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.
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CHAIRMAN: Good morning, ladies and gentlemen. I hope everybody is rested and rejuvenated and ready to cut the verbiage and get on with it.

Could I have appearances please for the applicant?

MR. MORRISON: Good morning, Mr. Chairman and Commissioners. Terry Morrison and David Hashey for the applicant. And with us at counsel table is Lori Clark.

CHAIRMAN: Thanks, Mr. Morrison. Canadian Manufacturers and Exporters?

MR. LAWSON: Gary Lawson, Mr. Chairman.

CHAIRMAN: There you are. Good morning, Mr. Lawson. Conservation Council?

MR. COON: David Coon for the Conservation Council, Mr. Chairman.

CHAIRMAN: Good morning, Mr. Coon. Eastern Wind? Enbridge Gas New Brunswick? The Irving Group of companies?

MR. BOOKER: Good morning, Mr. Chair and Commissioners. Andrew Booker and Bruce Nicholson for JDI.

CHAIRMAN: Good morning, Messrs. Booker and Nicholson. The Jolly Farmer is not here. Mr. Gillis is obviously not here. Rogers Cable? Self-represented individuals? Municipal Utilities?

MR. GORMAN: Good morning, Mr. Chairman. Raymond Gorman appearing on behalf of the Municipal Utilities. And this morning I have Dana Young and Michael Couturier with me.

CHAIRMAN: Thank you, Mr. Gorman. And Vibrant Communities? Public Intervenor?

MR. HYSLOP: Good morning, Mr. Chair. Peter Hyslop with Robert O'Rourke and Carol Power.

CHAIRMAN: Thanks, Mr. Hyslop. Any Informal Intervenors present? And, Mr. MacNutt, whom do you have with you today?

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

CHAIRMAN: Thank you, Mr. MacNutt. I'm almost afraid to ask this question. Any preliminary matters?

MR. MORRISON: No, Mr. Chairman.

CHAIRMAN: I knew it. Mr. Hyslop?

MR. HYSLOP: I regret to advise I have two documents I wish to get on the record, Mr. Chair.

First I left with the Secretary a sufficient number of copies of Mr. Knecht's pre-filed evidence which we filed with the Board on Friday electronically.

CHAIRMAN: My records indicate that should be PI-18.

MR. HYSLOP: Thank you, Mr. Chair. And the second, Mr. Chair, you might recall Mr. O'Rourke's homework that we looked at a week and a half ago. And we had put a document in last week. But there were some issues over the wording.

The issues over the wording have been settled. And the chart is I guess in its final form. And I would ask that that be marked as an exhibit.

I have reviewed the wording with Ms. MacFarlane and Ms. Clark. And they indicate that we are all in agreement on that issue.

CHAIRMAN: All right. So this is a revised PI-17 exhibit?

MR. HYSLOP: That would be correct, Mr. Chair.

CHAIRMAN: Okay. Well, I will put it in under PI-17, revised on February 20.

Anything else, Mr. Hyslop?

MR. HYSLOP: That is all I have at this time, Mr. Chair. Thank you.

CHAIRMAN: Any other preliminary matters? Continue, Mr. Lawson.

MR. LAWSON: Thank you, Mr. Chairman. I won't be long. This time I promise I won't be long.

CROSS EXAMINATION BY MR. LAWSON:

Q.243 - Good morning, panel members. Just to start off, perhaps you could explain what the rationale was for Disco in withdrawing its application for a fuel adjustment in its increase that was filed initially and then was subsequently withdrawn.

What was the rationale for not reinstating that as part of this new rate application?

MR. MAROIS: The key reason for not proposing a fuel surcharge at this stage was in our initial application which was for 05/06 the fuel surcharge was an integral part of trying to get an expedited decision from the

Board.

If you recall, when we filed our 05/06 application it was to be dealt with in two phases. And phase one was to deal with the fuel surcharge and the company variance account. And at the time we knew we had limited time to deal with all the issues of the case in order to get a decision in time to allow rates to be effective April 1 of '05.

So one way of dealing with the short time frame we had was to propose to deal separately with the fuel cost increase, have the Board deal initially with the fuel surcharge and hopefully get it implemented in time in combination with the variance account to be able to recover costs effective April 1st '05. So it was an integral part of the strategy at that time.

Q.244 - But what was the reason for dropping that component of the application this time and not making it sort of a component of the current application?

MR. MAROIS: Well, when we modified the application from an 05/06 to an 06/07 it was a totally different situation.

And then we just rolled in the increase in fuel costs with the normal increase in costs and rolled it into the rate increase. Because there was a lot more time in front of us to deal with the application.

Q.245 - When you made the initial application, I presume -- with the adjustment provision, I presume you felt that that was an appropriate way to deal with the fuel adjustment price changes, I will say, usually increases but price changes, is that right?
MR. MAROIS: Yes. Again what we were hoping for was it provided opportunity to deal with increases in fuel costs in an expedited manner. And our evidence supported using the fuel surcharge.
Q.246 - Now I'm gathering from the evidence that -- moving to another subject, by the way -- that in the course of the 06/07 period, that there is going to be a reduction in the power supplied out of Point Lepreau because of I gather sort of the aging facility, is that correct?
MR. KENNEDY: Yes.
Q.247 - Okay. And I presume that as it gets older this is going to become -- and prior to refurbishment commencing this will become progressively worse assumedly?
MR. KENNEDY: Assessment is done with respect to the capacity factor and availability off of the nuclear station. And that's factored into establishing the fuel component with respect to the vesting price.
The assessment is done based on a gradual slight degradation with respect to performance.

Q.248 - And am I correct in assuming that Genco has the contractual obligation to supply the replacement power to Disco that is lost as a result of the reduction in capacity out of Point Lepreau? Is that correct?
MR. KENNEDY: Yes. Genco has the obligation to backstop the lost energy supply from Point Lepreau.
Q.249 - And how does Disco, presumably in conjunction with Genco, intend to control the costs of that replacement power as one gets closer to refurbishment and then the course of refurbishment?
MR. KENNEDY: The answer to that question is that basically we are moving beyond the test period with respect to the case with the test year being 06/07 budget. And in that period, test period, the appropriate capacity factor has been budgeted.
And as a result of that, the fuel component price of the vesting energy price has been set. And it's fixed. And it's fixed for the year 06/07 budget year. And it doesn't change with respect to the performance of Point Lepreau.
Q.250 - Does Disco not have any particular plans as to how to address the issue of minimizing the cost of replacement power during the period that Point Lepreau is down?
MR. MAROIS: I guess there is two facets to that question.

From a customer's perspective the impact of the outage, there is the cost side of it but also there is how we recover those costs. I mean currently the way the Nuclearco power purchase agreement reads is the fixed costs during the outage would remain with Nuclearco. So that's the way it reads right now. And that creates a challenge, as Ms. MacFarlane mentioned the other day. The detailed plan on how replacement power will be obtained during refurbishment is not finalized yet. But just intuitively we know what is going to happen at a high level. I mean we will have to maximize the existing generation facilities and it's also going to reduce the possibilities to do export. So the export benefit does go down significantly during the outage and that's spelled out in the PPAs.

So the question becomes do we try to recover these costs in one shot, one lump sum from the customers, or do we spread that over time to recognize the long-term benefits of the refurbishment. And that we don't have a final strategy yet to deal with this.

Q.251 - Are there any specific initiatives though that are being taken by Disco to minimize that replacement cost -- replacement energy cost?

MR. MAROIS: Well all options are being looked at as we speak. Like I say the object is to maximize the existing resources but then there is going to have to be a cost benefit analysis of doing more -- in purchasing power at a specific point in time.

We are going to talk with the large customers to see if there is any opportunity to further do some curtailment at specific points in time. We are even looking at the possibility of advancing some of the renewable but there seems to be limited opportunities there. So everything is on the table as we speak.

MR. LAWSON: Those are all the questions I have, Mr. Chairman. Thank you, panel.

CHAIRMAN: Thank you, Mr. Lawson. Mr. Coon, do you have any questions of this panel?

MR. COON: Yes, Mr. Chairman, I do.

CROSS EXAMINATION BY MR. COON:

Q.252 - Good morning. My questions are all I guess around the power purchase agreement with the nuclear company. My first question is is this the only contract Disco has with any other branch of NB Power concerning the refurbishment or the purchase of power from the nuclear company?

MS. MACFARLANE: Yes, it is.

Q.253 - Now have there been any amendments or additional schedules added since the power purchase agreement was first signed?

MS. MACFARLANE: No.

Q.254 - Was there any direct guidance provided by the provincial government or consultants employed by the provincial government in terms of the kind of framework or considerations that should be used in developing the power purchase agreement?

MS. MACFARLANE: Yes, there was, in the sense that as my evidence indicates, it was the working committee made up of members of the provincial government with their financial advisors and their energy experts that formed the framework for the power purchase agreement with nuclear.

Q.255 - But was there an actual document provided to Disco or any other part of NB Power outlining the considerations government wanted you to bear in mind?

MS. MACFARLANE: If such a document was produced it was made available to the working committee and the financial advisors, not to Disco or to NB Power.

Q.256 - Thank you. With respect to this power purchase agreement, I have been through it and I couldn't sort this one out. Can you cut back your purchases if you need to under this particular power purchase agreement?

MS. MACFARLANE: No. Disco cannot reduce its purchases under this agreement.

Q.257 - On page 1, recital C -- recital C says, "Point Lepreau is considered a heritage asset and therefore the output from the unit generated will be used in accordance with the terms of this agreement to serve the load requirements in New Brunswick." And I have two questions about that. One is how in fact is a heritage asset defined? Maybe this has been before but I have missed it.

MS. MACFARLANE: Subject to check, I believe the heritage asset concept derived from the Market Design Committee and they were deemed to be assets that basically the customers of New Brunswick had the rights to and they also had the obligation for paying for those assets.

Specific to Point Lepreau and as I understand it this was after considerable debate in the Market Design Committee, the existing asset as well as the planned refurbishment were included in the definition of heritage assets.

Q.258 - Thank you. And with respect to that same recital where it says it will be used in accordance with the terms of the agreement to serve the load requirements of New Brunswick, does that include exports to anywhere else?

MS. MACFARLANE: The terms of the agreement indicate that there is one export take-off of Lepreau and that's with

Maritime Electric Limited, for five percent of the production.

But except for that, Lepreau is an in-province generator and is considered part of the must-run category in the PROMOD -- the production modelling run done by Disco.

Q.259 - Thank you. Is there any, to your knowledge, involvement by Maritime Electric through a contract in terms of taking a risk on the refurb?

MS. MACFARLANE: Yes, there is. We have a long-standing agreement with Maritime Electric where they pay their portion of all costs whether they are capital related or whether they are OM&A related, and in exchange for that they take a portion of the energy produced from the plant.

Q.260 - In the event that for some reason you couldn't take all of the output aside from what goes to Maritime Electric at Disco, who has the right to export any surplus or find market for the extra? Is that Disco or Nuclearco?

MR. KENNEDY: If there was a surplus to the -- it would be Nuclearco.

Q.261 - Nuclearco would then have the right to deal with the surplus, anything that is essentially freed up?

MR. KENNEDY: Yes.

Q.262 - Okay. And on that is there any kind of profit sharing agreement between Disco and Nuclearco in that kind of

scenario, if there were some surplus and Nuclearco found other markets for it?
MR. KENNEDY: No. Anything above the demonstrated net capability factor at the time of the establishment of the contract would be -- after the refurbishment if there is more than the 635 net then that would be to Nuclearco's account.
Q.263 - Thank you.
MS. MACFARLANE: Mr. Coon, I might just add that would be a very unusual circumstance. The base load even in the summer months seldom gets below 1,800 megawatts, and Lepreau being a must-run is part of the first -- it is after hydro the first load. And that's only 635 megawatts. So it would be a very unusual circumstance that it would be available for export.
Q.264 - Thank you for that. I thought I would ask just to explore that point though. Now who can actually terminate this agreement between Disco and Nuclearco?
MS. MACFARLANE: The PPA can be altered by Electric Finance Corporation if it chooses to do so. Disco cannot terminate the agreement and Nuclearco cannot terminate the agreement.
Q.265 - So if ten years out you found a better deal for that amount of power from some other source in the market you

couldn't get out of the PPA?

MS. MACFARLANE: That's correct.

Q.266 - Okay. A couple of questions around the issue of adjustments for environmental and regulatory costs that are provided for in the PPA. Now as I understand it, and tell me if this is the case, the way it's written currently, the nuclear company pays 50 percent of any cost overruns that might reoccur as a result of additional or unexpected regulatory costs, and Disco pays the other 50 percent.

So if the regulator says, you know, you have got to do something that was unanticipated in the context of the refurbishment, then those regulatory costs -- overruns let's call them -- would be split, or does Disco pay them all?

MR. KENNEDY: With respect to the refurbishment, the refurbishment cost has been fixed. This is with respect to future requirements that may come along with respect to environmental requirements or with respect to changes in the law after the refurbishment. It has nothing to do with the refurbishment. And there are various thresholds that are established, one being $5,000,000 with respect to any capital changes. And if there is any O&M changes on a go forward basis it has a threshold of $500,000.

So if there is something that needs to be done with respect to meet environmental requirements or nuclear law, there is a capital threshold of $5,000,000, and it has to exceed that before they come to Disco with respect to a request as a cost. And then that cost is fixed, an estimate with respect to what is required, and that is a fixed price and if that varies on a capital project, for example, then if it goes over by that agreed amount initially up front, then the Disco and the Nuclearco share the additional costs on a 50/50 basis above that. So that has nothing to do with the refurbishment price that has been fixed in the contract. That will be used to establish another tier 1 in the pricing mechanism after the refurbishment.

