSON: Could you, please?

MR. MORRISON: Yes, sir.

CHAIRMAN: Any other preliminary matters?

MR. GORMAN: Mr. Chairman, just one other preliminary matter. During my cross examination I requested a number of undertakings and it will no longer be necessary to fulfil the first undertaking given to us which was the question relating to the short term contract usage in the past. Since that's now coming out of the rate schedule we no longer require them to provide that information.

CHAIRMAN: Okay. Thanks, Mr. Gorman. Any other -- okay. Then does the Irving group have any questions, Mr. Booker?

MR. BOOKER: No, Mr. Chair, no questions for this Panel.

CHAIRMAN: Thank you. So, Mr. Gorman, do you have any questions of this Panel?

MR. GORMAN: No questions, Mr. Chairman.

CHAIRMAN: Good. Vibrant Communities isn't here. So we are down to the Public Intervenor. Mr. Hyslop, do you have any questions?

MR. HYSLOP: Less than five minutes worth, Mr. Chair.

CHAIRMAN: Good. Just before you start, Mr. Hyslop, the -- it's in the confidential response, Mr. Morrison -- sorry, in the confidential response that is A-160(c) it of course indicates the amount of settlement but it doesn't say in whose favour that settlement was.

MR. MORRISON: It was in favour of Coleson Cove, sir.

CHAIRMAN: Okay. Thank you. Sorry, Mr. Hyslop. Go ahead.

CROSS EXAMINATION BY MR. HYSLOP:

Q.23 - Thank you, Mr. Chair. I have two advisors I find my cross examinations become even shorter and shorter. Thank you, Mr. Harrington, Ms Black, it's nice to meet you and have you with us. And I will begin by prefacing my remarks or my questions by saying as Public Intervenor many of the policy points that you make are well taken. However, having said that I do have a couple of questions. And first, you did receive your franchise in August I think of 1999, Mr. Harrington?

MR. HARRINGTON: That's correct.

Q.24 - Right. And I understand from having a quick look through your franchise agreement there is supposed to be a seven year review take place and that's some time this fall or in the close foreseeable future, correct?

MR. HARRINGTON: This is the seventh year.

Q.25 - Yes. Okay.

CHAIRMAN: Now, Mr. Hyslop, don't bring up anymore work for us, please.

MR. HYSLOP: Trying to find a role for the Public Intervenor.

CHAIRMAN: I sort of thought that.

Q.26 - Having said that, I was interested in your comments on

price signals, and to achieve some of the goals that you have outlined for EGNB and what you see as the policy, would I be wrong to suggest that you would even recommend something like that residential electrical customers should be paying say rates that are 1.25 times their cost? Would that be something that you would see as reasonable, Mr. Harrington?

MR. HARRINGTON: Well Dr. Rosenberg put forward EGNB's rate proposal with regard to the residential rate. I think the primary changes there were -- as compared to Disco's proposal was to apply as much as possible under the Board's ruling to the tail block. Whether that's 1.25 or not I'm not sure.

Q.27 - Okay. Fair enough. That's a fair answer. And as a policy though would you suggest that we should lower the revenue cost ratios for the large industry in order to raise the revenue cost ratios for the residential class as a matter of policy?

MR. HARRINGTON: No. I think what is important is that customers receive the proper pricing signals for the energy that they are using. For instance on Enbridge Gas New Brunswick's proposal around the residential rate as I have indicated we have applied as much of the increase as possible to the tail block in accordance with the Board's

ruling, to make sure that the most effective price signal is sent. What the impact is to industrial customers and how that works out in the overall revenue to cost ratios, I think those were questions -- those would be questions that would be better put to Dr. Rosenberg.

Q.28 - Okay. So in terms of equity for example to achieve your goal, the fact that you would be moving the revenue cost ratio for the large industrial firm transmission class to a revenue cost ratio of less than .9, would that be something that if that happened that's the way it should be? That's the way you view it?

MR. HARRINGTON: If you look at Enbridge Gas New Brunswick's proposal for the residential -- for Disco's residential rate, what we are doing is making sure that the cross subsidy between customers who do not heat with electricity and customers who do heat with electricity are being brought closer together. And that really is all that we are proposing to do.

Q.29 - And that would be the same point that the Board in its December 21st ruling suggested that that whole spread should be collapsed over I think next five years in three equal parts. Is that -- are you suggesting that the Board in fact move even faster than what they ruled in December?

MR. HARRINGTON: No. I think we are comfortable with the

Board's ruling. I think what would be helpful is additional certainty over timing. We have been concerned since we commenced operations with the slowness of Disco to make changes to some of their rates. This is the one opportunity that we have had to come and offer our evidence on the matter. We know that the Board has said three equal changes over a period of five years. It would be very helpful if there was additional certainty so that customers could prepare and start responding to price signals.

Q.30 - Okay. So you would like to see the Board make that a very firm order at the end of the day at the end of these hearings?

MR. HARRINGTON: That's correct.

Q.31 - Right. Almost reaffirming the position that they took on December 21st, correct?

MR. HARRINGTON: That's correct.

Q.32 - Right. And last but not least -- and, Mr. Harrington, I don't in any way want to make a suggestion that -- I know business plans go awry, but in reading your request for -- or response to a request for proposal that you filed with this Board in 1999, I noted that there were 270,000 residential homes or locations in New Brunswick. Does that sound right, subject to check?

MR. HARRINGTON: In terms of all up residential customers at the time, yes.

Q.33 - Yes. And I did read -- I read the reports that Mr. Easson had been filing with the Board on the ongoing, and the last one I found was for December 31st 2003. And at that time that report indicated there were 2,312 customers of EGNB in New Brunswick at that date. Does that sound right, subject to check?

MR. HARRINGTON: It sounds approximately right. I could certainly bring you up to speed with where those numbers have gone beyond that.

Q.34 - Well yes, I would be interested in hearing. How are you making out the last couple --

MR. HARRINGTON: Well just to provide some comparison there. Our proposal back in 1999, almost seven years to this date was when it was submitted, it projected that we would be serving approximately 17,000 customers by this point in time. We are serving just over 5,000 customers at this point in time.

MR. HYSLOP: Thank you very much, Mr. Harrington. Those are all my questions, Mr. Chair, and again although I think at the end of the day I can't maybe go as far, I want to reiterate in principle the use of gas in New Brunswick I hope continued to be aggressively pursued by your company,

Mr. Harrington. Thank you.

CHAIRMAN: Thanks, Mr. Hyslop. Mr. MacNutt, does the Board staff have any questions?

MR. MACNUTT: Board staff have no questions for this Panel.

CHAIRMAN: Okay.

MR. MORRISON: I know you didn't ask, Mr. Chairman. But I have no questions.

CHAIRMAN: I can sense these things.

MR. MORRISON: But perhaps before the Board starts, I do have an answer to the question that was posed by Commissioner Nelson.

The precipitator contract was let under the provisions of the Crown Construction Contracts Act -- was.

CHAIRMAN: I have no idea. I'm not familiar with that legislation. I think Mr. MacNutt is. We are curious up here as to how under the Crown Corporations -- sorry, not the Crown Corporations but the Crown Construction Act something would be confidential.

MR. MORRISON: It has been a long time since I had a look at the Crown Construction Contracts Act, Mr. Chairman. But I understand the mechanism of the legislation is in the tendering process.

But once the contract is let then it proceeds in the normal course as any other commercial contract. And

therefore confidentiality provisions and so on would apply.

It is the tendering process that has to be -- which really the legislation is designed to control.

CHAIRMAN: Okay. Do you concur, Mr. MacNutt?

MR. MACNUTT: Yes. It is not -- the legislation and the regulations under the Crown Construction Contracts Act do not contain any provisions with respect to confidentiality However, the contracts entered into pursuant to them do contain some confidentiality provisions.

But I would believe in this situation, and perhaps it could be confirmed by Mr. Morrison, that the confidentiality clause that is inhibiting the putting of the settlement on the record would be in the settlement contract.

MR. MORRISON: It is in the settlement agreement. It is not in it itself. Which is not unusual in settlements of course.

CHAIRMAN: Good. Thank you.

MR. DUMONT: Mr. Harrington, from what I understand, if you were to get the pricing for electricity to encite people to switch to natural gas or whatever other fuel, what would people in the north do?

MR. HARRINGTON: Well, I think you mentioned it in your

question, other fuels. Actually there is a few points I would like to get out here.

One is it's not just about natural gas and conversion. Of course we have an interest in making sure that our business is as successful as possible and attracting as many customers as possible.

However, there are alternate fuels available in all areas of the province. Propane, oil, wood all have a part to play in terms of meeting end use energy requirements. And all are frustrated by the same issues associated with Disco's rates.

Third is it is a bit of a chicken and an egg. Enbridge Gas New Brunswick's ability to expand its distribution service -- and I won't be as facetious enough to say that we would be able to do that with the markets alone that are available -- is limited by our ability to compete with alternate fuels including electricity.

The fact of the matter is we will be able to provide more service to more areas more quickly if we are able to penetrate additional markets and especially those that we are restricted from right now due to Disco's rates.

MR. DUMONT: Thank you. That is all I have.

CHAIRMAN: I have no questions. Mr. MacDougall, do you have any redirect?

MR. MACDOUGALL: No, Mr. Chair.