Q.267 - Okay. So for example, during the hearings before this Board concerning the proposed refurbishment of Point Lepreau, there were a series of regulatory risks that NB Power have identified that could change the cost of refurbishment. Things like, you know, if the regulator decided as part of the refurbishment the steam lines over the control room had to be re-routed or what have you, that would increase the cost of refurbishment. So who pays if that happens?

MR. KENNEDY: After the refurbishment and if it has been identified that the costs are -- or the estimate is paid, Disco does.

Q.268 - So Disco pays 100 percent of any additional costs in the refurbishment as a result of requirements imposed by the regulator?

MR. KENNEDY: That is if at the refurbishment it includes a certain amount of work, identified work, and that the prescribed amount that is in the agreed upon estimate -- firm estimate that has been fixed, and that will constitute how the tier 1 prices and tier 2 prices are established after the refurbishment, once the refurbishment is completed.

But if there is further work with respect to items and with respect to environment or with respect to nuclear law, then the capital structure or the $5,000,000 has been exceeded. Then the price is established and fixed and Disco was responsible to spread that over the remaining life of the agreement. And there is a threshold of 500,000 with respect to O&M items that may be imposed on Nuclearco.

Q.269 - Thank you. And if it is capital cost overruns, as I understand it, those overruns are split 50/50 between Disco and Nuclearco?

MR. KENNEDY: No.

Q.270 - No?

MR. KENNEDY: Not capital cost overruns with respect to the Point Lepreau refurbishment.

Q.271 - And those are paid for by whom?

MR. KENNEDY: The capital cost has been established. And that is reflected after the post refurbishment with respect to the price that is charged on the tier 1, tier 2 and tier 3 prices on a go-forward basis. And Nuclearco takes the risk from now on with respect to the refurbishment once the price has been set. And the price has been set. And Disco has been notified of that price. And that has been established. The risk now of the refurbishment cost is with respect to -- it goes to Nuclearco.

Q.272 - Thank you. What happens after Lepreau, refurbished Lepreau has been in operation and the regulator derates it so that it only operates at some lower percentage? Does Disco end up paying for just the energy they take from the plant though it is working at less than the capacity that you were promised?

MR. KENNEDY: Disco only pays for the energy that it receives from the plant.

Q.273 - If an accident occurs or the regulator requires the plant to be shut down for safety reasons after it is refurbished, does the contract remain valid?

MR. KENNEDY: Yes, with respect to certain items.

Q.274 - Can you identify those items for me please?

MR. KENNEDY: Would be with respect to insurance, with respect to replacement costs, with respect to the nuclear unit to restore the unit, an example of one.

Q.275 - And are those items laid out in the power purchase agreement somewhere?

MR. KENNEDY: Yes, subject to check. I can get back to you with respect to that.

Q.276 - Okay. You could get back and just indicate where they are?

In the event of an accident who has the responsibility to provide the replacement power for Disco?

MR. KENNEDY: Disco has at its disposal all of Genco's assets with respect to providing the necessary energy to serve the in-province load. It will call back those assets to provide, to the extent that it can, with respect to supplying in-province load should Point Lepreau become unavailable.

And again it has the opportunity to go out to the market if there is additional capacity or energy is required.

But there is a significant amount of energy that is available from Disco's other heritage assets that it has under contract.

Q.277 - But what you are telling me is that in that situation Disco would carry the responsibility for purchasing the replacement power?

MR. KENNEDY: Through the vesting PPA Genco has the responsibility to backstop the loss of supply from Point Lepreau. And we basically compensate them for that. But it is their responsibility to do that.

We have priority on their assets. And if there isn't sufficient then we have the obligation to go out and purchase the capacity energy if it's not sufficient to serve the in-province load.

Q.278 - Thank you. Now with respect to questions of decommissioning and nuclear waste, if there is a change in the expected commercial life of the reactor, who then pays the unfunded, or underfunded, I should say, nuclear waste and decommissioning costs?

MS. MACFARLANE: Subject to check, while the plant is operating, Disco pays it. And when the plant ceases operation permanently, if there is any unfunded amount, or if as an example the cost estimate changes after the plant has finished operating, the Nuclearco company pays for it.

Q.279 - And Nuclearco would be on the hook then. So in the event say it had to shut down five years earlier than

planned, Nuclearco would be on the hook for those underfunded costs, not Disco?
MS. MACFARLANE: That's correct.
Q.280 - Thank you. If just say a refurbished Lepreau lost 450,000,000, like it did the first time around, who takes that on their books, Disco or Nuclearco?
MS. MACFARLANE: Nuclearco would retain any operating losses on its operation.
Q.281 - Has -- you are required to be provided with the as-built cost estimate by Nuclearco for the refurbishment, at least the as-built cost estimate which formed the basis of the decision to go with the refurbishment, correct?
MS. MACFARLANE: Nuclearco is required to provide that to Disco, yes.
Q.282 - Right. And has that been filed here before the Board?
MS. MACFARLANE: I don't -- I don't know if it has been filed. It wouldn't be relevant to this hearing. Because the relevance of that cost is for changing the price post refurbishment. It is a matter of public record though.
MR. MORRISON: I believe, Mr. Chairman, we filed the amount at some point in response to an IR.
Q.283 - If you could later come back just with an IR reference that would be much appreciated.
Has that as-built cost estimate been updated since it

was first provided to you?

MS. MACFARLANE: Are you referring to the amount determined when the project was approved? Or are you talking about --

Q.284 - Right.

MS. MACFARLANE: -- the amount that -- no. The project was approved in July of 2005 by the provincial government. And the as-built estimate has not changed since that time.

Q.285 - Did Disco use any outside consultants to look at what -- well, to look at that number, the as-built cost estimate?

MR. MAROIS: Disco did not.

Q.286 - Sorry?

MR. MAROIS: Disco did not.

Q.287 - Disco did not? Thank you.

And did that as-built cost number include replacement energy, replacement power?

MS. MACFARLANE: No, it did not.

Q.288 - Is Disco planning for any increase in that as-built cost estimate?

MS. MACFARLANE: Disco doesn't have to plan for an increase in the as-built cost estimate. Because any overage would fall to the Nuclear company.

Q.289 - This may be somewhere. I guess I haven't found it.

What is the overall estimate for purchase power costs that Disco will have to expend during the refurbishment?
MR. KENNEDY: It has not been determined yet.
Q.290 - It has not been determined yet? When will it be determined?
MR. KENNEDY: Over the next I would say year or so. We are basically exploring our options with respect to how we come about replacing that power during that time frame.
\Q.291 - Is there a return or profit figured into this PPA for the Nuclear company?
MS. MACFARLANE: Yes, there is. The PPA was structured so that over the life of the agreement, post refurbishment, so that's the -- from the time the contract was signed in October 2004 to the refurbishment, and then 25 years subsequent to that, over that time period on average the PPA would earn a 17 percent return on equity.
And the equity would represent 50 percent of the capital investment post -- leading up to and post refurbishment.
Q.292 - Thank you. How would you describe the risk-sharing arrangement between Disco and Nuclearco? 50/50, 75 on their part, 25 on yours?
MS. MACFARLANE: The evidence -- my evidence Part 1 describes the arrangement as one where the risk of

operating the nuclear plant is left with the management of Nuclear.

The risk related to things that are beyond management's control, such as changes in environmental law, changes in nuclear law or industry-wide changes in nuclear regulation, those are beyond Nuclearco's control. And those flow through to Disco.

As it goes to the refurbishment, again the -- once a budget is and has been established, that cost flows through to Disco. But any risk of construction overrun stays with Nuclearco.

And based on our experience, in looking for a third party investor in the nuclear operation, I would say that's a very commercial-like transaction. Because it was very similar to the transaction that we were exploring with Bruce Power.

Q.293 - There are two figures in the PPA in terms of the price per megawatt hour that Disco would pay for power from Nuclearco. One is $53.83 per megawatt hour, which is early on in the PPA, and the other is $67.60 per megawatt hour. Can you explain the difference on -- the difference between how these two are developed?

MS. MACFARLANE: In broad terms the $67 price is the post-refurbishment price. So it is representative of

collecting the capital costs invested on nuclear refurbishment.
Q.294 - And the other price?
MS. MACFARLANE: The other price is representative of the capital cost of the existing plant. And of course any investment between now and the completion of refurbishment in capital is collected in work in progress, and there is no collection of that capital or of the cost of obtaining that capital until such time as the plant begins to come back on line after refurbishment.
Q.295 - So costs associated with refurbishment or preparing for refurbishment are not part of the current price or do not affect the current price pre-refurbishment that you are paying to Nuclearco?
MS. MACFARLANE: No, they do not.
Q.296 - I just have one last question, I guess. If the owners of Maine Yankee, if they still exist, called you up and offered you the same deal that you have with Nuclearco, would you take it?
MS. MACFARLANE: Under the contract Disco would not have the right to do that. I would suggest that if the working committee and the financial advisors had contemplated such a situation, they also would have had to complement and build into the contract provision for recovery of the

stranded costs. And that provision is not there, which is why Disco cannot leave this contract.

Q.297 - But hypothetically if the contract -- this one hadn't been on the table but a similar one was offered by Maine Yankee, would you have taken it?

MS. MACFARLANE: Hypothetically if this wasn't on the table, I believe Disco would be required under the Act to conduct a request for proposal. And if Maine Yankee was the most successful bidder, then, yes, it would entertain it.

MR. COON: Thank you very much. Mr. Chairman, those are all the questions I have.

CHAIRMAN: Thank you, Mr. Coon. Commissioner Sollows has an inside track around here, and it says, reminder of ten a.m. fire alarm. Do we have to leave, sir? So I will not be calling our mid morning break this morning, the fire alarm will. Okay. Any questions from Enbridge Gas New Brunswick? They are not here, so they have no questions. The Irving group of companies?

MR. BOOKER: No, Mr. Chair. We were included with the CME.

CHAIRMAN: Thank you, Mr. Booker. Mr. Gillis is not here. Rogers is not here, the self-represented individuals. Mr. Gorman?

MR. GORMAN: Thank you, Mr. Chairman.

CHAIRMAN: We will take a break now.

(Recess)

CHAIRMAN: All right. Mr. Gorman.

MR. MORRISON: Perhaps, Mr. Chairman, just before we move on, sorry -- Mr. Coon had questioned about the costs and what IR that was for the refurbishment. And it's Disco PI IR-34 from November 14th. And I have provided Mr. Coon with a copy.

CHAIRMAN: Good. Thank you, sir. Mr. Gorman.

MR. GORMAN: Thank you, Mr. Chairman.

<u>CROSS EXAMINATION BY MR. GORMAN</u>:

Q.298 - Good morning, Mr. Marois, Mr. Kennedy, Mr. Peaco and Ms. MacFarlane. I would like to start by going to exhibit A-55, Appendix 6. Does everybody have that? This is a vesting operating committee minutes from September 22nd 2005, and it's a redacted version. And I notice that there are several attendees for Genco and several for Disco and the names are blanked out. Is there a reason for that?

MR. MAROIS: The only reason they were blanked out was to respect personal information.

Q.299 - And what personal information would that be? I guess I'm interested in who would be making these decisions on behalf of Disco?

MR. MAROIS: I can't recall the number but in a separate information request we provided the titles of the people that sat on the operating committee and a description of their role. It's not as much the name of the people, it's their function within each company.

Q.300 - Well I understand that for example that Ms. MacFarlane has a title if you will with Disco and a title with most of the other companies. So I'm not sure if that assists or not in the sense that I guess I am wondering who is making these decisions? Would it be possible for you to provide an undertaking to give us the names and titles of the members who sat in on that committee meeting?

MR. MORRISON: Mr. Chairman, I believe the decision to not identify people personally by name was as a result of the POPIA legislation. Now granted I didn't give an opinion with respect to that legislation but I believe that there is in-house legal opinions on that. I don't know whether it relates specifically to this document but a general POPIA policy. I believe we have provided the titles and if we haven't, we can certainly undertake to provide the titles of the people that were involved in the operating committee.

CHAIRMAN: You know, I don't know. I haven't looked at that legislation in the context of here, but to me it seems like a pretty wild stretch that somebody who has a

position with a company that if the minutes of a meeting of the company are put on the public record in this hearing that the attendees couldn't be made known as well.
MR. MORRISON: Quite frankly, Mr. Chairman, I don't know the answer to that, but we will look into it at the break.
CHAIRMAN: All right. If there is an in-house opinion then please give consideration to filing it with the Board.
Mr. Gorman?
Q.301 - Thank you. Just continuing on with Appendix 6 in A-55, I note that -- and of course we don't have the names but there are four members listed and then there are four guests. Can you tell me what the difference is between a member and a guest at this operating committee meeting?
MR. KENNEDY: Yes. Guests are invited to explain certain issues that we are dealing with. They could be from the various operating arms of the companies, whether it be Disco, Genco or Nuclearco, to deal with specific issues.
Q.302 - So would these guests necessarily be from Disco or Genco or could they be somebody who is not an employee but who is there for information purposes, for example?
MR. KENNEDY: Yes, I suppose they could be a third party with respect to analyzing things, but that is not the case in these minutes.
Q.303 - Now that particular meeting, if I go to page 2 of the

minutes, it says, minutes approved, date, and initialled by Genco and Disco member, and that's blank. It hasn't been blanked out but that's actually blank. Is there a signed approved copy of those minutes?

MR. KENNEDY: Yes, there is.

Q.304 - And does it vary at all from -- I assume this is a draft since it's unsigned. Does the signed copy vary at all from the draft?

MR. KENNEDY: To the best of my knowledge, there has been no change, but it's subject to final review and then each member of the operating committee signs off with respect to a complete -- to signify that the minutes are complete and it was recorded as per the session.

Q.305 - Would you undertake just to check the signed copy to determine whether or not there are any changes? And really all I am concerned about is item number 4, 2006/2007 budget modelling assumptions?

MR. KENNEDY: Yes, I will. I will check.

Q.306 - Now with respect to item 4, 2006/07 budget modelling assumptions, I note that the minutes say, Disco members approved the vesting energy price for the 2006/2007 budget year and the modelling assumptions as presented by Genco in the PROMOD input data binder. This committee, does it vote on matters such as this? Is it a consensus

committee? Just exactly how does it work?
MR. KENNEDY: It's consensus with respect to the operating committee.
Q.307 - Now I note that the assumptions are approved by Disco. I assume the reason it's not approved by Genco is that it's their numbers that are being presented. Would that be a fair assumption?
MR. KENNEDY: Yes.
Q.308 - The last sentence in paragraph 4 talks about the contribution to fixed cost, assumes a CPI adjustment of 2 percent, will be subject to an adjustment after January 1st 2006, when the relevant 2005 CPI index is published. Has that been done?
MR. KENNEDY: Yes, it has.
Q.309 - Do we have that information? I don't recall seeing it.
MR. KENNEDY: I don't believe that information has been provided to this hearing, but it can be.
Q.310 - Would you undertake to do so?
MR. KENNEDY: Yes, I will.
Q.311 - Now I just have a couple of questions now arising out of Mr. Coon's questions. And, Ms. MacFarlane, you testified in response to his question that you can't -- Disco can't terminate the PPAs?

MS. MACFARLANE: Yes.

Q.312 - And how long do the PPAs last?

MS. MACFARLANE: Subject to check, it is I believe for the life of the plant, but the life of the plant is 25 years.

Q.313 - And my understanding would be unless -- and if the plant were refurbished and continued on, then it would go beyond the 25 years. Is that a fair assessment?

MS. MACFARLANE: Are you speaking specifically, Mr. Gorman, of the nuclear PPA?

Q.314 - Well I'm speaking in general, but I understand Mr. Coon's questions were specifically to nuclear. So is that a 25 year agreement? Is it specifically 25 or could it be longer?

MS. MACFARLANE: The base term is 25 years following refurbishment, and Disco can further extend one year at a time on five years notice.

Q.315 - Okay. So Disco can't terminate the PPAs or its contract for supply of power. What about its contracts going the other way, that is to supply power say to wholesale or industrial customers? Can Disco unilaterally terminate any of those contracts?

MR. KENNEDY: The contracts with respect to the wholesale customers, that was your question?

Q.316 - Wholesale and/or industrial?

MR. KENNEDY: Yes. The contracts can be terminated provided that the necessary notice is provided by either party with respect to it. And after March 31st 2006, most of the contracts with the exception of a few can be terminated with respect to 12 months notice on either party's action.

Q.317 - Essentially that was my question. It goes either way then. Disco could terminate the wholesale or industrial contracts if they saw fit?

MR. KENNEDY: Yes. Of course we still have the obligation to serve all the customers that don't wish to go to the market as a standard service supplier.

Q.318 - So would that be a restriction on your right to terminate?

MR. KENNEDY: If we could terminate the contract, but if you -- if the entity -- the wholesale entity or the industrial still wanted the supply, we would have to -- we have the obligation to serve them.

Q.319 - Thank you. The second question arising out of Mr. Coon's questions that I want to follow up on is the return on equity with respect to Nuclear. Did I understand, Ms. MacFarlane, your evidence to be that based on 50 percent equity, there is a 17 percent return on equity?

MS. MACFARLANE: That's correct. On average over the life of the contract.

Q.320 - Now I understand that the process to develop the PPAs was not necessarily one of negotiation, would I be correct?

MS. MACFARLANE: That's correct.

Q.321 - And you would agree that the percent of equity and return equity is considerably higher than even Disco is seeking at these hearings?

MS. MACFARLANE: I would agree with that, but you will recall in my discussions with Mr. Coon I mentioned that we had looked for a third party investor last year starting in the fall of '04 and extending through to March of '05, that we were negotiating with Bruce Power, and we were unable to complete a successful contract. Largely because although the structure of the contract was very -- the PPA here was very similar to what Bruce was interested in, i.e., it was commercial in its nature, the return and the capital structure that they were proposing was very different. And the financial advisors that were assisting us at the time, who were different than the financial advisors who assisted the province with the structure of the PPA, told us that there is no nuclear plant -- standalone nuclear plant in the world that could finance with 50 percent equity.

In fact they were suggesting that the only viable

capital structure for Nuclearco if it were to look for a commercial partner would be 100 percent equity.
Q.322 - You would agree that the return on equity with respect to Nuclearco and the 50 percent return though were not negotiated. They were simply agreed to in the PPAs?
MS. MACFARLANE: They were provided by the financial advisors to the working committee for the Province of New Brunswick.
MR. MAROIS: You just mentioned 50 percent -- returning to your question. You mean 50 percent capital structure?
Q.323 - That's right. I would like now to go to exhibit A-96, if I could please. I have a few questions on this exhibit which was I guess entered into evidence at our last hearing date. But the title of this document is Power Purchase Cost Variance Only 2006/07 Over 2005/06.
And perhaps, Mr. Kennedy, you can verify for me. I understand that the document is intended to link your evidence to the La Capra Reports with respect to the assessment by La Capra on PROMOD, is that correct?
MR. KENNEDY: Yes. That's correct.
Q.324 - And before I go any further, I wonder if somebody on the panel could give me a layman's view of what PROMOD is. I have looked at this for months. And I know that it is a computer modeling system.

But could somebody give a simple explanation of just precisely what that system is?

MR. PEACO: I guess I have been nominated. I'm not sure if I can --

Q.325 - I can see you are elected.

MR. PEACO: PROMOD, first the name itself is a commercial software name. It is the type of a model which is a generating system simulation software package.

And what it and models like it are used in the utility industry is to do forecasting of how a system is dispatched over time, taking as inputs variable costs such as fuel, the characteristics of different units such as their heat rates, their capacity, their forced outage, maintenance schedules and so forth and typically hourly load or some period, you know, periods of load.

And it's basically going through the process of stepping through time and determining each hour, each time period, which units would be dispatched and what amounts and what costs would be incurred to serve that load.

Q.326 - Would PROMOD be used generally to ensure economic dispatch?

MR. PEACO: When you say ensure, I'm not sure if I know what you mean by that. PROMOD is designed to simulate economic dispatch. Ensuring economic dispatch in an operating sense would be done in some different way.

If you are asking the question does this inform system dispatchers as to how to run their system, probably not. This is, as it has been used in NB Power in particular, it is more of a planning tool than an operations tool.

Q.327 - Thank you. Now on A-96, I think perhaps, Mr. Kennedy, if I can refer you to the first four lines. I understand they represent the results essentially of the three La Capra reports, is that correct?

MR. KENNEDY: Yes. Line 1 is taken directly from table 1 of the La Capra reports with respect to the fuel costs that they performed the audit on and justified the variances.

Q.328 - Now, Mr. Kennedy, you testified on Thursday that line 4 is a bundled account to protect certain information. What is the nature of the protected information?

MR. KENNEDY: With respect to line 4 there is a capital and an O&M component that is reflected in the Genco heritage PPAs. That is a component that is a legitimate fuel cost to Disco.

But with respect to performing, when Dan Peaco did his audit, this component combined with other components, this component was not factored into his difference. Because what he was looking at was with respect to fuel cost.

So this component, as an actual cost to Disco, reflects the capital cost as I had mentioned with respect to the PPAs, as well as netted out of it is the CTs and emergency purchases that are in the PROMOD.

Because as per the contract, the Genco PPA, those CT and emergency purchases are the responsibility of Disco. So that was combined with these fixed costs that are in -- that are expressed as an energy charge, where in the PROMOD it had to be added back in to come to the total that basically shows up in my table 1(b), row 2, columns 3 and 4.

And again line 2 is another outline where we look at Disco's NUGs, the PPAs that we have with respect to wind and other power purchase agreements. They were -- when Mr. Peaco was doing his analysis they were items that were identified in the PROMOD run. So that basically those are contracts that are directly with Disco. They were to be backed out. And they were backed out. And they show back up in line 18.

And again the other costs that had to be added was the contribution to the fixed costs with respect to the vesting energy price, in other words, the $7.14 per megawatt-hour and $7.24 per megawatt-hour had to be added back into the -- added onto the component that is in line 1 to come to the energy charge with respect to Disco's

obligation for the various years, the test year being 06/07.
And that 06/07 was compared to 05/06.

Q.329 - Mr. Kennedy, I'm not sure I understood your answer.
The question that I had -- and I'm not sure if you answered it or not, but if you did I didn't understand it -- was that in your testimony you said this was bundled to protect certain information.
And I'm not sure that I got from your answer the sense of what was protected or what was the need to protect certain information.

MR. KENNEDY: What was being protected was the specific cost with respect to the third party NUGs, the third party NUGs being Genco's PPAs under the heritage assets.
These components were bundled together, and also netted -- the various other things were netted off of it.

Q.330 - And would that be the only thing you were referring to then, is just the specific costs on the third party NUGs?
That is what needed to be protected?

MR. KENNEDY: Yes.

Q.331 - My second question arising out of line 4 is -- it talks about capital, O&M, natural gas, PPAs and other.
And I'm not sure if you answered maybe in your earlier answer what was included in other. If not, would you please do that?

MR. KENNEDY: In other is CTs operation and emergency purchases and diesel fuel that is supplied. That was indicated and with respect to the Point Lepreau standby generator.

Because those costs belonged to Nuclearco and not Disco. And those costs were netted off of this and backed out to reflect the costs, what we are basically obligated to pay for.

Those are very small costs. But when the PROMOD is run, the fuel costs -- all fuel costs are taken into account.

Q.332 - So would the amount included in other such as emergency purchases be spread evenly to all of the rate classes?

MR. KENNEDY: CTs and emergency purchases show up again down in line 12.

Q.333 - Yes.

MR. KENNEDY: That is a direct cost that Disco is responsible for as per the Genco PPA.

Q.334 - So in terms of paying for it then, how is it distributed amongst the classes?

MR. MAROIS: I think maybe you should keep that question for the upcoming panel with Mr. Larlee. We are not -- we don't know the answer.

Q.335 - Okay. Thank you. Still on A-96, there are a series of notes on the bottom of the page and then there is a column which indicates which note applies. Now for example, if I go to line 1 and it has note A and line 1 deals with 2006/2007 -- sorry, column 1 -- and then column 2 deals with 2005/2006. Does the note apply to both columns?

MR. KENNEDY: Yes.

Q.336 - Still on A-96, I am going to go to line 8, export benefits. And, Mr. Kennedy, in your testimony on Thursday you said that export benefits are "hard wired" into the contracts. What did you mean by that expression?

MR. KENNEDY: Yes. If you go -- when you go to the contract, the Genco PPA, if you refer to schedule 6.3 --

Q.337 - Yes.

MR. KENNEDY: -- it identifies the prescribed export benefit, that is, to be provided to Disco in that year.

Q.338 - Okay. I am going to move on to another topic. Ms. MacFarlane, in your direct evidence you stated that Disco does not need to provide evidence that the prices in the Genco PPA are cost based. Is it fair to say that your position is that the costs are as dictated by the Genco PPA regardless of cost?

MS. MACFARLANE: Some elements of the Genco PPA are tied to costs, as an example the energy charge, and that's adjusted every year. Other elements are stated in the contract, for example the capacity charge and the contribution to fixed costs and the vesting energy price. Those are prestated in the contract. Export benefits and hydro flows, though they are prestated in the contract there is an adjustment in the contract for in-year variances between actual costs or benefits incurred by Genco and the amount passed on to Disco in the initial setting of the Genco -- pardon me -- in the initial setting of the vesting energy price and the amounts passed on from Genco to Disco as of October 1st.

Q.339 - So just to make sure that I understand then, for certain elements in the PPAs, they apply regardless of cost, would you agree?

MS. MACFARLANE: That's true. The broad construct of the PPA was based on an estimate -- a forecast of what Genco's costs would be over the long-term, including costs of capital, and again the broad constructs was to reimburse Genco for its costs over that period of time. But there is commercial risk sharing built into the contract so that if Genco's costs are in some instances better than anticipated in that forecast by virtue of Genco's management, Genco benefits from that.

In other cases if the performance by Genco is worse than what was anticipated in that long-term forecast, then Genco obviously suffers that through a lower return on equity.

Q.340 - And I understand that and I guess the intention of my question was simply to establish that cost is not the basis on which you determine what will be paid, it is the PPA. And if you could show that there was a lower cost I think your evidence is that doesn't matter?

MS. MACFARLANE: It depends on the term of the PPA. That's what dictates what the cost will be. In the case of fuel costs, obviously that is determined based on what the current forwards are and that is passed through based on the hedged prices in the contract. So there cost does matter, cost to Disco does matter. In areas such as OM&A the capital costs, et cetera, incurred by Genco, if they are not able to perform at the levels that they recover under the PPA, then Genco takes a hit. Their costs don't matter.

MR. MAROIS: Maybe another example of where cost matters is the example I gave last week of the fuel blending at Belledune. That resulted in reduced fuel costs which were passed through to Disco.