CHAIRMAN: Good. Thank you, panel. You are excused.

ROBERT KNECHT, sworn:

DIRECT EXAMINATION BY MR. HYSLOP:

CHAIRMAN: Go ahead, Mr. Hyslop.

MR. HYSLOP: Thank you, Mr. Chair. Good afternoon, Commissioners and good afternoon, Mr. Knecht.

Q.1 - Would you please state your name again for the record, sir?

A. My name is Robert D. Knecht.

Q.2 - Right. And in response to Disco's refiled CCAS and Rate Design Proposal, I understand you have prepared some additional evidence?

A. I did.

Q.3 - Right. And I refer you to what has been entered, I believe, as exhibit PI-18. Was this document prepared by you and under your supervision?

A. It was.

Q.4 - Right. And do you have any corrections with respect to the same at this time?

A. I have no substantive corrections and I think we will skip the typos.

Q.5 - Okay. And do you now adopt this evidence for purposes of these proceedings?

A. I do.

Q.6 - Right. And, Mr. Chair, I believe at the earlier CARD hearing Mr. Knecht was accepted as a witness with respect to cost allocation and rate design. And I assume that such designation and acceptance by the Board continues?

CHAIRMAN: Oh I would certainly think so.

MR. HYSLOP: Thank you.

Q.7 - Mr. Knecht, my first question is with regard to Mr. Larlee's revised CCAS. Can you generally state how good a job he did on that?

A. I think Mr. Larlee did quite a good job. I felt my assignment was to evaluate how consistent the refiled study was with the Board's December 21st decision. Generally it was quite consistent. We found a few things in the discovery process that we corrected. There were two issues I think deserving of a little bit more mention. One was the treatment of the transmission costs being allocated to the interruptible customers. And the second is the treatment of the combustion turbine costs in the -- in Schedule 5.1 of the CCAS.

Q.8 - Let's deal first with the impact of changes to the OATT tariff. Would you comment on that please?

A. Sure. Mr. Larlee changed the methodology that was used in the CCAS we were working with last fall to reflect

a change that went into effect in May of 2005 with respect to the open access transmission tariff, the OATT. He changed the methodology to reflect the fact that the rates for interruptible service were changed for self-generators, the capital I Interruptible service, if you will, were changed. In the OATT this reduced the allocation of costs to the interruptible customers by about 1.7 million and redistributed it to the other -- to the rest of the customers.

I believe this change is consistent with cost causation. The objective that the Board had, I think that we all had in the fall, was to pass through transmission costs as accurately as possible. And this change is consistent with that. The only reason I highlight this particular change is that in the Board's decision it seemed to feel that this was not going to have an impact on interruptible customers whereas if we are going to set rates for interruptible customers that are based on allocated costs, then this in fact will have and probably does have an effect on the rates for interruptible and possibly surplus customers as well.

Q.9 - Thank you. Now the second issue you mentioned was the allocation of combustion turbine costs. Can you outline your issue with respect to this and any concerns that

these costs happen to increase say during the Point Lepreau refurbishment?

A. This was an issue that was not specifically addressed in the Board's decision. In the CCAS that Disco filed last summer, I guess they had an allocation methodology which assigned to all of the CT, combustion turbine costs only to essentially electric heat customers. Residential, GS II -- residential electric, GS II and a portion of the wholesale customers which were deemed to be electric heat customers.

In the study that I had filed I had used the 1992 methodology and had basically classified them as energy related and allocated them to all the rate classes on that basis.

From a cost causation standpoint, any customer who is using the system when those are running is contributing to the need for those systems, whether they are electric heat customers or large industrial customers or residential non electric heat customers. Everyone is contributing to the need for that and so therefore, it would seem to me that while you can make an argument for different allocators, the one that Disco is using is not correct. And that it seems like the options are either to use an energy allocator consistent with the 1992 methodology or to use

some sort of peak based allocator for anyone who is contributing to those peak costs.

Obviously this problem is relatively insignificant at current levels of CT operation. If in fact that increases it becomes a bigger matter, and one that I think would be worth resolving now rather than waiting for that to come.

Q.10 - Thank you. Now there has also been some minor confusion over the treatment of export sales credits and I think I went through that with Mr. Larlee a little bit the other day, but would you please comment on Mr. Larlee's position, the point you are raising and any recommendation you might have?

A. My view is there is two separate issues with respect to the treatment of the export margin credits. First is how you assign them to each class. How much credit you give to each class. And this is the issue of how they get classified and how they get allocated, whether they are treated as a revenue credit or they are treated as a cost offset, the classification and allocation is an arithmetic exercise that has been resolved.

There is a second issue which Ms. Chown and I raised in 1991 with respect to how you consider that when you are doing your revenue cost ratio calculations. Do you consider that as an offset to costs or do you consider it

as an addition to revenues?

That is is it similar to a cost credit or is it similar to pole revenues, some additional revenues that get earned and get added to the revenue base. And this is a completely different issue and I think Mr. Larlee is trying to push them together to apply the Board's ruling to the treatment of these classes as a cost credit.

Back in 1991 when Ms. Chown and I did present evidence on this topic, we argued that the company was building capacity in advance of domestic need in order to serve the export market, and therefore they were -- these were costs that were really associated with the export market and therefore should be assigned to the export customers, as you will, and therefore should be treated as a cost credit. The Board didn't agree with us at the time and determined that a revenue credit was more appropriate.

To be perfectly honest I think the cost basis that Ms. Chown and I used in 1991 is less -- is certainly less true today if it is true at all. I see much less of a sense that the company is building to serve the export market.

But I guess my point here really was this was an open issue. It was not addressed in the December decision. It was addressed in the 1992 CARD decision and my recommendation is the Board just clarify how it should be

done.

Q.11 - Now in your evidence based on Disco's total revenue requirement in its filing, did you propose any different allocation, each class as revenue requirement?

A. I did not. I looked at the proposal. When it comes to allocating the revenue requirement to the various rate classes I think everyone agrees that this is a matter of judgment. We all like to see some progress towards cost base rates. We all like to see some treatment of gradualism.

In that progress that is being made, I looked at the proposal that they made, I looked at the progress towards cost based rates. I guess I would say it's on the unaggressive end of moving towards cost based rates, particularly for the business classes, and particularly between the large industrial and the smaller business classes.

But generally there was progress being made and it looked like it was enough that it was within the range of being reasonable.

Q.12 - Now in your evidence, exhibit PI-18 at page 11, you have something called progress metric. Can you explain to the Board what a progress metric is and how it works and what it attempts to show?

A. I apologize for giving the thing a bad name, but the idea is to try to show how far -- how much progress -- quantify how much progress each class is making towards cost based rates as part of the proposal. And in that I start with what I call the normalized revenue to cost ratios, that is, the revenue cost ratios under present rates, as if they were recovering all of the costs. And then compare that to the revenue cost ratio under the proposed rates. And I look how far you need to go to get to 100 percent, and then how far you actually get.

So for example if a class started at 90 percent and it goes to 92 percent, it has made -- it has progressed 20 percent of the way towards getting to fully allocated costs.

And that's all this is. It's a little way to try to gauge as if -- well we are looking at one class and it has moved 86 to 87, how does that compare to a class that has moved 94 to 95? And so it's assigning a little bit of a scale to estimate how much progress is being made.

Q.13 - Now after you filed your evidence we found an additional $2.1 million in revenues, and I guess my question is have you had the opportunity to update the progress metric that was found at page 11 of your evidence?

A. I guess I did. Are you submitting --

Q.14 - Yes. We would like to submit that as --

A. I would. It's simply reflecting the fact -- as I guess the Board is aware, we found that the underestimated the revenues coming from the interruptible surplus customers in the amount of 2.1 million. The company agreed that that should be taken out of their revenue requirement and they have taken that out of the -- proposed to take it out of the large firm industrial customers, thereby lowering the increase for the large industrial customers and lowering that class' progress towards cost --

Q.15 - Maybe just hang on until we get the exhibit marked and before the Board, Mr. Knecht, if you wouldn't mind.

MR. HYSLOP: I move to have this entered as an exhibit, Mr. Chairman.

CHAIRMAN: It will be PI-23.

Q.16 - I might -- Mr. Knecht, now that everyone has PI-23, could you indicate quickly the findings and perhaps commenting on what the results are in general terms and specifically perhaps to residential and other classes?

A. Yes. This table shows basically the same pattern as that in table RDK-2 on page 11 of my evidence. The points that I would make is that the residential class of the

major classes is the one that's making the most progress towards cross-based rates. And that's about 20 percent which is not terribly aggressive but not bad. It certainly gets it within the 95, 105 range which is a positive feature.

The General Service I and General Service II classes are making less progress. And they are basically constrained by the fact that there is not much progress being made by the large industrial customers, particularly the large industrial firm transmission customers.

And with the assignment of that 2.1 million that progress towards cross-based rates for large industrial firm transmission customers has now dropped to 5 percent, it is getting to be very little progress at all.

Q.17 - Now during these hearings -- and we again had evidence filed by EGNB by Dr. Rosenberg on behalf of EGNB. And have you had an opportunity to review Dr. Rosenberg's proposal? And have you had an opportunity to prepare a progress matrix with respect to his proposal, sir?

A. Yes, I have.

MR. HYSLOP: Okay. We would move to have a further exhibit entered, Mr. Chair.