Q.341 - Thank you, Mr. Marois. I guess that does lead into a

question for you. The PPAs -- still staying on the subject of the PPAs. It's my understanding that they were not negotiated but they were set by a working group as a result of restructuring, is that correct?
MR. MAROIS: That's correct.
Q.342 - And after restructuring -- from sitting through -- I don't know what day we are here now, but day 40-something of hearings, it seems to me that the Applicant is claiming that the business units have become separate independent stand-alone companies, is that correct?
MR. MAROIS: You said numerous things there. You said it fast.
Q.343 - Well after restructuring, is not the position taken by the Applicant that the various business units of the former NB Power have now become separate independent companies -- stand-alone rather than independent?
MR. MAROIS: Yes.
Q.344 - Independent may not be the right word.
MR. MAROIS: Definitely that's the case, yes.
Q.345 - So who protected the interests of Disco's customers during the setting of the contracts?
MS. MACFARLANE: I believe we answered an IR on that. The contracts -- the contract structure was defined by the working committee and there were NB Power people,

specifically at the time, the director of corporate planning and regulatory affairs and his -- pardon me -- the vice president and his director -- were working with the working committee. They represented NB Power's interests which at the time would have included Disco's interest. But in broad measure the construct of the PPAs was defined by the working committee and by their financial and industry advisors with the intent they be like commercial contracts.

Q.346 - Well then let me put to you that the setting of the contract, at least in my view, is different from the negotiation of the contract, would you agree?

MS. MACFARLANE: Yes, I would.

Q.347 - And would you agree that what occurred in this case was the setting of a contract, not the negotiation?

MS. MACFARLANE: I would agree with that.

Q.348 - Do you agree if there had been a negotiation that the customers of Disco may have been better served?

MS. MACFARLANE: I'm not able to answer that. It was a very complex process and the interests of the ratepayers of Disco, the interest of the shareholder, the interest of the taxpayers of the Province of New Brunswick, were all taken into consideration in the restructuring and in the design of those contracts.

Q.349 - Mr. Peaco, you testified last Thursday that the word reasonable is used in your presentation, that would be A-95, and in your reports, does not reflect that the price of power that Genco is supplying to Disco is reasonable, is that correct?

MR. PEACO: I believe the discussion was question was as to whether the reasonableness was relative to the terms of the PPA or relative to the market.

Q.350 - Yes.

MR. PEACO: And my answer was relative to the terms of the PPA.

Q.351 - And not to the market?

MR. PEACO: That's correct. Well I didn't do that analysis.

Q.352 - You then stated that the reasonableness criteria that you were applying were the calculations and assumptions used in a reasonable range relative to the interpretation of the PPA.

MR. PEACO: That's correct.

Q.353 - What do you mean by reasonable range?

MR. PEACO: Reasonable range meaning that the given parameters were consistent with operating history and industry practice, but there are any set of numbers. For example, you take the operating heat rate of a given unit and you look at the operating history over the last period of time, four or five years, they may be a range of values and you may be picking one number, or you may be picking one number from a set of information pertaining to hydro production.

Picking a number from that range of values reflecting -- reasonably reflecting that distribution is the kind of thing we are looking for, as opposed to setting a specific number within that range. We are just testing to see that those numbers fell within those kinds of parameters.

Q.354 - When I hear I guess the word range it implies to me that the results can vary up or down within a range, that in fact there is no absolute number. It can be a little bit more or, more importantly, it could be a little bit less?

MR. PEACO: That's correct.

Q.355 - Somewhat like the clinical surveys we hear that are correct 19 times out of 20 within so many points, and using that perhaps almost as an example, can you tell me what that range might be in fact in doing this analysis if there is a reasonable range? You know, could the values actually be lower and how much lower?

MR. PEACO: I did not conduct that type of an analysis. We just looked at the inputs as used and tested them against

the information provided to determine that they were reasonable. We did not test the implications of alternative numbers and the impact on the potential alternative budgets.
Q.356 - Well maybe that leads into my next question. You were asked if you reviewed the inputs to ensure their correctness, and you answered their reasonableness. What was the distinction you were making?
MR. PEACO: I'm sorry. The question you are referring to again is what exactly?
Q.357 - You were asked on cross examination if you reviewed the inputs to ensure their correctness, and your response was their reasonableness.
MR. PEACO: Yes.
Q.358 - You were distinguishing correctness and reasonableness. I am just wondering what was the distinction you were making in your evidence?
MR. PEACO: We did not -- in the case we would look at the inputs for various types of parameters that go into the model, tested them against a reasonable range. If there were say some very minor areas in the data calculation we wouldn't necessarily look for that. If it was within a reasonable range that we -- our review stopped at that point.

Q.359 - Mr. Peaco, I'm going to refer now to the various documents prepared by you, being exhibits A-5, A-9, A-49 and A-95, and those are the three technical audits in your Power Point presentation.
MR. DUMONT: Is that A-45 and A-49?
MR. GORMAN: I'm sorry. A-5, A-9 and A-45 -- sorry -- A-49.
Q.360 - Mr. Peaco, did the reports -- in conducting the investigations for these reports, did La Capra conduct an audit as stated in the title of each of these reports, or was it a reasonableness review?
MR. PEACO: The title is consistent with the terms of reference as a technical audit. The nature of the audit is, as I described in the presentation, in the -- the ultimate objective of each of these was to determine -- for us to reach or conduct a review of the analysis done by Disco and Genco, to determine whether the result in each of the three phases was a reasonable value.
In the first instance it was the 2005/6 budget total, 907, and in the phase II and phase III it was the variance analysis. So the ultimate objective was to conduct sufficient review to determine if those numbers were reasonable estimates.
Q.361 - Okay. And again I'm not sure that I got the answer to my question. I guess you say that it was an audit. I

think that was your response. My question was whether or not
it was a reasonableness review or an audit and I think
your answer was that it was an audit?
MR. PEACO: Yes.
Q.362 - Now if I get you to refer to page 5 on exhibit A-9. I
think I have got the right exhibit number.
MR. PEACO: That's the first audit?
Q.363 - No. That would be the second. That's the July 7th
2005, audit.
MR. PEACO: I'm sorry. On page 5?
Q.364 - Page 5, yes.
MR. PEACO: Okay. I have that.
Q.365 - I'm going to refer you to note 6. And the last
sentence in note 6 says, in other words, the assessment
was a reasonableness review and not a thorough audit.
MR. PEACO: Yes.
Q.366 - I guess I want you to reconcile that statement with
what you have just told me when I asked you if it was a
reasonableness review and you said no, it was an audit?
So the two statements seem to be at odds, so perhaps you
could explain?
MR. PEACO: We will go back to my prior answer. I indicated
that it was a technical audit of the materials used to
produce the numbers in question in each phase, and with

the ultimate objective of determining whether the object numbers were reasonable.

And to do that reasonableness test of the result we had to review Genco's and Disco's computations and so forth. This particular footnote is referring to the PROMOD component of that directly. We did not conduct a what I would call thorough audit of the model operation in the sense that we did not itemize the -- replicate the analysis of the model or go through the detail every input. We looked at the results sufficient to determine the reasonableness criteria.

Q.367 - So are you saying that a portion of this report, which is the second report, is not a thorough audit but part of it is?

MR. PEACO: It's not a thorough audit with respect to the technical components of the PROMOD data set, but it is an audit of the variance analysis that were conducted by Disco.

Q.368 - Well if I could refer you to an IR, this was in A-54, and I don't think it's necessary to turn it up for the panel, it's fairly short. It's A-54, Disco PI IR-84. You were asked to indicate if the work was an audit or a reasonableness approach, and your answer was the work conducted was a reasonableness review.

Perhaps you may want to turn that up because -- and then the second question was if the answer number to number 1 was that it was a reasonableness approach, please indicate how this differs from an audit approach. And there is a paragraph long answer which ends with the distinction being drawn is one of level of effort and detail.

MR. PEACO: Yes, I have that. And I think the second response to that is very similar to the answer I just provided you.

Q.369 - So then would you agree that this is a reasonableness review and not an audit? That seems to be what your answer has been on the IR and quite frankly in looking at the reports.

MR. PEACO: And I think as I said earlier this morning, the ultimate objective of each of these pieces was to conduct a reasonableness review of the object information. And to determine that we had to conduct a sufficient review of the calculations done to get to that conclusion.

Q.370 - If the distinction is one of level of effort and detail, would a thorough audit be more reliable than a reasonableness review?

MR. PEACO: Any time you do more review you become more comfortable with the results. I think in this case one of the points that we were indicating here is that to get to the conclusions we were asked to find, the type of audit of the PROMOD model was not necessary in this case.

Q.371 - You were asked on Thursday in cross examination -- sorry, I think this was in direct examination -- you were referred to Mr. Strunk's report and talked about him having some criticism of the La Capra review and Mr. Strunk had asserted that your review lacked detailed analysis.

And I took from your response that you agreed that in New York in some other instances that the -- there in fact would be more detailed analysis, is that correct?

MR. PEACO: I think I indicated that -- Mr. Strunk had indicated that -- citing an example from the New York system, that in some instances that a regulatory review of this type would include a detailed review of the PROMOD modelling, including a hands-on analysis by regulatory staff as well as the utilities.

And my comment was simply an indication that I think that that's an extreme example and not typical of how reviews are done, but there are reviews done at that level of detail, but it's not -- in my experience it's not typical of all states in the U.S. in terms of how these reviews are done on a regular basis. -

Q.372 - Okay. Would you agree though that a more detailed analysis again would make the results more reliable?
MR. PEACO: Of course.
Q.373 - If I could ask you now to go to exhibit A-5.
A. That is the phase I audit?
Q.374 - That is the first audit, yes.
A. I have that.
Q.375 - And I'm going to refer you into about the fourth paragraph, five lines down, it talks about a reasonable range of contract cost outcomes that can be expected. Again there would be highs and lows, would that be correct?
MR. PEACO: I'm sorry. I missed the page reference.
Q.376 - Sorry. Page 1. It is the Executive Summary at page 1.
MR. PEACO: All right. Can you point me again to where you are reading?
Q.377 - Sure. Fourth paragraph, fifth line down. It talks about a reasonable range of contract cost?
MR. PEACO: Yes.
Q.378 - And again because we are talking about range, would you agree that it could be something more or something less?
MR. PEACO: That's correct.

Q.379 - And I would refer you in that same paragraph to the last three lines where it begins "Lastly the documentation of certain assumptions was limited. La Capra Associates recommends implementation of improved documentation procedures for future annual computations of the vesting contract price."

What assumptions were limited?

MR. PEACO: This first review was conducted -- this is the first computation. This is a review of the first computation of the vesting price relative to the PPA where we came in, there were a number of assumptions that were -- had been prepared.

But there was not a data binder. I think you referred to a data binder earlier that was brought to the -- a lot of the data had not been assembled in that form when we had come in for the first review. And we were -- as we conducted our interviews with NB Power, as we asked for certain information, that was assembled.

So I think many of the pieces of that that were relied upon had not been assembled in a way that you would expect if you were, you know, preparing work papers for an auditor or an external technical review at that point in time.

Q.380 - That is not how I interpreted your comments. I guess

I'm surprised by your answer. Because perhaps that changes the course of my cross examination.

I took it to mean -- and maybe you can reflect on this for a moment -- but there was -- the documentation of certain assumptions was limited, not the form in which it was presented to you, but the existence of the documentation itself was limited.

That is how I took your sentence to mean. Now mind you, it is your report. And you know, it is up to you to explain it.

MR. PEACO: I think there were some of each. I think largely there was -- it was largely the latter category though, in that there was material that would have been relied upon that was somewhere in the organization but hadn't been assembled. And we had to go through that. In some cases there were assumptions that had been made that were basically determinations by the operating committee. And there were -- those were more limited.

Q.381 - Well, if I can refer you to page 2 of the same report. And it would be the first paragraph after the four numbered paragraphs under paragraph 2.1.

You indicate "The audit scope did not include an independent verification of the derivation of all of the specific input assumptions used in the analysis or the details of how all resources and costs are represented in the PROMOD simulation model."

I guess my question would be why not?

MR. PEACO: I guess going back to the discussion we had earlier about the ultimate objective that we were asked to conduct in this phase 1 work was to verify the reasonableness of the overall budget and provide documentation of that. It was not to conduct a detailed audit of all of the components regardless of their impact on the result.

MR. MAROIS: Mr. Gorman, maybe it's important just to put these reports in context. If you go to page 17, attachment 1, the terms of reference --

Q.382 - Yes. I have that.

MR. MAROIS: -- these terms of reference were provided to the PUB at the outset of this.

So we did this in the spring just to clarify the type of work we would be doing. And the PUB supported these terms of reference.

So this is the work that we asked La Capra to do. And this is what they have done.

Q.383 - Well, the schedule that you have just referred me to, under Introduction I notice that it says that Disco is seeking an independent third party audit.

So is this an audit or a reasonableness review? I think we are back to that question. It seems to me the terms of reference ask for an audit.

MR. PEACO: I think again if you look at -- there is no page numbers -- the second page of the terms of reference, at the top of the page it describes the purpose of the audit.

Q.384 - Yes.

MR. PEACO: Third party review of Disco's budget of fuel and purchase power costs including payments for capacity to verify the budgeted costs are consistent with the pricing terms in the PPA.

And again that's the criteria that was applied to the level to which the materials needed to be reviewed to make that determination.

So I think the question is a matter of what degree is necessary to answer the objective of the terms of reference.

Q.385 - I think we could turn to this attachment by Mr. Marois. And where we had been was dealing with on page 2. But I want everybody to kind of keep that attachment. Because I think it ties in.

"The audit scope did not include an independent verification of the derivation of all of the specific input assumptions used in the analysis."

And if I go under Terms of Reference and I take the third bullet, it says "Verify the input assumptions are consistent with the terms of the PPAs."
How do you reconcile those two?
MR. PEACO: Verifying that they are consistent with the PPAs refers to reading the terms of the PPAs, understanding what is being called for, and is there a consistency between the assumption used and the description of what was required, what is called for by the PPA.
Q.386 - So is your evidence that in fact you carried out that third term of reference, that you did verify the input assumptions are consistent with the terms of the PPAs?
MR. PEACO: Yes.
Q.387 - But you did not conduct any independent verification of the derivation of those inputs?
MR. PEACO: It wasn't an exhaustive review of all of the inputs. We reviewed the ones that had the most significance, again with the overall objective of getting to reasonableness of the budget, consistency with the PPAs, not simply for the purpose of checking every number regardless of its import to the outcome.
Q.388 - I guess from that paragraph on page 2 I don't take it that you did any independent verification of the derivation of these specific assumptions at all?