CHAIRMAN: That will be PI-24.

Q.18 - Mr. Knecht, I would ask if you could briefly comment or

provide any comments you might have with regard to Dr. Rosenberg's proposal. And then if you would briefly comment on the results you obtained in exhibit PI-24?

A. I think the issue with Dr. Rosenberg's proposal is that Dr. Rosenberg is implicitly relying on a cost allocation study that's not consistent with the one that Disco has filed in these proceedings.

And the reason that I say that is exhibited in PI-24 here. Dr. Rosenberg proposes very substantial progress towards cost-based rates for the residential class. I calculated at 71 percent in this exhibit.

And pretty good progress towards -- very good progress towards cost-based rates particularly for the GS I class by assigning a zero percent increase.

I guess where I am concerned here is that with respect to the large industrial class and particularly the firm transmission customers, he is actually proposing a less than system average rate increase, which is going to lower the revenue-cost ratio for that class and thereby obviously not make any progress at all towards cost-based rates.

And that would not fall into the range of what reasonable proposals are I think, unless there are strong extenuating circumstances for setting the rates for that

class at well below cost.

At this point, and based on the evidence on the record, I don't know that there is strong evidence that large industrial firm transmission customers should be getting an increasing discount from their cost responsibility as a result of this proceeding.

Q.19 - The exhibit PI-24 shows only the firm transmission large industrial customers, not the interruptible customers. It also breaks the large industrial rates into distribution and transmission categories. Why did you do this?

A. Actually the distinction between those two -- I have two different reasons for doing that. Separating the firm large industrial from the interruptible, small i interruptible customers, is because interruptible service is a very different kind of service.

It has very different service characteristics. It can be interrupted. And moreover, it's served by a very different set of tariff charges. It's not based on embedded costs. It's primarily an incremental cost-based tariff.

And the rates are completely different. They are set in a completely different way for a different service. And therefore, as a general rule, I think that Disco

should separate out firm and interruptible customers in its CCAS.

With respect to the distribution voltage and the transmission voltage customers, again this I think falls under what Dr. Rosenberg described as more information is better. It does provide a little signal as to perhaps the rate design within the large industrial class as to whether it is properly structured.

Q.20 - Mr. Knecht, in the Board's December 21st 2005 ruling it dealt with interruptible and surplus rate customers and stated as follows at page 33.

The Board considers it appropriate that interruptible rate customers should pay for some of the fixed generation costs. For most of the years it is the in-province generation that provides the interruptible energy and at a lower rate than for firm energy. The specific amount of the contribution will be established during the review of Disco's revenue requirement. First what was Disco's proposal?

A. When it was filed Disco proposed that it make no change to the adders that it adds on above the incremental generation cost for these customers.

At the time, Disco believed that that would actually mean a negative contribution to any costs above that. It

would be about .7 million below the actual allocated costs for generation and transmission to those customers.

With the 2.1 million that we found, the proposal is now to provide 1.4 million from these customers as a contribution above the generation and transmission costs.

Q.21 - Can you outline what you understand to be their reasoning for not proposing a contribution to fixed generation costs and provide any comment that you might have on their position?

A. They offer two reasons for not doing that. One is that they felt like that they needed to do something to their cost allocation study to figure out what sort of costs needed to be allocated to these customers so that they could then add them into the rates. And the second concern they raised was that they were concerned about switching to firm service.

I don't think the first concern is relevant at all. There is no reason that you need to make a judgmental contribution to generation costs or overhead costs based on a cost allocation study. In fact we see there are not revenue-cost ratios that are 100 percent for any of the classes.

The issue of switching -- of these customers switching to firm service I believe is a very serious issue. I'm

not sure that a modest contribution to fixed cost is going to make that difference.

The issue with respect to the Lepreau refurbishment I think is a much more serious concern than some small contribution to -- than some small contribution to overhead and fixed costs.

Q.22 - Now do you have a recommendation that you would make to this Board with respect to a change in the surplus interruptible rate?

A. The recommendation I put in my evidence was that overall something on the order of about $3 a megawatt-hour which would be about 5 percent of allocated generation and transmission costs should be -- would be, you know, a very modest contribution for what is essentially an opportunity service.

Therefore, because it's 5 percent, it implies a revenue-cost ratio of about 105 percent.

Q.23 - Okay. Now you mention something about the ability of surplus customers and the concerns of moving them into firm service and perhaps vice versa. Can you elaborate on that point to the Board?

A. Let me answer in a general way. Interruptible customers, as Mr. Larlee was saying, can provide very significant values to firm service customers, if the

interruptible customers are contributing something above the incremental costs that they cause, and if the customers are there when you need to interrupt someone to avoid having to build additional capacity. In essence interruptible customers can be valley fillers.

But you have to recognize there is two kinds of valleys. There is the within the year valley which is, because of the seasonal nature and the time of use nature of firm demand load, there are valleys during the day and there are valleys in different seasons during which interruptible service can be provided, and fill up those valleys. And if they are providing something in excess of the incremental costs, everyone benefits.

There is also longer term valleys. Capacity additions, generation capacity additions are lumpy. You get big increases in capacity when a new generator comes on. And that provides a longer term valley during which interruptible customers can take nearly firm service for a long period of time. And even that has value to the firm customers if those customers are still there when capacity tightens back up again.

But if you don't impose some pretty strict requirements that interruptible customers stay interruptible when capacity tightens up, you create this

incentive for them to jump in when there is big valleys and jump back out again just when you need them.

And I think with respect to where Disco is, and as I understand their contracts, you know, there is only a 12-month notice. And that seems to put the firm customers at some risk if the interruptible customers can switch to firm on relatively short notice.

Q.24 - Now there has been some discussion between Mr. Larlee and Dr. Rosenberg over how the adjustment to the declining block rate for the residential class should be calculated. Would you comment on the one-third adjustments and the differences if any between Disco's and EGNB's position?

A. Yes. When I first read the Board's ruling I actually interpreted it exactly the same way Dr. Rosenberg did. I looked at the way Mr. Larlee did it. His method is certainly reasonable. And it could be -- the Board's interpretation could be a reasonable interpretation of the Board's decision.

I think Dr. Rosenberg's interpretation could also be perfectly reasonable. I don't really have a strong opinion about which one is better. Either of them is consistent with the Board's ruling.

And I think that the big picture is that we are taking the first stage of adjusting the residential rates, which

is to phase out the declining block. And the difference between those two is not terribly substantial.

MR. HYSLOP: Thank you. I didn't want to get on the record that the PI was in agreement with both EGNB and Disco on some point in these hearings, Mr. Chair.

Q.25 - Finally, assuming that we have some success with regard to reducing the revenue requirement for Disco in these hearings, do you have any recommendations that you would make to the Board on how these reductions should be applied?

A. I guess I would encourage the Board to be as specific as possible in its directions, as a general matter, just to reduce the potential for argument, one more time around here.

Specifically I would say that if the -- as I understand it, the possibility that there would be any reduction in the overall revenue requirement is most likely to relate to distribution costs.

If in fact it is only reduction in distribution costs, I would make sure that the reduction in the revenue requirement therefore flowed to the customers who take service at distribution voltage. Because the customers who take service at transmission voltage are not contributing to those costs.

The one other item that's in my evidence is that I looked at the residential rate design. The customer charge looked reasonable. The energy block charges looked reasonable within the Board's guidance.

If in fact there is a reduction in the overall revenue requirement and the residential class revenue requirement, I would make sure that there is some reduction to both the customer charge and the energy block charges. And those ought to be split about 50/50 in terms of the revenue associated with each.

MR. HYSLOP: Mr. Chair, that concludes my examination of Mr. Knecht. And I leave him available for cross examination by those parties who wish to do so.

CHAIRMAN: Thank you, Mr. Morrison. Would you like to go first this time?

MR. MORRISON: That's fine, Mr. Chairman. Thank you.

CROSS EXAMINATION BY MR. MORRISON:

Q.26 - Mr. Knecht, you just talked about the discovery of the $2.1 million of understated interruptible sales.

A. Yes.

Q.27 - And I think you said that that now results in a revenue to cost ratio in the interruptible class, all the interruptible customers of 1.02.

A. That's approximately correct, yes.

Q.28 - And I think you mention that that translates into -- it is in your evidence and I believe you just mentioned it -- an over-recovery of approximately $1.50 per megawatt hour?

A. Yes. Actually -- it is on that order, $1.40, $1.50.

Q.29 - And you don't have to turn this up but on page 15 of your evidence, you recommend that a $3 megawatt hour contribution in excess of incremental generation allocated transmission costs be added to the interruptible sales, you are looking for a $3 adder, if you will? Correct?

A. Yes, including the -- including the -- that would include the 140 that is already there. It would be about $1.60 on top of that.

Q.30 - Okay. And you are aware, Mr. Knecht, that there is already a $9 adder on peak and a $3 adder off peak?

A. The $9 adder on peak and the $3 adder off peak are there -- - yes, I am aware that they are there. My understanding is that they are there to contribute to the allocated transmission costs as well as any allocated overhead costs that might flow through the cost allocation --

Q.31 - No. I am just trying to get clarification that what you are recommending and what is in this $3 adder is in addition to the adders that are already in place. Is that correct?

A. The full $3 is not in addition to the adders that are already in place. It is the $1.60 to get us up to a full $3 over recovery that would be in addition to the $3 and the $9.

Q.32 - Okay. I see. I was not clear. Now the $3 adder that you are proposing, do you have any mathematical basis for that calculation?

A. A mathematical basis is the one that I gave in my direct evidence and is in the prefiled evidence which is it puts the class at about 105 percent revenue cost ratio and that is within the 95 to 105 range. As a general matter, this is an issue of judgment. It is a -- it is a opportunity service. It helps other rate payers if it contributes in excess of incremental costs. If it is not contributing in excess of incremental costs, it is not helping everyone else out. I have been in some places where I have seen, you know, $3 a megawatt hour as a contribution from opportunity of service so between it being 5 percent and having seen it in Alberta, it seemed like a reasonable number to me but it is a judgmental factor.

Q.33 - And that is the point I am trying to get at, Mr. Knecht, you have no cost basis for it, this is just a judgment on your part? Correct?

A. Well it's not without cost basis in that it's 5 percent of the allocated costs.

Q.34 - But was there a cost analysis done to support that --

A. Yes, I looked at the -- I looked at the allocated costs to the interruptible surplus customers and it was about $60 a megawatt hour. I would have to go check exactly what it was but my recollection is this brought it in at about a little over -- between 104 and 105 percent.

Q.35 - But the magnitude was something that was in your judgment in terms of you chose 5 percent?

A. With the Board's 95 to 105 guidance, yes.

MR. MORRISON: Okay. Thank you. Those are all my questions, Mr. Chairman.

CHAIRMAN: Thanks, Mr. Morrison. We will take a ten minute recess. And Mr. MacNutt, can you find out from counsel how long they thing they have for this witness?

MR. MACNUTT: I will, Mr. Chairman.

(Recess)

CHAIRMAN: Mr. MacNutt was the bearer of bad tidings. Okay. Mr. Lawson?

MR. LAWSON: Thank you, Mr. Chairman.

CROSS EXAMINATION BY MR. LAWSON:

Q.36 - Good afternoon, Mr. Knecht.

A. Good afternoon, Mr. Lawson.

Q.37 - I would like to start questioning with respect to the - - sort of the demand energy weighting issue and I believe you would agree that Disco's application took fixed generation costs and allocated it at 40 percent demand and 60 percent energy related with 100 percent allocation for variable generation as energy. Is that a fair assessment and consistent with the CARD decision, I believe, of December?

A. Yes, I think so.

Q.38 - Okay. Now if you took the total generation costs and classified what part was energy, have you taken a look at that? Sort of taking the two, the fixed generation costs and total variable costs, add them together to see what percentage would be actually energy related, both with and without the consideration of the export sales credit being applied?

And I have done the calculation. Let me ask you, would you agree it is in the order of magnitude of 80, 20 when you don't consider the export credit and 85, 15 or maybe the other way around -- 85, 15 after the export credit is recognized and 80, 20 otherwise? Is that order of magnitude familiar? If not, then I will take you through some statistics which will take us a few minutes?

A. Rather than go through them all, I believe that I had

done a calculation similar to that probably in the fall and at least got numbers on that order of magnitude. If you want, I can accept them subject to check.

Q.39 - Okay. Subject to check then, you would agree then that it would appear as though it is about with the export credit in consideration, 85 percent energy and 15 percent demand. Is that right?

A. Again, subject to check, that does not sound completely out of the range of possibility. Sounds about right.

Q.40 - Okay. Now just related to that, this classification, this 40/60 split that was used was the same classification methodology for generation costs in the 1992 decision of this Board, I believe?

A. Yes.

Q.41 - Would you agree that as energy costs increase with all remaining other costs remaining the same, that -- and the classification methodology of 40/60 remaining the same, that the proportion of costs classified as -- sorry, energy costs increase -- I have written this out incorrectly but let me try independent of my written question.

As energy costs increase, that their proportion of the costs will increase more significantly as a result?

A. Yes, if fuel costs increase and non-fuel costs don't increase, then yes, by definition the proportion -- the overall proportion that is energy related will increase and I think with the rise in fuel costs, you see exactly that. Mr. Marois was referring I think the other day to that and the implications of that.

Q.42 - So you would agree that a significant factor for the escalation in costs are related to energy costs, fuel cost increases in this case?

A. Certainly in the past couple of years the increase in the fuel costs has been -- the increse in costs has been driven by the fuel costs. Whether that's true over the longer term since the last time I was here I haven't studied.

Q.43 - No, no. I wouldn't expect that either. If my memory serves me correctly it was not more than a few years ago that large industrial customers were in fact at unity. Is that your understanding? Or near unity, perhaps not exactly at unity.

A. I would have to go back and check, but my recollection from when I was here the time before that is the large industrial customers had revenue cost ratios in excess of unity, yes, so at some point it crossed back over.

Q.44 - Right.

A. And I also did an analysis in my September evidence I think which showed that the average revenues paid by the residential class had risen much more than larger industrial customers had done. So some of the change in revenue cost ratios over that period were due to different rate increases for different classes.

Q.45 - But obviously as the energy costs increase, and more particularly over the last couple of years, because of this energy sensitivity, if you will, to the rates for the large industrial, that has driven up the costs for the large industrials, is that a fair assessment? It has been a significant factor?

A. I think that's consistent with what Mr. Marois said the other day and it certainly makes sense to me.

Q.46 - Right. So there is a significant sensibility or sensitivity I guess it is in the large industrial rates to these energy costs?

A. Yes, I would agree with that. And as Mr. Marois said, you know, all other things being equal an increase -- you know, a disproportionate increase in fuel costs will tend to have a larger impact on those customer classes that are -- whose load is more related to energy than to demand.

Q.47 - Sure. And would you agree that as the proportion of energy costs increase the costs allocated to a higher load

factor classes, such as large industrial principally, increases relative to lower load factor rate classes?

A. I just said yes.

Q.48 - Yes. And I would like to refer to -- in your evidence you make reference to the Quebec scenario on the revenue cost ratio, and in fact you say that legislation mandates retention of historical revenue cost ratios, and then you indicated which exceed 115 percent for large industrial customers. You have in fact testified in Quebec matters, have you not, matters before the Regie in Quebec with respect to these rates?

A. I have.

Q.49 - And in fact you were involved in a rate increase in I believe it was 2001 -- involved in hearings with respect to rate increase in 2001, is that right?

A. Yes, I was. Was that the generation rate proceeding?

Q.50 - Yes.

A. Yes.

Q.51 - And in that am I correct in understanding that you were proposing a 60 percent energy and 40 percent demand allocation in that case for total generation?

A. I believe that I did for total generation costs in the context of Hydro Quebec at the time. Actually to be perfectly honest, using analysis that was very similar to

the analysis that Ms. Chown and I presented before this Board in 1991.

Q.52 - So that would be the equivalent to our 80 or 85 percent, 20 or 15 percent that we are talking about now, isn't that generally correct, total generation allocation?

A. It would be correct that it is related to total generation costs. Obviously the types of generation are very, very different in Quebec than they are in New Brunswick.

Q.53 - Sure. No, I understand that.

A. So that it's not clear that that comparison is -- can be taken just as it is. There is the caveat that the generating mix is very different in Quebec.

Q.54 - Right. But I presume you would agree that to see an energy classification for generation -- total generation costs as high as 80 or 85 percent as we are talking about here is unusually high?

A. I don't -- I can't say that I -- I have studied enough thermal systems that have a traditional demand energy split to say that this is unusual. In general it's -- certainly we can go dig out the evidence that Ms. Chown and I filed in 1991 which in fact did a survey of all the Canadian utilities and did in fact compare the demand energy splits among them all, which led to our

recommendation in that proceeding, which was not adopted by this Board.

Q.55 - Right. But based on what you do recall and know from your experience, including that and subsequently which may be fresher in your mind, for those of which you are aware would you agree it is unusual?

A. Based on the evidence from that proceeding and probably not very many utilities after that, it is a relatively high mix of energy costs. In fact with the recent run-up in fuel costs everyone -- as you mentioned earlier, everyone's mix is increasing. I haven't done an exhaustive study. The last one we did was over ten years ago.

Q.56 - Okay. Thank you. Now just turning to interruptible power, I guess you have an indicated an acknowledgement there is a contribution of $1.4 million being made towards costs beyond the generation and transmission costs for interruptible power now, is that right?

A. Based on current revenue estimates from the interruptible class, yes.

Q.57 - Right. Okay. Now if I can just refer you to page 17, the bottom of page 17, top of 18 of your report marked PI-18. And just the very last sentence on the bottom of 17. However if Disco deems that large customers can meet

the proposed rates, there is no need, et cetera.

Now is there any evidence to which you can point us that indicates that Disco has in fact deemed that customers can in fact pay those rates?

A. No, I can't. We actually asked some questions of Mr. Marois subsequent to my having read this evidence, asking whether he had any information that would show that large industrial customers could not afford that. And he said that he did not.

Q.58 - Now since we are into hearsay, can I go so far as to say though he probably did tell you that large industrial expressed grave concern with respect to the rates that are being proposed?

A. I don't recall that from the transcript. I do recall that that was part of Disco's filing back last year as part of this, that they were concerned about loss of load.

Q.59 - Yes.