MR. PEACO: I'm sorry. As I read that sentence it says, the audit scope did not include independent verification of the derivation of all the specific input assumptions. We did do some and the most significant of those but not all. The overall point we are trying to get conveyed here is that this was not an exhaustive review of every data element in this model.

This is looking to understand the overall veracity of the approach and the result, and that the major drivers of the results were consistent with the PPAs and were a professional method of deriving the inputs.

This was simply to indicate that we didn't look at every individual number regardless of impact on the overall result.

Q.389 - If I can take you to page 10 of the first report under heading 4.3, PROMOD Input Review, and the last sentence. Are we talking about the same thing here, by the way? Is this the same topic? It talks about your scope of work did not include an independent verification. Is this just a restatement of what we have just been talking about?

MR. PEACO: It looks to be verbatim from page 2.

Q.390 - If I can take you to page 11 you deal with fuel prices, unit capacity, heat rates and unit availability. Firstly dealing with unit capacity, you say that "Unit

ratings as modeled in PROMOD are based on historical operating data which was not available to La Capra Associates for review." Why not?
MR. PEACO: I don't recall the specific reason for that at this point. It was --
Q.391 - Would that data make your review or your audit more reliable?
MR. PEACO: In this particular respect it would not add much to the value. Because the unit ratings are also specified in the agreement. And so there would be some added value. But many of the parameters were identified from other sources.
Q.392 - Fair enough. But the report does indicate that the ratings are modeled on historical operating data, you would agree?
MR. PEACO: Yes.
Q.393 - Going down to heat rates, again these were derived from historical operating data. And you comment again "This data was unavailable to La Capra Associates for review."
Would that have helped to have that information in preparing your report?
MR. PEACO: Yes.
Q.394 - Going down to the next heading, Unit Availability, you

are dealing with -- about halfway down you say "The only item of note relates to the Point Lepreau nuclear facility whose capacity factor, while not implausible, is somewhat high."

I just found that to be an interesting impression, "while not implausible." Did this not I guess meet the expectations that you would have had? Was there something about the nuclear facility that caused you to use that expression? And really what did you mean by it?

MR. PEACO: I think we were just noting that the 83 percent capacity factor used in that year was consistent with some of the higher end of the range of historical operation that the unit had observed.

So that it would be somewhat on the high side of the range of outcomes you would expect if they were operating normally.

Q.395 - If we can go to page 12, Hydro Production. Again you indicate you weren't able to review historical data to confirm the calculations, is that correct?

MR. PEACO: That's correct.

Q.396 - And under Load you say "The data and models used to prepare the forecast were unavailable to La Capra Associates for review." Is that correct?

MR. PEACO: That's correct.

Q.397 - And again with respect to hydro and load, if the historical data had been available again, that would have been helpful?

MR. PEACO: Yes.

MR. KENNEDY: If I might add, the load forecast is provided by Disco to Genco. And that load forecast has been filed with this Board. And that's what drives the requirements of the PROMOD run. So it's on record what our load forecast is.

And that is -- that is what is used to provide the driving factors on a month by month basis for the determination of the generation that's required to serve the in-province load as well as to provide an opportunity for exports.

Q.398 - If we can go to page 13, Reasonableness of Resultant Power Costs, the final paragraph indicates that the PPAs do not fully fix the cost of power for Disco.

And your final statement there is that La Capra did not analyze the issues dealing with hydro production, CT usage, et cetera, is that correct?

MR. PEACO: I think what you left out in the middle there, it was simply -- this is basically pointing to those things that are after the fact true-ups built into the PPA.

So we weren't asked to review any sort of true-up opportunity that might arise. This is the setting of the initial budget only.

Q.399 - So these are items that you weren't asked to review? Is that what you are saying?

MR. PEACO: That's right. But the indication would be that clearly there would be -- these items that are identified in this paragraph are ones that are subject to true-up after the fact.

Q.400 - Could I take you to page 14 of your report please. That is under heading number 5, Findings of Note. And 5.1 deals with vesting PPA contribution to fixed cost. There seems to be some difference between. And in Section 6.2.6 of the contract it seems to indicate the price of $7 per fiscal year adjusted for inflation. But that is not the manner in which this was used. Can you perhaps explain paragraph 5.1 and advise as to whether or not the amount used was different from what was actually in the contract?

MR. PEACO: Yes. One of the purposes of our work in this phase was to conduct a review of the terms of the PPA and see that the inputs being used in the calculation were consistent with the PPAs. This is one place where the language in the PPA was not as straightforward as we might

have liked -- as it may have appeared.
In the section that's referred here it refers to $7. And reviewed in the context of the section that the PPA is in which is energy pricing mechanism, and as the way Genco and Disco were using this, it was used as a $7 per megawatt-hour value. And that was how it was used in the analysis.
We were just noting that this was a point where the language could be clearer in the contract.
Q.401 - In fact I guess what you seem to be saying is that the method in which Genco and Disco applied this was in a sense at odds with what was in the contract?
The contract seems to call for $7 per fiscal year as opposed to $7 per megawatt-hour?
MR. PEACO: Well, I think as I say, the contract needs to be -- the document refers to Section 6.2.3 and 6.2 taken together, to make it clear that the context is an energy rate. But the one place where the $7 is mentioned does not give those units of dimension.
Q.402 - So if you used $7 per fiscal year as opposed to a per megawatt-hour -- and I have no idea of where this would go -- but if the PPAs are something that the parties have to live with, and if the contract language says something that I guess you feel it couldn't have meant to say that,

but nevertheless if it does say that, where would that -- what would that do with the outcome?

MR. PEACO: If you refer to A-96, exhibit A-96 --

Q.403 - Yes.

MR. PEACO: -- this number refers to row 3, the contribution of fixed costs to the vesting energy price. So I think it's a question as to whether the intent of the parties was to have $7 per year as contribution to fixed costs in the vesting energy price or 70 plus million dollars a year, and in the context of reading the agreement and what the intent was, the $7 per year is not really consistent with that concept.

Q.404 - I'm sorry. When you were giving that explanation I just didn't find it on A-96. Were you referring to --

MR. PEACO: I'm sorry.

Q.405 - Was that row 3?

MR. PEACO: Row 3.

Q.406 - Okay. Could you go through that explanation again please?

MR. PEACO: Sure. The row 3 values are derived from the $7 per megawatt-hour value. And adjusted for a CPI index I believe. So in these two budget years the contribution to fixed costs and the vesting energy price is 73.1 and 77.1 respectively.

That number is derived from taking the $7, and I think in this case adjusted for CPI, times the energy in the vesting energy agreement, to get a total contribution to fixed cost.

And reading the totality of Section 6 of the contract and the concept of being valued here and being the contribution to fixed costs, the $7 per year value did not make sense in the context of reading that section of the agreement.

Q.407 - And I appreciate your evidence that maybe it doesn't make sense in the context of the agreement.

But if the agreement itself says that it is $7 per fiscal year, what impact would that have on column 3, if in fact that was what the parties intended?

MR. PEACO: Well, it would be the difference between $7 and $77 million.

Q.408 - So the contribution to fixed charge would effectively be zero if it was $7?

MR. PEACO: That's correct.

Q.409 - Can anybody advise me as to whether or not the PPAs have been amended to reflect the manner in which they have -- this has been applied?

Because obviously it has not been applied in accordance with the strict wording of the contract. So has there been an amendment?

MR. KENNEDY: Excuse me. Could you ask that question again?

Q.410 - Sure. Have the PPAs been amended to reflect the $7 per megawatt-hour interpretation, if you will, from the $7 per fiscal year as it presently appears in the contract language?

MR. KENNEDY: What was done here was an interpretation was applied with respect to the $7. If you look at the vesting contract, and if you take vesting energy price -- I refer you to article 6.2, and specifically to 6.2.1 where it states "Except as otherwise specifically provided for this agreement, Disco shall pay Genco monthly for each megawatt-hour of net energy or energy purchased pursuant to this section." That is basically scheduled with the System Operator. That describes the vesting energy price. And then if you go to 6.2.3, "For each fiscal year the vesting energy price shall equal the fuel component plus the contribution to fixed cost, each in respect to that fiscal year."

So when you are adding the intent and analysis of the contract, it would be that the $7 contribution to fixed cost is $7 per megawatt-hour.

Q.411 - Mr. Kennedy, what exhibit number are you reading from?

MR. MORRISON: It is exhibit A-4. That would be the Genco vesting agreement. And it is article 6.2.1.

MR. GORMAN: Mr. Chairman, if we could just have a moment to pull up exhibit A-4. Thank you.

Q.412 - Mr. Kennedy, perhaps you could take us through that again? I did not have the exhibit in front of me at the time and it might be easier for me to follow with the exhibit.

MR. KENNEDY: Yes. Article 6.2 --

Q.413 - Yes, I have that.

MR. KENNEDY: -- do you have that?

Q.414 - Vesting energy price?

MR. KENNEDY: Vesting energy price. Except as otherwise specifically provided for in this agreement, Disco shall pay Genco monthly for each megawatt hour of net energy or energy purchased pursuant to Section 3.1.5.2 scheduled of the System Operator to be purchased and received hereunder by Disco for each hour during that month an amount equal to the vesting energy price. And then further to that --

Q.415 - Yes.

MR. KENNEDY: -- if you go to 6.2.3, for each fiscal year the vesting energy price shall equal the fuel component, plus the contribution to fixed costs each in respect of that fiscal year.

Q.416 - Well, I am afraid we are going to get into I guess an issue of legal interpretation and so I suspect that your counsel will be on his feet shortly, because Section 6.2.1 does say, except as otherwise specifically provided for in this agreement. You would agree that those words are there?

MR. KENNEDY: Yes.

Q.417 - And with the inclusion of those words, I certainly could read Section 6.2.6 to be something that's specifically provided for otherwise in the agreement, could I not?

MR. MORRISON: Mr. Chairman, I suspect that Mr. Gorman and I will have an argument on that but --

CHAIRMAN: You are not on your feet, Mr. Morrison.

MR. MORRISON: Don't have the energy this morning, Mr. Chairman. I read it a different way, but I am sure that we can have that debated at the appropriate time.

CHAIRMAN: Yes. I think summation is the time to do that, Mr. Gorman.

MR. GORMAN: Thank you, Mr. Chairman.

Q.418 - Mr. Peaco, I am now going to take you to page 15 of the initial audit.

MR. PEACO: I have that.

Q.419 - And I am referring specifically to Section 5.4, Availability of Supporting Data. And you state that there

were times throughout the document where La Capra Associates were unable to review source documents and relied on interviewing Disco and Genco personnel. Do you see that?
MR. PEACO: Yes.
Q.420 - And that would not be the preferable manner in which to conduct an audit, would it? Having the backup documents would be better evidence?
MR. PEACO: Yes.
Q.421 - And at the very last sentence on page 15 you say, however, not all input data could be completely verified as accurate, nor do La Capra Associates attest to such accuracy. Is that correct?
MR. PEACO: Yes.
Q.422 - But if you had the documentation available to you and had reviewed it exhaustively, you may well have been able to attest to its accuracy?
MR. PEACO: If I had been asked to conduct a review of every input to that effect, that's true.
Q.423 - Well can I say that if you had been asked to conduct an audit as opposed to a review, is that what it's coming down to again?
MR. PEACO: I am sorry. I am not clear on your question.
Q.424 - Well, I guess really what my point is, could you have

verified that data if in fact this had been a full audit as opposed to a review?

MR. PEACO: I take it, as you are using the term, full audit, could -- that would be the case.

MR. GORMAN: Can I just have a moment, Mr. Chairman.

Q.425 - Mr. Peaco, I think we already looked at the Phase II audit, which was exhibit A-9. But I am going to take you to page 5 of that -- of exhibit A-9 of the second audit. I am also going to take you to page 5 of the third audit, which is A-49?

MR. PEACO: I have those pages.

Q.426 - And exhibit A-9 has a note 6 and exhibit A-49 has a note 4. It appears to me that they are identical. In other words, they say in other words, the assessment was a reasonableness review, not a thorough audit, is that correct? Does that caveat in a sense apply to both number 2 -- report number 2 and report number 3?

MR. PEACO: Yes. As it pertains to the PROMOD inputs data set and modelling. In each case, the footnote is referring to a reference to the model structure and inputs and outputs of PROMOD.

Q.427 - Sure. And exhibit A-49 -- in fact if I go to the last full paragraph above the note, you indicate as in Phase II of the audit, the PROMOD analysis was the subject of a

technical review, but not a complete independent audit of the model structure and all inputs and outputs, is that correct?
MR. PEACO: That's correct.
Q.428 - If I could go back to A-9 at page 12. The last paragraph begins, based on the information available to us. Was there information not available to you?
MR. PEACO: I am sorry. The line reference again?
Q.429 - Sorry. It's page 12. It's under paragraph 4.2.1, Comparison to Historical Data. And it's the last paragraph and it's the first line that begins, based on the information available to us, and then you talk about what it includes and makes some conclusions.
My question is using that expression, based on the information available to us, are you telling us that there is information that was not available to you?
MR. PEACO: I think that is referring to the limitations on the information that you and I have discussed earlier this morning.
Q.430 - Thank you. Now, I am going to change to a different topic. Mr. Kennedy, you testified on Thursday that in terms of the arrangement with Genco for the supply of power, that basically it is done through an economic dispatch of units subject to contract constraints. That

may be my expression. But is that basically correct?
MR. KENNEDY: Yes.
Q.431 - And I understand that some of the units are must runs, is that correct?
MR. KENNEDY: Yes.
Q.432 - And the non-utility generators, I guess we have been referring to them as the NUGs, are they must runs?
MR. KENNEDY: Yes.
Q.433 - Is that the case in other jurisdictions? Does anybody on the panel know if that's the case?
MR. KENNEDY: It would not be uncommon. I wouldn't think with respect to a situation where the fixed component or the capacity component is in the contract as an energy charge.
Q.434 - That's an opinion though. Do you have any knowledge --
MR. KENNEDY: No.
Q.435 - -- as to whether or not that's the case in other jurisdictions?
MR. KENNEDY: No. I can't comment.
Q.436 - So does Disco interrupt the economic dispatch of your units in order to take energy from the NUGs even when it's more expensive?
MR. KENNEDY: The assessment is done based on the actual

load during that hour. And if the unit is it must run and if the load is such then that there could be a situation where lower cost units are being put out on the export margin out onto the export market.