A. And at the time we asked some Interrogatories on that. And again there was no specific evidence.

Q.60 - No.

A. My own evidence -- as you know, having represented industrial customers, I worry about loss of load. But regulators generally need some hard evidence to rely on when reacting to that kind of situation.

Q.61 - Sure. And that is I guess why I would ask you to point to us any evidence that shows that indeed large industrial customers can afford the proposed rates?

A. Well, I'm sure the attorneys will argue burden of proof here. But it seems to me that if there isn't any proof either way as to whether or not they can or cannot afford it, then we rely on the results of the cost allocation study for setting rates.

Q.62 - But your reference is to an assumption of an acceptability of those rates, is that correct, to the customer, and that mere falling back to the rate study doesn't do anything to consider the impact on the customers, isn't that right?

A. I'm sorry, I didn't understand the question.

Q.63 - The rate study -- you know, you have filled in the mathematical consideration, it doesn't give any consideration to what kind of impact the consequences could have of a rate increase on those particular customers, isn't that right?

A. That's correct. But if there isn't any evidence past that then what's what we ought to rely on.

Q.64 - Okay. That again perhaps will be a subject for debate. But we won't engage in it now.

Now you did acknowledge in your evidence on direct

that there is a very significant concern that can fall out of switching -- customers switching from interruptible, small i as referred to this morning, interruptible power to firm power, you would agree?

A. Yes.

Q.65 - And you did agree I believe also that interruptible power plays an important or valuable role in filling in what I think is described as two types of valleys?

A. What I said is interruptible can provide value if the conditions that I described were met, namely that they are contributing something in excess of the incremental costs and in fact that they are there to be interrupted when the long valley ends.

Q.66 - But you would agree though that they are of value, even if they were not contributing anything above unity, for the purposes of planning for the needs for power for Disco and Genco, wouldn't you?

A. Yes. They are valuable if in fact Disco or Genco or --

Q.67 - Whoever?

A. -- however it's going to be defined, can rely on them remaining interruptible.

Q.68 - That is right. Yes. Precisely. So therefore it is important, you would agree, to strive to keep those

customers as interruptible customers to the extent possible, and not to switch to firm?

A. I guess I would agree with that. I might put it just a little bit differently in that I would -- I would impose some pretty -- restrictions requiring them to remain interruptible when the long valleys end.

Q.69 - And obviously this is of particular concern, I would assume you would agree with Disco on, with the pending time of Point Lepreau shutdown for its renovations, if you will, that this is of grave concern if there is a switch to firm power by interruptible customers at the moment?

A. Yes, I would.

Q.70 - And I presume you don't know of anything that would -- you don't know whether or not large industrial customers taking interruptible power will convert to firm power if the cost increase goes in place that you are suggesting, do you?

A. I have no independent knowledge regarding that other than what Disco has presented.

Q.71 - But you agree the potential would be pretty significant to Disco and to its customers?

A. I believe it could. I don't -- I haven't seen any quantitative analysis of it. I understand that they cannot convert if capacity actually needed to be built to

serve them, which means at least the lights will stay on. There could be economic impacts as you push your way up the merit order, meaning that the fuel costs will be that much higher for all customers.

Q.72 - Right. For all customers. And therefore I assume that given this potential adverse affect such a change to firm power could have on Disco, wouldn't you agree that it's logical to study the affects of any further changes being added to interruptible power before imposing any of those, rather than acting on fairly quick notice without really a comprehensive review of the issue?

A. The issue I think that needs the study is the ability of customers to switch to firm service with very little notice, and I would agree that that requires some significant study.

Q.73 - But wouldn't you agree that one should know what kind of an impact that this -- any increase in interruptible power may have on customers and their switching to firm power before you impose that kind of an increase?

A. Well it depends on what kind of an increase we are talking about here. My proposal here is so modest that I would be very surprised if it would have a significant impact on the interruptible customer's decision. That decision is going to be driven much more by their

expectation for being interrupted and their expectation for incremental fuel costs, the effects both of which will dwarf a dollar and a half a megawatt hour contribution to fixed costs.

Q.74 - But the consequences of taking that chance are pretty profound, are they not?

A. I don't believe --

Q.75 - The potential consequences?

CHAIRMAN: Mr. Lawson, that's the third time you have re-emphasized that. I think we have got the point.

MR. LAWSON: Thank you, Mr. Chairman.

CHAIRMAN: Mr. MacDougall?

MR. MACDOUGALL: Thank you, Mr. Chair and Commissioners.

CROSS EXAMINATION BY MR. MACDOUGALL:

Q.76 - Good afternoon, Mr. Knecht.

A. Good afternoon, Mr. MacDougall.

MR. MACDOUGALL: Mr. Chair, I only have about 10 or 12 prepared questions. So I shouldn't be that long. However, Mr. Knecht did raise what he calls some form of progress matrix this morning that we had not seen before. And it is in relation to a portion of ENGB's evidence, that of Dr. Rosenberg. So I may have to spend a few minutes on that as well.

CHAIRMAN: You can have the time it takes.

MR. MACDOUGALL: Thank you.

CHAIRMAN: I'm not saying whether it is all today or over to Monday or whatever. But you certainly can have your time.

MR. MACDOUGALL: We will certainly try to get through it today, Mr. Chair.

Mr. Chair, I just want to start by handing out one document that I would like to have marked as an exhibit and that I would like to ask a couple of questions of Mr. Knecht on.

And, Mr. Chair, with the exception of a few other references, this is the only document that isn't currently in the records. So maybe we could just give this a exhibit number.

CHAIRMAN: It is another excerpt from the Bible.

MR. MACDOUGALL: Yes.

WITNESS: This appears to be the older Bible as opposed to the revised standard version.

MR. MACDOUGALL: The is the Old Testament, Mr. Chair.

CHAIRMAN: We are all referring to Bonbright's book. And this will be ENGB-16.

MR. MACDOUGALL: Thank you, Mr. Chair.

Q.77 - Now, Mr. Knecht, if we could go to your evidence. I'm sorry. I actually don't have the reference. But it is Mr. Knecht's evidence, page 5, line 18.

A. Yes, sir.

Q.78 - And on page 5, line 18 you state that of the traditional rate design criteria, the most common non-cost considerations in the revenue assignment process are a) the principle of gradualism or avoidance of rate shock in which large rate increases for individual customers or classes of customer are avoided, and b) the value of service principle. Correct?

A. Yes.

Q.79 - If we could go to Professor Bonbright's text, exhibit EGNB-16. And if we could go to page 291 which is the second page.

I just want to read out the top sentence there that says, The sequence of the eight items is not meant to suggest any order of relative importance.

And then he lists what is known as "Criteria of a Desirable Rate Structure", correct?

A. Yes.

Q.80 - And number 8 is "Efficiency of the Rate Classes and Rate Blocks in Discouraging Wasteful Use of Service While Promoting all Justified Types and Amount of Use", correct?

A. Yes.

Q.81 - And then at the bottom you will see a reference that says "Three Primary Criteria." Do you see that?

A. Yes.

Q.82 - And if we could go over to the next page, the first full paragraph. And that paragraph starts "Among these objectives three may be called primary, not only because of their widespread acceptance but also because of the more detailed criteria are ancillary thereto." Do you see that?

A. Yes.

Q.83 - And of what Professor Bonbright calls the three primary criteria, could you read in number (c), the third primary criteria from Professor Bonbright?

A. (c), the optimum use or consumer rationing objective under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships between costs incurred and benefits received.

Q.84 - Thank you. And of those three primary criteria, including looking at number (a) and (b) as well as number (c), none of those three primary criteria from Professor Bonbright are either of the two, what you call most common non-cost considerations in the revenue assignment process, are they?

A. Well, let me point out you are comparing apples and

oranges. First off, of the three primary criteria, the first two are cost-related. So therefore by definition they are not non-cost.

The second thing that I would point out that you are -- where you are comparing applies and oranges is this section of my evidence relates only to the part of the rate design process which is allocating the revenue requirement between the rate classes.

And I view that the overall process of rate design to which the Bonbright text relies as three significant steps. One is the allocation of costs to the rate classes in the cost allocation study. The second is the allocation of the revenue requirement to each of the rate classes. And that's the criteria that I was talking about in this step. And the third step is the design of the rates within each rate class.

In the Bonbright text he is designing rates. He is laying out these objectives for all three steps. The portion of my testimony or my evidence that you quoted relates only to the second step.

Q.85 - And that is fine, Mr. Knecht. That is what I wanted to get clear. And you would acknowledge though that of the three primary criteria that Dr. Bonbright sets out with respect to the overall process, one of what he calls the

primary criteria, is the efficiency of the rate classes and rate blocks in discouraging wasteful use of service, correct?

A. He does. And he also specifies I believe here in part (b) fair cost, a fair -- the fairness or equity standard for allocating the revenue requirement between the rate classes.

Q.86 - Correct. Thank you very much. Now go to page 3 of your evidence, line 7. Here you say, while it may reasonably be argued that these fuel costs are more related to either peak demand or seasonal energy than they are to annual energy, they are not related only to demand by electric heat customers.

For the record could you just indicate what fuel cost you are referring to there?

A. This is the CT costs that I discussed in my direct evidence this morning.

Q.87 - Correct. This is just the CT costs -- or is it the CT costs and the emergency purchases?

A. I believe it's the whole pool.

Q.88 - Okay. Great. Thank you. So you do not disagree that such fuel costs are more related to peak demand or seasonal energy?

A. I would not disagree with that. That interpretation

might not be consistent with the Board's methodology.

Q.89 - Yes. But you don't disagree with it?

A. I would probably not. If I only looked at those costs and particularly it was in a marginal cost framework, everyone who is contributing when those costs are on, should be paying for those costs. And if you are only consuming when those costs are not being incurred, then you should not necessarily contribute to them.

Q.90 - Sure. And I'm not --

A. So there is a philosophy of cost allocation issue here and there is the Board's ruling on what that cost allocation methodology should be.

Q.91 - Sure. And I agree with that and I'm not going to your underlying point. I just wanted to come back just to make sure. You do not disagree that those types of fuel costs are more related to peak demand or to seasonal energy?

A. As a theoretical matter I would not disagree with that.

Q.92 - Good. Thank you. And would you concur that for Disco oil and gas fuel costs are distinctly weighted to the peak winter months?

A. Yes, I would. I think one of the issues that -- as a caveat to that I would say is that -- you know, is that the oil costs are -- a significant amount of the winter

related oil costs are related to the high oil costs at Coleson Cove, which at least at one point I believe NB Power had hoped to mitigate anyway through the use of Orimulsion.

Q.93 - Sure. But certainly the data that is shown -- and I don't think we have to go to the IR responses, we could -- I mean, you would concur that for Disco oil and gas fuel costs are distinctly weighted to the peak winter months under the current structure?

A. I would agree, yes.

Q.94 - Thank you. And there is a more pronounced distinction for oil and gas fuel costs in the winter months for either coal, Pepcoke or Orimulsion, correct?

A. The -- I think that was -- I'm not sure how that question is different from the first one.

Q.95 - I'm just comparing it to the other fuel costs that are not as pronounced in the winter months, correct? Again I can bring you to the --

A. Certainly the fuel costs as currently incurred by Genco in the winter are higher than they are in -- they are higher in the winter than they are in the non-winter period because there is a higher proportion of the higher cost -- -oil and gas costs, yes. That's not --

Q.96 - Good. Thank you.

A. That's certainly correct.

Q.97 - But just so that we are all clear on this and for the Board's record, in the CCAS all of the fuel costs are allocated on the basis of annual energy, correct?

A. That's correct.

Q.98 - So currently the CCS reflects no seasonal differentiation in the allocation of the fuel cost?

A. It does not.

Q.99 - Thank you. And if we could go to -- still on page 3, line 25. And here you have noted just in going through your review of Mr. Larlee's approach to CCAS, that Disco has classified the export sales credit as 100 percent demand related consistent with the CARD ruling, correct?

A. Yes.

Q.100 - And Disco itself had proposed this classification in its evidence, correct, from the CARD ruling?

A. Yes. For this specific component, yes.

Q.101 - Yes. For that component. But at the time they had proposed that they had also proposed that the generation fixed costs for Genco be classified 100 percent demand, correct? I'm just talking about what they actually proposed?

A. They had proposed that part of the PPA from Genco that was demand related be classified as a -- I'm sorry. Can

you repeat your question?

Q.102 - Yes. I just said that Disco had at the same time they proposed the export sales credit as 100 percent demand related they had proposed that the generation fixed costs for Genco, not for Nuclearco, also be classified 100 percent demand, of course they were basing it on the PPA?

A. The only reason I am hesitating, Mr. MacDougall, is there was a piece of the Genco cost that was split 60/40. The O&M -- the fixed O&M cost was split 60/40. So when you say Genco fixed costs, I'm having trouble saying that they were all -- that they were all demand related.

Q.103 - The generation fixed costs.

A. But yes, I agree that the export sales credit and the -- or I'm sorry -- that the -- that there was a different -- within Disco's overall proposal was a different classification of generation costs than that which was subsequently adopted by the Board.

Q.104 - Okay. And this ruling -- and again just to get clarity so that we are all on the same page, this benefits the residential class in that there were less cost charged to demand under what the Board ruled and the full export credit goes to demand, correct?

A. This methodology will assign a greater proportion of the credit to the residential class than other

methodologies, such as an energy or a demand energy split.

Yes, that's correct, within the cost allocation study.

Q.105 - Great. Thank you very much. And then if you could go to page 8 in the footnote. And I think you referred to this this morning. So I won't go into it in any great detail.

You indicated that you and Ms. Chown have presented evidence when you were here previously in support of the cost offset approach, correct, with respect to the export credit?

A. We did. We did for the reasons that I explained in my direct evidence.

Q.106 - Yes. And I won't come back to that.

So would you agree that off system revenue should go to offset the cost of native load?

A. I'm struggling with how to answer that. Because I don't know whether we are talking about as it should apply only to NB Power or as a general rule of regulation or --

Q.107 - Let's start as a general rule of regulation and then go to NB Power.

A. As a general rule of regulation it would depend on the, you know, regulatory -- the legal and regulatory structure of the jurisdiction.

In general it has been my experience with traditional

regulated utilities that if they earn revenue from off system sales of some form there is either a sharing or a credit of those revenues with the franchised ratepayers.

Q.108 - Thank you very much. And now if we can go to page 6, line 8 -- I'm sorry, line 18, Mr. Knecht. So page 6, line 18?

A. Yes, sir.

Q.109 - Here you say "In the present circumstances in New Brunswick a number of factors militate against assigning a very low rate increase to large industrial customers", correct?

A. Yes.

Q.110 - And from Appendix A-121 which was the update of Disco's material, my understanding is Disco is proposing a rate increase to the large industrial class of 12.1 percent, correct?

A. Yes. Let me -- just to clarify, this paragraph is a paragraph -- this question and answer within my evidence was one that was excerpted from my September evidence.

Q.111 - Okay.

A. So it was -- this particular sentence was in the context of the proposed increase at the time, which I believe was zero for the large industrial class.

Q.112 - Okay. But now we are in this phase. So I want to get

this very clear for the Board. You are not saying to this Board that a 12.1 percent increase is a very low rate increase are you?

A. No, I'm not.

MR. MACDOUGALL: Thank you. If you just give me a moment, Mr. Chair, I will knock out a few questions. It is getting towards the end.

CHAIRMAN: I'm in favor of that, Mr. MacDougall.

Q.113 - If we could go, Mr. Knecht, to page 6, line 28. Here again you are talking about large industrial customers. And you were talking about the allocation of cost. In the very last line you used an example from Quebec. You say in fact in Quebec the enabling legislation mandates retention of historical revenue to cost ratios which exceed 115 percent for large industrial customers?

A. Yes.

Q.114 - Could you tell us what the absolute rate is for electricity for large industrial customers in the province of Quebec?

A. I believe you asked me this last fall on the same quote from the same evidence. I don't know exactly what it is for large industrial customers. And I would have to go look it up. It's --

Q.115 - Order of magnitude?

A. -- probably on the order of 40 to $50 a megawatt-hour when you add in the transmission costs which are relatively high and the mandated revenue to cost ratio.

Q.116 - Sure. 4 to 5 cents a kilowatt-hour?

A. 4 to 5 cents a kilowatt-hour, yes --

Q.117 - Thank you.

A. -- should be ball park, subject to check.

Q.118 - Sure. And are you aware that jurisdictions have contract rates for industrials?

A. Yes.

Q.119 - And those contract rates don't usually show up in revenue-cost ratios in jurisdictions where they exist?

A. They don't -- they tend not to show up in revenue to cost ratio calculations. The issue is whether -- if there is a discount for contract rates that's being borne by the utility, or in the case of a provincially-owned utility by the Province or whether it's being borne by the other ratepayers. That I think can vary significantly.

Q.120 - Thank you very much.

And just before we go to the progress metric questions which will be my last questions, Mr. Knecht, I just have one question before that. Page 17, line 8. I guess it starts on line 7, you say it is relatively common for customer charges to be modestly, and then you say, or

sometimes significantly below customer costs?

A. Yes.

Q.121 - Could you explain why sometimes customer costs can be significantly below their actual costs -- why customer charges can be significantly below their customer costs?

A. I believe that in my experience the reason that you see that is that ratepayer advocates, particularly for the residential class in the United States, and public utility commissions in the United States, are looking at the customer charge as a lower customer charge to provide a little break to lower income customers, and therefore they are willing to set that charge below cost as a -- almost for policy reasons.

You see customer charges well below customer costs much more frequently in the United States than you do in Canada.

Q.122 - Thank you, Mr. Knecht. That's what I thought was their reasoning. Now, Mr. Chair, I just have a few questions arising from the document that Mr. Knecht put forward this morning, and I think that was -- if I have got it correct, PI-24. It's his so-called Progress Metric Analysis and I think he has used some of Dr. Rosenberg's proposals.

Just a couple of -- just to give us a couple of

starting points, Mr. Knecht. Again if I looked at exhibit A-121 which again was the update to Disco's evidence. and So it was the update to the table 1 of Disco's revenue requirement evidence, so it's Appendix -- or it's exhibit A-121, page --

A. Give me a minute, Mr. MacDougall. I had it handy. There it is.

Q.123 - It would be page 3 of that appendix which is the updated Table 2 of Mr. Marois' evidence.