Q.437 - So do you agree with the proposition I put to you that the economic dispatch of the units would be disrupted in order to take energy from the NUGs, because of your contractual obligations, but do you agree that that is the case?

MR. KENNEDY: Yes.

Q.438 - I believe that you testified that the most expensive power is generally being exported, but is that always the case?

MR. KENNEDY: Not lately. There has been some issues with respect to the hydro basically finding its way out onto the export market due to the abnormal conditions, the low loads, as well as the high hydro for this time of year.

Q.439 - Would there be any savings to Disco if all power was dispatched to Disco entirely on an economic basis?

MR. MAROIS: We did respond to an IR on that. I don't know the exact number. And at the end of the day, there was not much impact because, yes, you could lower the vesting price paid to Disco, but then you would reduce the export benefits. So they almost net out. There was a net difference of about $5,000,000.

Q.440 - And would that be a $5,000,000 benefit to Disco?

MR. MAROIS: No, it was not a benefit.

Q.441 - It went the other way?

MR. MAROIS: Yes. Maybe just for the record, the clause in the PPA, the Genco PPA that states that the NUGs must be run -- considered that must runs is in Schedule 6.2 section 2, subsection 2.

Q.442 - Now, If there are any more NUGs added in the future, will the cost to Disco increase in terms of having to buy power from these must run units?

MR. KENNEDY: It will depend on how the contract is structured with additional NUGs that would come under contract directly with Disco.

Q.443 - I just have one follow-up question on the series of questions that Mr. Lawson asked on hedging. And in looking at particular page 30 of the Power Point presentation, I see that the key elements or components of hedging relate to heavy fuel oil and currency. Is there any hedging on gas?

MS. MACFARLANE: Yes. By virtue of those heritage PPAs that Genco has with units that burn gas, the contracts are tied to gas indices. So although Genco is not buying and therefore not transferring on to Disco actual gas purchases, they are exposed to the natural gas market. And so hedging is done to cover that exposure.

Q.444 - Thank you.

MR. GORMAN: Those are all the questions from the Municipal Utilities. Thank you to the members of the panel.

CHAIRMAN: Thank you, Mr. Gorman. We will break now and come back at quarter after 1:00. And Mr. Hyslop you can be ready to go with your questioning then.

MR. HYSLOP: Thank you, Mr. Chair.

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

CHAIRMAN: Good afternoon. Any preliminary matters?

MR. MORRISON: No, Mr. Chairman.

CHAIRMAN: Go ahead, Mr. Hyslop.

CROSS EXAMINATION BY MR. HYSLOP:

Q.445 - Thank you, Mr. Chair. Good afternoon, Panel, and especially Mr. Peaco and Mr. Kennedy from Summerville, Carleton County, New Brunswick.

I just want to take maybe a moment or two and just kind of put in perspective a little bit where we are at. And last week you will recall we spent some time dealing with some of the policy in the White Paper. And one policy I didn't touch on was the refinements to the regulatory regime. And just quickly in looking at page 28 of the Paper -- of the White Paper -- under the heading

3.1.6.1, one of the recommendations was -- I'm looking halfway down through the first paragraph on the fifth line.

It says, most importantly with respect to the generation business the province will give the Board authority to monitor the competitiveness of the wholesale market and ensure that the Crown utility is unable to exercise market power.

Would the Panel agree that that was one of the policies set out in the New Brunswick energy policy? I think probably Ms. MacFarlane --

MS. MACFARLANE: Yes.

Q.446 - Thank you. And also in that regard I understand in fact that recommendation made its way into the Electricity Act and, subject to check, I think it was Section 127. Would that be your understanding, Ms. MacFarlane?

MS. MACFARLANE: Subject to check, yes.

Q.447 - Thank you very much. Now just looking at the problem as a whole. I understand this White Paper came about to some extent in the late 1990's and early part of this decade and part of it -- I think probably the progenitor of it was the issue of the fact that around 1997 or 1998 it was necessary to take a $450 million write down due to Point Lepreau. Would there be some cause and effect

there?
MS. MACFARLANE: I have never understood there to be. There might well have been but I have never understood that to be the case.
Q.448 - But in any event it's fair to say that because of this write down and because of some of the problems that the Chair alluded to the other day, the debt of NB Power was becoming a significant problem?
MS. MACFARLANE: That's correct.
Q.449 - Right. And this debt of course was held by the taxpayers of New Brunswick as represented by their government?
MS. MACFARLANE: That's correct.
Q.450 - And I would expect that the people in the Department of Finance started asking questions about how can we get some of this repaid, would that be fair -- I'm sorry, NB Power wanted to look at ways of doing this?
MS. MACFARLANE: That's correct.
Q.451 - Right. And also at this time -- and I don't know the value of the asset at that time, but right now the ball park value of the NB Power group of companies is about $3.5 billion?
MS. MACFARLANE: That's correct.
Q.452 - Right. And I imagine most people that owned such an

asset would be looking for a way to at least make some return on their investment?
MS. MACFARLANE: That's correct.
Q.453 - Right. Okay. So that kind of puts things in perspective. And for that reason we brought in some industry advisors and financial experts to assist?
MS. MACFARLANE: The province did, yes.
Q.454 - Yes. I'm saying we. I guess more particularly the Province of New Brunswick. And you mentioned the other day -- I think during Mr. Lawson's cross examination you referred to them as bankers. So I take it that's merchant bankers we were dealing with?
MS. MACFARLANE: They were investment bankers.
Q.455 - Investment bankers. And they were asked I assume by the province how we go about answering the questions of this debt and getting a return on our assets, is that correct?
MS. MACFARLANE: I suspect the terms of reference was broader than that, but that was certainly part of it, yes.
Q.456 - Okay. Well if you are owed, you know, the amount of money the province was it certainly would be one of the key factors, would you agree?
MS. MACFARLANE: Yes.
Q.457 - Right. So we had this reorganization and

restructuring and this included the Electricity Act which I think we looked at, the role of EFC and the shareholder's agreement, they would be some of the key parts of this reorganization?

MS. MACFARLANE: That's correct, yes.

Q.458 - Right. And the one part we are now dealing with is the purchase power agreements, and I think certainly from what we have read and heard these are an integral part of this reorganization?

MS. MACFARLANE: That's correct.

Q.459 - Right. Okay. In fact when I asked questions on some of my IRs which were subsequently revised, but the question of what is in and what is part of these PPAs, the understanding I got -- and I appreciate that this has been withdrawn and replaced -- but at one time I was told that what is in these PPAs wasn't challengeable.

In view of the fact that we discussed this overriding power of the Public Utilities Board would you agree with the concept this Board at some point in time has a regulatory authority over the purchase power agreements, or is that just something that's absolutely locked in stone from the applicant's point of view?

MR. MORRISON: I don't know whether the witnesses are qualified to answer that question, Mr. Chairman. I think it does require an interpretation of the Statute.

MR. HYSLOP: Okay. I will live with the fact -- would you accept that answer of your attorney then?

MS. MACFARLANE: Yes.

Q.460 - Thank you. Now one other little point there. These merchant bankers were brought in in part I assume to -- as much as possible to allow a return on this investment with a certain element of a risk attached to it?

MS. MACFARLANE: As I understand it they were involved in the unbundling of the electricity market in Ontario and in forming the relationships between the successor entities to Ontario Hydro, and they were also involved in some of the power purchase agreements that were outside of the Ontario Hydro successor group, and that they were asked to undertake a restructuring of the corporation and put in place these power purchase agreements in a way that would allow for recovery of that debt over a reasonable period of time, and further allow that any debt incurred by the NB Power group of companies thereafter would be on its own credit.

Q.461 - Sure. And given that background would the possibility of a noisy Public Intervenor upsetting the apple cart and causing an unfavourable regulatory ruling be one of the risks that these people might have wanted to try to avoid?

MS. MACFARLANE: I'm not sure what risk they were specifically trying to avoid.

Q.462 - Sure. In any event I want to deal with some aspects of the purchase power agreement and in particular I think everybody can probably pull the purchase power agreements out in front of them. I will be dealing with them fairly consistently through my cross examination. And the one I will be dealing with probably 95 percent of the time is the Genco vesting agreement which is the third tab in exhibit 4.

I want to deal first for a few minutes with the capacity payment. And that is referred to in article 6 under the heading Price and then 6.1, Capacity Payment at page 45. And the other day, Mr. Kennedy, you indicated that some payments were wired-in payments, is that correct?

MR. KENNEDY: Yes.

Q.463 - Yes. And my interpretation of what you meant was that this was amounts or numbers that could be plugged in through the PROMOD directly from the power purchase agreement itself. Is my understanding correct?

MR. KENNEDY: The numbers that I'm referring to are numbers that can be calculated quite easily from the power purchase agreements. And one of them would be the capacity payment for example --

Q.464 - That is right.

MR. KENNEDY: -- in the Genco PPA.

Q.465 - Right. And that is because the identification of the capacity payment and the amount that it is is actually referred to in Schedule 1.1.17, is that correct?

MR. KENNEDY: That is correct.

Q.466 - Right. And that is found at the first page after the last page of the contract which is page 123. And for the purposes of the purchase power agreement there is a table. And it indicates the specific year and the specific capacity payment for that year, is that correct, Mr. Kennedy?

MR. KENNEDY: That is correct. It outlines the monthly payment with respect to capacity.

Q.467 - Right. And I take it, Ms. MacFarlane, that these capacity payments in this schedule were developed by your merchant bankers?

MS. MACFARLANE: Investment bankers, yes.

Q.468 - Yes. I'm sorry. Investment bankers. And, Mr. Peaco, I take it as part of your retainer what you did is you came down and you looked at this part of the purchase power agreement. And for example in the year 2004/2005 you would have ensured that the price per megawatt per month of $9,477.50 was properly inputed into the PROMOD model?

MR. PEACO: Well, technically it wasn't in the PROMOD model. But yes, in phase 1 we did verify the capacity computation that Genco and Disco did.

Q.469 - Yes. Now part of your review would not have been however to make an analysis of this $9,477.50 as to its appropriateness?

MR. PEACO: That's correct.

Q.470 - Right. And I understand, Ms. MacFarlane, that in fact these capacity payments include the return on the investment given the -- I'm going to use the word deemed and implied but the deemed capital equity structure and implied rate of return over the life of the contract?

MS. MACFARLANE: Yes.

Q.471 - Right. So -- and then, Mr. Peaco, I understand that in your practice you would have been involved in return on equity hearings from time to time?

\ MR. PEACO: Our firm has been. I have not.

Q.472 - Okay. Would you know enough about those type of hearings to know that often there is a great deal of evidence in support of whatever the capital structure being developed and the return on equities might be?

MR. PEACO: For a regulated cost of service?

Q.473 - Yes.
MR. PEACO: Yes.
Q.474 - Yes. Okay. And so in this case you didn't review any documents which would have determined whether for example for Genco the 50/50 debt equity structure and the 11 1/2 percent return on equity would or would not be appropriate? You have reviewed no documents in that regard?
MR. PEACO: I was not asked to look at any such information, no.
Q.475 - Now I was looking down through this, Ms. MacFarlane. And I think the other day you indicated that there would be a few years of transition. And then we would go into a phase where the full rate of return that was expected would be built into these capacity payments. I think you led some evidence to that effect?
MS. MACFARLANE: That's correct.
Q.476 - Right. And when I look down through these I see an increase for the first few years. And then in the year ending 2008 I see $13,027.72 per megawatt-month. Do you see that number?
MS. MACFARLANE: That's correct.
Q.477 - Right. And I calculated that number to be about a 20 percent increase from the year ending March 31st 2007. Is

that correct?

MS. MACFARLANE: Subject to check I will accept your answer.

Q.478 - It is 20 percent and change. But please check. And I would if it was my number. So I guess that is the year you are anticipating the full capital structure to kick in. It would be the end of 2008 according to the schedule?

MS. MACFARLANE: The full cost of equity is to be recovered over the length of the contract. And it's not an exact science. It obviously will depend on the operating circumstances and the success of Genco's management of the day.

But conceptually that was the intent, that by 2008 Genco would be earning its returns as designed by the financial advisers.

And as you see the capacity payment therefore remains constant until 2016 when it then begins to decline because some of the amortization on some of the units begins to decline.

Q.479 - Right. And the amortization on the units, that would normally be part of the fixed or capacity costs for the generation assets?

MS. MACFARLANE: That's correct.

Q.480 - Right. And I don't see any depreciation for these

assets for the first -- from 2008 until we hit 2017. Am I to assume that that is because you are using a straight line depreciation method?
MS. MACFARLANE: We are using straight line depreciation.
Q.481 - I gathered that from your financial statements. And we went into the other day the differences between that methodology and the methodology under the Income Tax Act and whether that would have any impact.
Under the Income Tax Act I understand the balance declines annually as opposed to taking so much depreciation each year?
MS. MACFARLANE: That's correct.
Q.482 - Right. And have you calculated or tried to calculate the difference or the impact of that difference throughout the first 10 years of the capacity payments?
MS. MACFARLANE: No, we have not.
Q.483 - Do you know whether your investment bankers did this as part of their analysis?
MS. MACFARLANE: If they did do it they did not share it with NB Power.
Q.484 - Okay. So they may have shared that only with the government? Okay.
Now my question is the increase -- and this is subject to check -- but when I take this increase from 2007 to

2008 -- and I understand that roughly calculates out to an increase in the price of electricity under the PPA as an increase of about $86 million. Subject to check would you advise whether you agree or disagree with that?

MS. MACFARLANE: I believe that we have either been asked or perhaps even filed an undertaking on that. And our undertaking would suggest that the increase puts out $37 million in year over year between '07 and '08.

Q.485 - But I'm not asking between '07 and '08 as a whole. I'm just asking with respect to the capacity payment?

MS. MACFARLANE: That is just the capacity payment. It increases by 37 million.

Q.486 - I will accept that and chat with you over coffee the number. So it is $37 million gets kicked in that year.

MR. MAROIS: Which year are you looking at, Mr. Hyslop?

Q.487 - I'm looking at the increase from '07 to '08, Mr. Marois.

MR. MAROIS: I think it's 26 million.

MS. MACFARLANE: We have a undertaking. As I say, it's either filed or it is being prepared to be filed. And the number will be confirmed at that time.

Q.488 - Thank you. I will accept that. Now again I want to go back. As far as the purposes of regulation -- of the capacity payment, your technical audit person has indicated that he made no review as to the reasonableness of the 9,477.50 number, correct?

MR. PEACO: Yes.

Q.489 - Right. And in that regard would it be your intention then, Ms. MacFarlane, at the next hearing before this Board for a rate increase or any review hearing, to present the evidence in support of the reasonableness of the $9,477.50?

MR. MORRISON: Mr. Chairman, I'm going to object to that question. Can we please try to keep this focused on this hearing and let the future take care of itself? I don't think that is an appropriate question for an 06/07 revenue requirement hearing.

CHAIRMAN: Mr. Hyslop, repeat that question please?

MR. HYSLOP: Okay. My question is -- and it goes back -- I will repeat the question first. I'm asking with respect to determining the reasonableness of the $9,477.50 capacity payment, in view of the fact it is only contained in a power purchase agreement, without any audit or check, I have asked whether or not it will be the intention of the utility at the next rate hearing or at any review hearing to present evidence which would be in support of the reasonableness of the $9,477.50?

And the reason I ask it, Mr. Chair, in answer to

Mr. Morrison's objections, the first two questions I asked go to the role of this Board in terms of its power to regulate and monitor the generation business as we go through the movement to competition.

And I'm trying to understand exactly down the road when we will actually get a chance after this hearing to determine the reasonableness of many factors in the PPA agreements.

CHAIRMAN: Be careful, Mr. Hyslop, when you say regulate or monitor. Because I think our jurisdiction is to monitor --

MR. HYSLOP: Yes.

CHAIRMAN: -- and not regulate. And we kept pretty well to the test year. But I think the line of questioning the PI is pursuing right now is okay. So would you answer the question.

MS. MACFARLANE: I believe, Mr. Hyslop, that NB Power and yourself would perhaps take a different interpretation of the words in Section 156 that say for purposes of the first hearing.

It is NB Power's understanding that the intent of that section was to protect the PPAs as they exist and to open to review of reasonableness any changes to the PPAs.

And with that understanding -- and I believe that that may be subject to argument. But with that understanding it is not our intent at anytime to provide evidence to support the reasonableness of the capacity payments. Because we don't believe it was the intent of the designers to call for that to happen.

Genco specifically under the Act is not regulated. And the PPAs, we believe under Section 158 the foundation -- the baseline of them is not subject to regulatory review.

Q.490 - That is fine. And would that also hold to any other of the set prices in the power purchase agreements, Ms. MacFarlane, in your view?

MS. MACFARLANE: That's our understanding of the way the legislation was constructed and the way the PPAs were constructed.

Q.491 - Now I want to talk a little bit about the method of the vested energy price under Section 6 of the power purchase agreement. Now as I understand the methodology for establishing the price -- and when it comes to the fuel purchases, you do a PROMOD run of some sort to determine the volumes of fuel you will need in the test year?

MR. KENNEDY: Yes, that's correct.

Q.492 - Right. And then you take the prices of the heavy oil on October 1st of the year preceding the financial year -- fiscal year in question?

MR. KENNEDY: At the time of preparing the budget we look at the forward prices and we factor in also the hedge prices that are in play at that time.

Q.493 - You factor in the hedge prices?

MR. KENNEDY: Yes.

Q.494 - Okay. So will you know the actual hedge prices on October 1st for each year you are using the hedge prices and not the October 1st price? I was confused a little bit by that the other day. Do you use the October 1st spot price to set the fuel prices in the PPAs?

MR. KENNEDY: It is used to determine the dispatch the forward prices -- the spot price is used to determine the dispatch and then the hedges are factored in to -- the hedge settlement is factored in to come back to the actual hedge price that is used to determine the fuel component price for the year, the budget year. In this case it would be 06/07.

Q.495 - Okay. So the October 1st 2005, spot price, that's not multiplied by the volume of fuel that you would need to establish the fuel component in the PPA?

MR. KENNEDY: No.

Q.496 - You use the hedge prices as they exist at that time?

MR. KENNEDY: Yes, that's correct.
Q.497 - So there would be six months -- you would have the whole year hedged on October 1st then on an 18 month basis?
MR. KENNEDY: Yes.
Q.498 - So you are using the hedge prices themselves?
MR. KENNEDY: That's correct.
Q.499 - So it's the actual hedge prices that Genco has incurred -- is expected to incur that are used to determined the fuel component on the PPA price?
MR. KENNEDY: Yes.
Q.500 - And at the end of the day though if you had a price -- a hedge price that comes due on July 1st 2006, is there any reconciliation of that price against the actual price on July 1st that enters into the pricing?
MR. KENNEDY: No.
Q.501 - No. So do you do an analysis of the hedge prices against the actual prices to measure in some way the effectiveness or efficiency of the hedging itself?
MS. MACFARLANE: There is a calculation done simply because the settlement has to be made of the hedge price when the contract comes due. We do not track that for purposes of looking at the effectiveness of hedging because that by definition is a rear view view -- rear mirror view, and is

not -- is not relevant to the effectiveness of the hedging.
The hedging policy is there to ensure predictability, to enable us to set our budgets, to set the vesting energy price and to -- in the case of Disco is necessary to go forward to the regulator.

Q.502 - Now -- and in that regard -- you use the word hedging but would I be more accurate to say you are just buying futures, Ms. MacFarlane?

MS. MACFARLANE: The hedges are future contracts, yes.

Q.503 - Yes, that's right. But you are not involved in any speculation, that's outlined in your policy. You leave that right alone?

MS. MACFARLANE: That's correct.

Q.504 - So you would agree it's not a very aggressive -- and in fact I think you described it as a very conservative method of purchasing fuels?

MS. MACFARLANE: Yes. And I think I had said at the time that it was the view of our Board that NB Power has very high operating risk, much of which we have no control over, and that therefore we should do whatever we can to mitigate financial risk.

Q.505 - Okay. Now you hold these contracts all to maturity. You are not buying or selling them on an ongoing basis, your future contracts?

MS. MACFARLANE: We hold them to maturity. The only time there is any activity on them other than at the expiry date is if the load forecast changes for some reason and we find ourselves over-hedged, in which case the contracts are terminated, or in some cases moved to another month.

Q.506 - And if you hold these contracts to maturity and the contracts settle against spot prices, do you agree it's not possible to know what the settlement costs or credits will be ahead of time?

MS. MACFARLANE: That's correct.

Q.507 - Right. And if the settlement costs or credits will not be known at the time the vesting energy prices set -- let me rephrase that. And you wouldn't know the settlement costs or credits at the time the vesting energy price is set, is that correct?

MS. MACFARLANE: We do not know the settlement amounts when the vesting energy price is set, but the amount of cash out the door paid is the hedge contract amount, and that is the amount that is included in the vesting energy price.

Q.508 - And are expected hedging settlement costs ever trued up to the actual hedging settlement costs or credits and then flowed back into the PPA prices?

MS. MACFARLANE: As I say I may be miscommunicating how a hedge contract works. Regardless of what the spot price of the day is what Genco pays is the contracted hedge amount. So from that perspective that is the as I say cash out the door and that is the amount known in advance that is included in the vesting energy price. There is no plus or minus cash coming in or out. It's simply we pay the contract amount.

Q.509 - And you don't factor in what the price would be based on the spot price on the closing date of your futures contracts?

MS. MACFARLANE: No, we don't, because we have paid the hedge price.

Q.510 - I appreciate that, but I'm just saying there is no truing up of those things at that time?

MS. MACFARLANE: No, there is not.

Q.511 - So at the end of the day if we looked at the actual markets on the date that these contracts were actually settled, there is never any reconciliation to the price on that specific date?

MS. MACFARLANE: The way the contracts work is that we physically are buying heavy fuel oil as an example from suppliers. So there is a cheque out the door to the supplier. There is a subsequent payment or credit received from the counter party to the financial contract and it is that net amount, the amount paid to the supplier, plus or minus the amount settled with the counter party that represents the contracted amount in the hedge.

Q.512 - Yes.

MS. MACFARLANE: And so to enable that payment to or receipt from the financial counter party with the hedge contract, there is a calculation done. But as I say the net amount out the door is the amount contracted for in the previous year.

Q.513 - Now the hedging policy in exhibit A-55, Appendix 7, that was the relevant hedging policy for fiscal year 2006/2007?

MS. MACFARLANE: Yes, it was.

Q.514 - And that policy remains in effect as we go forward?

MS. MACFARLANE: Yes, it does.

Q.515 - Thank you. And the policy states that the fuel is to be hedged 80 to 100 percent of the volumetric targets for 18 months. Can you explain how the policy is implemented given the structure of forward fuel and foreign exchange markets?

MS. MACFARLANE: First I'm going to ask you if you could give me the appendix number again, please?

Q.516 - 7. I'm sorry. That's exhibit A-55.
MS. MACFARLANE: Could you repeat the question, please?
Q.517 - Yes. I was asking can you explain how this policy is implemented given the structure of the forward fuel and foreign exchange markets?
MS. MACFARLANE: The policy is operated by a committee, financial hedging committee, and once a month the hedging committee receives the most recent updated forecast for the next 18 month period.
And at that point in time there is a recommendation that comes forward from the operating members of the hedging committee and that would be the people involved in the production modelling, people involved in fuel purchasing, the treasury group, et cetera, and they make a recommendation as to what hedged transaction should be undertaken on foreign exchange, on natural gas and on heavy fuel oil for the eighteenth month. And if there is any change in the 18 months that is already hedged -- the 17 months that is already hedged, if there has been any change in the outage schedule that has arisen or any characteristics of the operating units that have changed such that the forecasts has changed and we find ourselves in those periods either over or under 80 percent, then those adjustments are recommended as well, and the hedging

committee reviews those and approves them and then the transaction is effected.

Q.518 - Now I'm just trying to get an understanding not how it works internally but outside of NB Power. So if you entered into a futures contract for fuel for April of 2006, you would be making that contract 18 months ahead, i.e., in October 2004?

MS. MACFARLANE: That's correct.

Q.519 - Right. And would the company then be entering into a hedging contract for May 2006 in November 2004, 18 months prior?

MS. MACFARLANE: That's correct.

Q.520 - Right. And would the company be buying seasonal or annual hedging products?

MS. MACFARLANE: In the case of natural gas --

Q.521 - Yes.

MS. MACFARLANE: -- we would buy in strips. And I believe they are five month strips. In the case of heavy fuel oil we buy based on the hedged price or the hedge prices available in the market for the particular month.

Q.522 - Would the 18 months be calculated from the first delivery date or from the last delivery date for the product in question?

MS. MACFARLANE: We would be looking at any deliveries

required during the calendar month.
Q.523 - Okay. Do you rely on expertise outside of NB Power for purposes of purchasing your futures contracts?
MS. MACFARLANE: We rely on outside expertise in terms of how the policy operates, the methodology, how the committee operates, et cetera, and we have been relying on a consultant called Risk Advisory Group in Calgary in terms of effecting the transactions themselves. They are done by internal staff directly with counter-parties. There is generally three quotes obtained and then the most attractive quote at the moment is the one selected.
Q.524 - Have you obtained or assessed the possibility with your outside experts of a more aggressive futures purchases policy?
MS. MACFARLANE: Could you give me an indication what you mean about more aggressive?
Q.525 - Well you indicated that your reliance on futures contracts is very conservative. It's an 18 month, to use Mr. Lawson's phrase, riding the wave, and my question is have you looked at a more aggressive policy which could result in fuel savings -- fuel cost savings?
MS. MACFARLANE: Generally speaking more aggressive, Mr. Hyslop, equates with more risk, and it may result in more savings, it may result in more cost. The program that we

have is not aimed at savings. We are not speculating, we are not trying to beat the markets. We are not in that business. And as I think I said to one of your counter-parties, I probably wouldn't be working with NB Power if I was able to predict the fuel markets. I would either be rich or bankrupt I think Mr. Lawson said.

So no, we have not looked at a more aggressive policy because our advisors have told us that that is not appropriate for a regulated entity.

Q.526 - You are making the point Genco is not a regulated entity?

MS. MACFARLANE: Genco and Disco both have exposures. They both have different applications of this policy. The way Genco is hedging is at the request of Disco. If that request had not been made Genco's only exposure arises when it sets the hedge price -- or the vesting price, pardon me, on October 1st, and that's when Genco would be hedging. And all those costs would be passed on to Disco.