A. Yes, sir. I have it now.

Q.124 - When I'm looking at that, you have a column here that says RC Ratio at present rates. However, we look at column 1 of Disco's appendix, it says revenue to cost at July 7, 2005, rates, which is again the present rates, yet we see that all of the RC ratios are different. I just want to make sure that we get this clear.

In Disco's table they are only recovering 91 percent of their costs at present rates. So when you say present rates here you must have done something though to get the total up to 100 percent and to get the RC ratios changed, because at present rates these aren't Disco's RC ratios. So maybe you can explain to us what you did there and why you used the word present rates?

A. Yes. The first column in my exhibit PI-24 is

comparable to Column 2 in Disco's exhibit. What I call an RC ratio at present rates I should have said that that's what I described as normalized revenue cost ratios such that all the revenue cost ratios are adjusted so that overall they are at 100 percent. It's essentially the same calculation as that presented by Disco in Column 2.

Q.125 - Okay.

A. So that when we are comparing present rates to proposed rates we are only looking at progress towards cost based rates on, as Mr. Marois said, an apples to apples basis.

Q.126 - Sure.

A. So this is more comparable to Columns 2 and 3 than to Column 1.

Q.127 - Yes. So your Column 1 though here at present rates already has built into it an average increase of 11.4 percent for all those customers, correct?

A. You can describe it that way or you could describe it as a normalization of the revenue to cost ratios such that the revenue requirement is deemed only to be the revenues that are actually collected at the time.

Q.128 - Sure. But the way I described it isn't incorrect. It already has that average rate increase built in?

A. You could describe it either way.

Q.129 - Thank you very much. Now I note when I look at Disco's table that they never break the large industrial class out. But here you did break the large industrial class out because you said earlier today for the same reason Dr. Rosenberg talks about more information being better you thought you would do that, correct?

A. There is actually two reasons there. I have done two things that are different from what Disco did. One, I split out -- I took the interruptible/surplus customers out entirely, and then the second is I broke the large industrial into distribution voltage and transmission voltage.

Q.130 - Sure.

A. The latter segregation I did for the reasons consistent with what Dr. Rosenberg said. The former was for more fundamental reasons related to the different character of the service.

Q.131 - Sure. But just so that we know here, comparing it to the one rate class that we have of large industrial, you don't have surplus or interruptible here and now you are breaking it into two distinctions which are not distinctions in the actual rate class that Disco is charging its rates to, correct?

A. Yes. They are not distinctions in the rate class and

I have split them out, yes.

Q.132 - Okay. But you didn't split out the residential even though Disco always shows the residential. How come since that has been showing as being split out all the time you didn't do it either the first time around in your evidence and you didn't do it in either of these exhibits, if you were trying to show more information? Why did you neglect to continue doing that consistent?

A. Honestly I actually don't have an awful lot of confidence at this point in the split between the electric and the non-electric heat. I don't think there was anything malicious in my not including it. I just don't -- some of the splits that Disco has there were subject to some debate in the fall proceeding about how seasonal customers got included in electric heat in one place and not included in another. There has been a fair amount of evidence I think both in this proceeding and the last proceeding that it's a little bit of an arbitrary distinction about which customers are where. I -- you know, if it would help I would certainly be happy to make versions of these exhibits, you know, with that distinction, with those caveats?

Q.133 - No. I don't think I need it. I just want to try and get clear on the record what it is that you had been

showing here.

A. I have some concerns about the level of detail in Disco's study regarding those two, but, you know, perhaps I should have.

Q.134 - Maybe if we could now look at large industrial distribution and transmission, and Dr. Rosenberg didn't distinguish between those classes in his recommendations, correct?

A. That's correct.

Q.135 - Okay. So it's hard for me to compare anything that he said to what is here because you have broken the two up, one that's at 100 percent and the other at 87.57. But if we could just turn to EGNB-7, just to try and get some clarity on this.

A. EGNB-7 is?

Q.136 - Is response to undertaking March 2006?

A. I may not have it.

Q.137 - Maybe your counsel could provide you a copy. Because I think you should take a look at it.

MR. HYSLOP: I do not have that exhibit with me, Mr. MacDougall.

MR. MACDOUGALL: EGNB-7, response to transcript reference March --

A. I have it.

Q.138 - You have it? And here I just wanted to see -- there were some questions asked to Dr. Rosenberg. Because in his evidence he hadn't broken up how he was going to allocate the $8.7 million.

And here he does say that he would propose applying 4.4 million to the small industrial class in recognition of the greater RC ratio of this class. The remainder of the 4.3 million would be used to moderate the increase to the large industrial class?

A. Yes.

Q.139 - When you did your progress metric here, did you allocate all of the 8.7 million to the large industrial class? Or were you aware of this response and only allocated the 4.3 million?

A. What I did to create this table is I took the specific -- I took the specific tariff charges that Dr. Rosenberg proposed for the residential class and I believe the General Service class -- no, I'm sorry, just for the residential class.

And I determined -- and I set the GS I class to zero as he proposed. Then I calculated on what was left.

Q.140 - Yes.

A. And I didn't actually get the 8.7 million that Dr. Rosenberg has here. I got about 9.5 million. So I

took that 9.5 million. And I did use his response.

And I assigned the 4.4 million to the small industrial class to get it to 95 percent revenue to cost ratio which is what Dr. Rosenberg proposed. And then I assigned the residual to the large industrial class.

Within the large industrial class, to keep this exhibit consistent with the prior exhibit and have the split, I simply did a pro rata sharing of that based on current revenues.

Q.141 - Okay. So what you did was pro rata split between two parts of the large industrial class which Dr. Rosenberg didn't do and which Disco doesn't do.

And you allocated a number greater than what Dr. Rosenberg said he was allocating, because your math didn't come out correct, correct?

A. Well, I don't know how Dr. Rosenberg got the 8.7 million. Because when I put his specific figures into the billing determinants for the residential class I seemed to be getting more revenues than he was predicting.

Q.142 - But you did allocate those extra revenues in preparing this?

A. That was my best understanding of how Dr. Rosenberg's logic would work. Because he said he targeted the small industrial class at 95 percent revenue to cost ratio.

Q.143 - Sure. And I guess did you hear Mr. Harrington's evidence today that EGNB's primary interest is in sending the correct price signals to the residential and the GS classes?

A. Yes.

Q.144 - Okay. So if the Board wanted to reallocate the 8.7 million here, for example, if they wanted to use some of that money to reduce, for example, the wholesale class which is at 105, in the same way that Dr. Rosenberg said you could do with the small industrial class, the Board could certainly do that, correct?

A. Yes.

MR. MACDOUGALL: Could you just give me a minute, Mr. Chair. I just have a couple of other questions.

Q.145 - And here I just want to try and get this progress metric correct in everybody's mind to just see what happens here. I think this clarity may be useful. In your progress metric what you are actually looking first off is movement to unity. You are not comparing any movement here to within the Board-approved 95, 105 range are you?

A. Yes. I thought about that. And you could certainly make a reasonable case for trying to measure the progress metric that way.

But in general, even when you are within the 95 to 105 range, and you have some confidence in your cost allocation study, I still think some progress towards unity has value. And therefore I did it based on unity, yes.

Q.146 - Sure. But the Board has actually allowed Disco a range between 95 and 105. And progress towards getting to 95 is obviously something that the Board considers useful, correct?

A. Yes.

Q.147 - Thank you. And now just to be even clearer, what you have then done is you have taken how far a class is coming, right?

And you have taken the percentage in the change from how far from unity it is, correct?

A. Yes.

Q.148 - So that means that a class that starts farther from unity, correct --

A. Yes.

Q.149 - -- would obviously need a much larger increase to have a higher progress metric, correct, because they are coming from a farther distance?

A. And I would argue that that would be more appropriate. Because they are farther away. And therefore you should

be giving them a larger increase. If you have a class at 94 percent and you have a class at 88 percent, to give them both the same increase doesn't make much since. And it will not make as much progress towards cost-based rates.

Q.150 - Yes. But you cannot -- if you are farther away, to get an equivalent progress metric, you have to have a much higher increase, correct? That is just mathematically the way it works?

A. "Much" is a subjective determinant. You take the word "much" out of that, I will agree with you.

Q.151 - Okay. You have to -- depending on how far away you are, you have to have a bigger increase to have a bigger progress metric, correct?

A. That's exactly right. And that's exactly the point.

Q.152 - So those classes that are farther away would not be expected to have as high a progress metric unless they had a larger increase, correct?

A. Yes.

MR. MACDOUGALL: Thank you very much. Mr. Chair, that's all my questions. I don't think I have beat Mr. Lawson but I think I beat my own estimate.

CHAIRMAN: Yes. I think you did too. Thank you, Mr. MacDougall. Mr. Gorman, do you want to ask your questions

from there?

MR. GORMAN: Sure. That might save some time. And since I estimated five minutes don't expect that I will achieve the same level of savings. In fact I was going to ask whether or not I can have the time they didn't use.

CHAIRMAN: The answer is no.

CROSS EXAMINATION BY MR. GORMAN:

MR. GORMAN: I rather suspected that. And before I ask my questions, I remember Mr. Morrison on the 14th of February wished everybody a Happy Valentine's Day. So I would like to wish everybody a Happy St. Patrick's Day tomorrow. Now that we have got that in and that's part of my five minutes.

Mr. Knecht, if I could take you to page 9 of your report, and I'm referring to the table on page 9, and I want to refer you to large industrial firm transmission, and I just want you to explain how you got there, how you got that number. I understood from your response to Mr. MacDougall that the cost offset numbers in your table came from one of the tables in Mr. Marois' evidence?

A. All the figures in this table are from the CCA, yes.

Q.153 - Okay. So where did those numbers -- in the cost offset method, the first column, where did those numbers come from?

A. They were from the company's CCAS that I have an electronic version of. I needed to probably do some calculations to get the revenue cost ratios to split out between the large industrial -- distribution and large industrial firm transmission. But the numbers are all available within the study to do that calculation.

Q.154 - So in breaking down between large industrial distribution and large industrial firm transmission what did you do with the interruptible? Is there some difference with respect to what is in the Disco report and yours with respect to interruptible? Did you do something different?

A. Yes. I did two things different. Mr. Marois' table reports the entire large industrial class which includes distribution voltage firm, transmission voltage firm and interruptible/surplus. I took interruptible/surplus out entirely from this calculation and then I split the firm customers into distribution voltage and transmission voltage.

Q.155 - Okay. And that resulted -- and if I go down to the large industrial firm transmission using the cost offset method in 89.9 percent revenue to cost ratio?

A. Yes, sir.

Q.156 - And when you didn't take the interruptible out and if

you put the two together going to table 2, my understanding is it would have been at .91. So it's actually two percent less, would that be correct?

A. Yes, that's true, because the interruptible classes as we discussed under Disco's proposal is slightly above 100 percent, 102 percent or so. So when you take that factor out it lowers the overall average.

Q.157 - Okay. So would it be fair to say then that your evidence would be that based on the CCAS that has been filed for large industrial firm transmission taken separately that their revenue to cost ratio if approved at the present level would be 89.9 percent?

A. Yes. Using the cost offset method, yes.

Q.158 - Mr. Knecht, I would like to take you to page 11 of your evidence. And I'm looking at the first full paragraph after your table RDK-2, and I'm referring to the last sentence which says, despite the above system average rate increase for the residential class, Disco is not able to make significant progress towards cost base rates for General Service customers primarily because relative little progress was made by firm large industrial transmission customers. Do you see that?

A. Yes.

Q.159 - Do you agree that that would hold true for any class

with a revenue to cost ratio over unity?

A. Would I agree that the ability of Disco to -- yes, I would agree that the ability of Disco to get any rate class that is above unity closer to unity is constrained by the progress towards cost base rates of the large industrial class.

Q.160 - Thank you. Now I'm going to take you to page 18 of your report. And at the top of page 18 you say, Second, it is my understanding that any reduction in the revenue requirement will likely relate to distribution costs which are not allocated to large industrial transmission customers. Since those customers will not see any cost reduction associated with any adjustment they need not share in the revenue reduction. Similarly wholesale customers should also not see reduced rates as a result of any such change. Do you see that?

A. Yes.

Q.161 - What about the hydro savings this year if in fact they are applied to the test year, should all customers in that case not share?

A. If there is a savings in generation costs I believe that all rate classes should share.

MR. GORMAN: Thank you. I have no further questions.

CHAIRMAN: Thank you, Mr. Gorman. Mr. MacNutt, you don't

have any questions do you?

MR. MACNUTT: Board staff have no questions for this witness, Mr. Chairman.

CHAIRMAN: Okay.

BY THE BOARD:

MR. BELL: Good afternoon, Mr. Knecht.

A. Good afternoon.

MR. BELL: On your proposition that interruptible customers had value, if they contribute something greater that their marginal cost, or rather incremental cost, and secondly cannot move readily back and for the between interruptible and firm, I understood earlier -- on short notice rather -- and I understood earlier from evidence from Disco that there was at least a one year requirement to notify if there is a change, would that be in your opinion be an unreasonably short notice?

A. Yes.

MR. BELL: It would be?

A. Yes.

MR. BELL: What would you have in mind as a reasonable notice?

A. I don't know that I have a definite answer to that. And I wish I could say that I went and studied everybody elses' rules, but you know big capacity valleys,

particularly in a place with a relatively small overall load like New Brunswick can last a long time. You know, three years, five years, I think would be -- would provide the utility with some planning benefits.

MR. BELL: Thank you.

DR. SOLLOWS: Yes. I want to refer to EGNB-16, which is the photocopy of the Bible according to Bonbright. And I was looking at page 292, actually Vice-Chairman Nelson pointed this out to me. The three principal ones that Mr. MacDougall pointed out to you, reading the first one it says, "(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies." Now, we aren't dealing with a private utility company. And so is there any place in Bonbright where we would find specific reference to the fair-return standard for publically-owned utility companies?

A. I don't know.

DR. SOLLOWS: Well that is a short and quick answer. Thank you.

A. The return for publically-owned companies is not one of my areas of expertise, with the proviso that almost anybody can find something in Bonbright that he likes.

CHAIRMAN: Either the Old or the New Testament. Those are

all the questions, Mr. Knecht. Thank you for your testimony.

MR. KNECHT: Thank you, Mr. Chairman.

MR. MORRISON: Mr. Chairman, before we close off for the day, if we could have a few minutes. We have some more undertaking responses we would like to get on the record. They haven't been delivered to the Board Secretary yet. So if we had five minutes to get the paperwork straightened out, we could get those on the record.

CHAIRMAN: You can put them on the record on Monday. The record will not close. Now, Mr. Hyslop, I didn't give you the opportunity of redirect. Do you have any, sir?

MR. HYSLOP: This panel and this Board and the participants will be eternally thankful to Professor O'Rourke, who has informed me I have no redirect.

CHAIRMAN: I knew that he would come up with something sensible.

MR. MORRISON: Mr. Chairman, the only reason I thought we would try to get them on today in the event that some of the Intervenors can get these for final argument preparation and so on. So it would take a couple of minutes.

CHAIRMAN: Yes. All right. But I won't require -- I won't require anybody who doesn't want to to stay. I will stay.

These fellows will probably go.

MR. MACNUTT: And just for the record, Mr. Chairman, if Mr. Knecht could be formally discharged of his duties.

CHAIRMAN: He already has.

MR. MACNUTT: I missed it.

CHAIRMAN: That I did do. Okay. So you take your time and just come and knock on the door and we will give it an exhibit number and put it on the record. Anybody who wants -- can you inform people what these questions are that you are working on so they will know whether they want to stay or not?

MR. MORRISON: Well the first one is actually -- it's a request by yourself, Mr. Chairman. It relates to the NUG issue, dispatchability of the NUGs.

CHAIRMAN: Yes.

MR. MORRISON: And as you know, the Board has already adjudicated on that issue that the NUGs don't have to be produced and information about them don't have to be produced. But we have gone to great lengths to try to get this information and get the consents of the NUGs to have it filed with the Board in confidence. So it's from February 23rd. So it will be filed with the Board in confidence.

CHAIRMAN: Sorry. I missed the last?

MR. MORRISON: It was requested by you on February 23rd.

CHAIRMAN: Yes.

MR. MORRISON: And we will be filing that with the Board in confidence on the pink paper.

CHAIRMAN: Okay. That's good. We will -- those who don't wish to stay, we will be reconvening this hearing on Monday morning at 10:00 a.m. There is one member of the public who Mr. Young informs me has maybe 15 minutes and then we will get into summation.

MR. MORRISON: Just so everybody else knows, the next one is a request from Commissioner Sollows. Again this deals with the dispatchability of the plants. This one is not confidential, because it's just a reference to a previous IR.

Undertaking number 5 from yesterday, it's from Mr. Hyslop and it dealt with the minutes of the Operating Committee when the change in the methodology was first raised.

And the last one is also from yesterday and it's from Commissioner Nelson. And he wanted to know what the difference would be up to the end of February. So those are the four undertaking responses.

CHAIRMAN: Good. Thanks, Mr. Morrison. You knock on the door when you are ready.

MR. MORRISON: Apparently, we are ready. They worked their magic behind my back, Mr. Chairman.

CHAIRMAN: The first exhibit is A-161. It was a request from the 23rd of February. It doesn't show -- well, of course, it wasn't an official undertaking.

MR. MORRISON: That's correct.

CHAIRMAN: So you don't have a number. But it was as a result of my request. And it comes in both the expunged version and confidential. So the expunged will be A-161. And the pink version is A-161(C).

The next is again -- it has to do with a request by Commissioner Sollows on the 22nd of February. And the question is dispatching the plants and capacity available in the province on a purely economic basis, what would be the estimated cost to Disco? And that will be A-162.

Yes. A-162.

The next will be A-163. And that's undertaking number 15 of March 15th, request by the Public Intervenor.

MR. MACNUTT: I understand that it is undertaking number 5 it should be, Mr. Chairman.

CHAIRMAN: Yes. What did I say, Mr. MacNutt?

MR. MACNUTT: 15. Unfortunately you said 15.

CHAIRMAN: Okay. You are right. The next one is undertaking number 6, March 15 and that will be A-164.

MR. MORRISON: That's it, Mr. Chairman. Thank you very much.

CHAIRMAN: Thank you. And we reconvene on Monday at 10:00 a.m.

(Adjourned)

Certified to be a true transcript of this hearing, as recorded by me, to the best of my ability.

Reporter