Q.527 - I want to talk about the third party gross margin credit, which is in Article 6.3. It shows up at the bottom of page 46.

Q.528 - And to just walk my way through it. And also I think you have to look at schedule 6.2.3. But I'm going to kind of run a little hypothetical so I understand how it works.

If third party gross margin credit for a given year was set at $70 million, I understand that results in two thresholds being created, a lower threshold which is 20 percent less or $56 million?
MS. MACFARLANE: That's correct.
Q.529 - And an upper threshold of $84 million which is 20 percent more than the $70 million?
MS. MACFARLANE: That's correct.
Q.530 - Right. And I understand if the third party gross margin credit in a given year then fell between the 56 and $84 million, that the amount of the credit which Disco would be entitled would remain at $70 million?
MS. MACFARLANE: That's correct.
Q.531 - Right. And if it falls lower than 56,000,000 Disco pays 50 percent of the difference?
MS. MACFARLANE: That's correct.
Q.532 - So in the example I stated, if the third party gross margin credit actually was 40,000,000 in a given year, then Disco would pay Genco 40 less 56 minus 16 divided by two and pay them $8 million?
MS. MACFARLANE: That's correct.
Q.533 - Right. And similarly if the third party gross margin credit in a given year was $100 million, then Genco would pay Disco another $8 million on top of the $70 million we

started with?

MS. MACFARLANE: Did you say if the third party gross margin credit was 100,000,000?

Q.534 - Yes.

MS. MACFARLANE: The difference is 30,000,000. Oh, I see. It's the difference over the 20 percent. Yes, you are correct.

Q.535 - That is right. Yes. It would be over -- you take it from the threshold, not from the 70'?

MS. MACFARLANE: Yes. That's correct.

Q.536 - And if you want to take it from the 30' we won't object.

Now I was wondering. Now Mr. Peaco, when you did your analysis, I take it your analysis or your audit or technical audit, what you did is you reviewed the amounts of the third party gross margin credit as set out in the power purchase agreement?

MR. PEACO: In phase 1 we did, yes.

Q.537 - Yes. And in phase 1 you would have accepted these as the numbers from the contract and would have used them for purposes of going through your investigation to determine the proper electricity prices, correct?

MR. PEACO: That's correct.

Q.538 - Right. Now you didn't do any investigation as to the actual reasonableness or appropriateness of third party gross margin credits as specified in the power purchase agreement?

MR. PEACO: As to the derivation of the numbers in schedule 6.3?

Q.539 - Yes.

MR. PEACO: No, I did not.

Q.540 - No. You didn't do that. Okay.

And I understand, Mr. Kennedy, this is another one of those wired-in numbers?

MR. KENNEDY: Yes.

Q.541 - Thank you. And I also recall in dealing with the third party gross margin credit this is something you look at on an every five-year basis, is that correct?

MR. KENNEDY: Yes.

Q.542 - Right. Now -- and I also understand that, looking quickly at the schedule under 6.6.3, and in particular under the credit for the year on March 31st 2009 there is a considerable drop from about 69,000,000 down to around 19,000,000?

MR. KENNEDY: That drop is due to the Point Lepreau refurbishment project with respect to the fact that Genco has to haul its asset back and serve the in-province customers.

Q.543 - Right. And now just as a little something, Mr. Peaco. If the third party gross margin credit was set artificially low, would that tend to remove the risk from Genco and put more of the risk on Disco?
MR. PEACO: I'm sorry. You are saying if this was set too low?
Q.544 - Yes.
MR. PEACO: Relative to what?
Q.545 - To a reasonableness or an appropriate amount determined --
MR. PEACO: You mean if the export market was consistently higher than this?
Q.546 - Yes. That would tend to work in Genco's favor?
MR. PEACO: Yes.
Q.547 - Yes. Thank you.
I won't ask my obligatory one, how you are going to approve this at the next hearing.
CHAIRMAN: Mr. Hyslop, I think we will take our 10-minute break right now.
MR. HYSLOP: My voice appreciates that very much, Mr. Chair.
(Recess - 2:00 p.m. - 2:15 p.m.)
CHAIRMAN: Mr. Morrison, in your summation I know you will address the interpretation of 156. And when you do, answer why the government of the day, if it shares your

view, would have passed the regulation it did defining first hearing.

MR. MORRISON: Fine, Mr. Chairman.

CHAIRMAN: Thank you. Okay. Any preliminary matters? Mr. Hyslop?

MR. HYSLOP: I can only wait to disagree with Mr. Morrison on some of those issues.

Q.548 - Just following up on the last line of questions, panel, I recall at one time at the Coleson Cove and Point Lepreau hearings the great claims that NB Power used to make that the third party credits were a benefit, a significant benefit to the ratepayers of New Brunswick. Am I to conclude from the way the third party gross margin credit now works that the full benefits of a good year in the gross margin credit at least no longer all fall to the ratepayers as some of it heads to Genco?

MR. MAROIS: From a forecast perspective they all go to Disco. If you look at schedule 6.3 the amounts there are 100 percent of the amounts that were forecasted at the time.

So on a forecast basis it goes 100 percent to Disco, then it's the variance that gets shared between Disco and Genco. So from a forecast point of view it still goes 100 percent to Disco.

Q.549 - My understanding, Mr. Marois -- and Ms. MacFarlane may correct me if I'm wrong -- the amount of the third party gross margin credit to Disco is the amount that is provided in schedule 6.3, correct?

MR. MAROIS: That's what is factored into the PPA, yes.

Q.550 - Yes. And if the third party gross margin credit happened to be 20 percent more in one year, that would not add to the amount of the third party gross margin credit that Disco would receive, would it?

MR. MAROIS: Are you talking actual versus --

Q.551 - I'm talking actual versus forecast.

MR. MAROIS: Well, I believe that is what I just said. I said from a forecast perspective 100 percent of the benefits flow to Disco. If there is a variance then the variance gets shared based on the formula as in the PPA.

MS. MACFARLANE: I think Mr. Hyslop --

Q.552 - The word I missed was "forecast".

MS. MACFARLANE: Yes.

Q.553 - I understand.

MS. MACFARLANE: Because rates are set on forecast.

Q.554 - Right. And I understand that they are set on the forecast.

But as Mr. Peaco has indicated, he has done no evaluation as per part of these proceedings to determine whether or not the forecasted amount and the amounts set out in 6.3 are properly forecasted or might be high or might be low.

And I understand that from your evidence, Mr. Peaco, you have made no such assessment?

MR. PEACO: That's correct.

Q.555 - Thank you.

Another clause I looked at in this PPA agreement was article 16 which is the termination clause.

MS. MACFARLANE: Mr. Hyslop, while people are finding that I can clarify for you the capacity payments. It was undertaking A-110 of February 14th. It indicated that the capacity payment in the year ending March 31st '08 is $36 million higher than it is in the year ending '07.

And I think the confusion is that you are asking your questions on the Genco price only. And the monthly payment is on schedule 1.1.17 on the opposite page.

That's the way the capacity price is calculated. And it's a blend of the Coleson price and the Genco price given the agreement.

Q.556 - I will check that out.

Now dealing with article 16, that deals with the term and the default and the termination of the contract?

MR. MAROIS: Yes.

Q.557 - And there is a couple of questions. So we will just clear it out. But it commences on the 1st day thereof and shall include all days up to and including the later of the date upon which the nominated capacity is zero or the date that the Coleson Cove tolling agreement terminates or the term expires.

So the later of those dates I'm suggesting will likely be the date that the nominated capacity becomes zero?

MR. KENNEDY: Yes.

Q.558 - Yes. And that -- right now the nominating capacity is 2425 megawatts?

MR. KENNEDY: Yes. Subject to check I believe that's it, or a ball park.

Q.559 - And that involves the capacity of all the so-called heritage -- of generation assets of Genco?

MR. KENNEDY: That includes all the heritage assets of Genco including the peaking assets --

Q.560 - Yes.

MR. KENNEDY: -- which amounts to 1258 approximately megawatts?

Q.561 - It doesn't include the CTs?

MR. KENNEDY: Yes. It does include the CTs.

Q.562 - Okay. So we are paying the capacity charge on those as well. Now what I was wondering, Mr. Kennedy, was that one of the recommendations in the White Paper to increase competition in the market was to sell off some of the various generation assets.

What would happen to this contract if for example the EFC decided it would sell off your Belledune generation station?

MS. MACFARLANE: Mr. Hyslop, the Act does not allow for that. The Act only allows for the Coleson Cove operation or plant and the nuclear plant to be -- to have third party investment.

Q.563 - Okay. So that the prospect of selling off the generation assets of Genco not only isn't something envisioned by the vesting agreement, it's something that's not envisioned by the Electricity Act, correct?

MS. MACFARLANE: It is envisaged as it goes to Coleson Cove, and remember that Coleson Coveco is a subsidiary of Generation, and as it goes to Lepreau I believe that the thinking at the time with the energy policy was that each of those provide approximately one/third of the capacity in the province, and that if those two assets were no longer owned by NB Power we would have three different major suppliers in the province.

Q.564 - But within the group of generation assets besides Coleson Cove and Point Lepreau there would be no intention

within the Act or within the -- I was only going to ask about the PPA -- to further the intention to create said competition?
MS. MACFARLANE: That's correct.
Q.565 - Thank you.
MR. MAROIS: Mr. Hyslop, I just wanted to correct maybe one statement. In the previous question you mentioned we were paying capacity charges on the CTs. We are not.
Q.566 - On the CTs?
MR. MAROIS: Yes. We are not. It's only -- the capacity charge only applies to base load generation.
Q.567 - Okay. Thank you. Now just going back to the La Capra report, Mr. Peaco, if we could. My understanding from reading your reports, and in particular I think the first exhibit, A-5, can you confirm that in doing so you were only looking at the budgeted cost but did not look at any of the year-end adjustments that would be made to the purchase power prices?
MR. PEACO: That's correct. That would be the budget set at the beginning of the fiscal year.
Q.568 - Right. And are you in a position to list the year-end adjustments? Do you know what they are?
MR. PEACO: No, I do not.
Q.569 - Thank you. And -- however, can you in your opinion

and knowledge of these adjustments, could in some years these adjustments be fairly large and significant in theory?

MR. PEACO: I really haven't looked at the magnitude of them in the system.

Q.570 - Thank you. So you didn't examine or opine on a reasonable range for these adjustments as part of your review?

MR. PEACO: No, I did not.

Q.571 - No. Has La Capra and yourself acted for regulators from time to time in reviewing of purchase power agreements submitted for their consideration?

MR. PEACO: For regulators with respect to reviewing a purchase power agreement?

Q.572 - Yes. I shouldn't say La Capra. I guess I'm asking specifically whether you have, Mr. Peaco?

MR. PEACO: I have not worked on behalf of regulators.

Q.573 - Okay. Have you acted for parties who have been in the position of a purchaser of purchase power under agreements in negotiations or in conducting a review of the pricing under purchase power agreements supplied to them?

MR. PEACO: Yes. I have worked for parties entering into agreements and I have worked for parties intervening in proceedings, reviewing, but not on behalf of regulators per se.

Q.574 - Okay. In view of the fact that this is a first hearing under a new purchase power agreement, Mr. Peaco -- and I appreciate that you may or may not have a position on this -- but if you were retained for example by a regulator with regard to this, would it be your view that the acceptable practice would be a full and complete audit of the various factors going into the purchase power agreements as being preferable? Would that be your professional recommendation?

MR. PEACO: Could you help me out with what you would consider a full and complete audit?

Q.575 - Okay. A full evaluation of all the various input prices, for example in this case an evaluation of the capacity price, an evaluation of the vested energy price, a full evaluation of the reasonableness of many of the factors which you simply relied on the statements by the applicant that they were relying on historical costs without an examination of those historical costs?

MR. PEACO: I'm not sure if you are distinguishing between the forming of the PPA versus the interpretation of the PPA in your question.

Q.576 - Okay.

MR. PEACO: Can you help me with that?

Q.577 - Okay. Well I will do my best. With regard to the formation of the purchase power agreement, if you were advising a regulator as to the reliability and the extent they would want to go, would you advise that regulator that it would be proper to complete a full investigation of those various items?

MR. PEACO: If the PPA were being brought before the regulator for approval or inclusion in rate base or in rates for the first time is the subject of a prudency review, it would be.

Q.578 - Thank you. You indicated some experience with PROMOD in your direct examination, Mr. Peaco?

MR. PEACO: Yes.

Q.579 - Yes. And I have heard all kinds of numbers. But could you ball park the number of inputs that would actually be used into a PROMOD model?

MR. PEACO: In terms of individual data elements?

Q.580 - Yes.

MR. PEACO: No. There is quite a number.

Q.581 - Okay. Would it be in the hundreds?

MR. PEACO: Surely.

Q.582 - Okay. Now just refer you briefly to exhibit A-5 which is your report of May 18th. And starting at the top, first full sentence on the page, the inputs --

CHAIRMAN: Sorry, Mr. Hyslop. What page?
MR. HYSLOP: I'm sorry, Mr. Chair. Page 5.
Q.583 - And the part I'm referring to reads, The inputs examined were the generating, unit capacity, generating unit heat rates, generating unit outage rates, load, fuel prices, hydro production and export pricing representing the major drivers of the contracted electricity costs.
MR. PEACO: Yes.
Q.584 - Yes. And were these all of the factors of the many hundreds of inputs that you reviewed, Mr. Peaco?
MR. PEACO: There are other inputs into the model. But these are the major ones.
Q.585 - And these were the major ones that you reviewed?
MR. PEACO: That's correct.
Q.586 - Right. And did you do this for each and every generation unit? Or was it just on an aggregated basis?
MR. PEACO: Well, as I mentioned in the presentation last week, there are only a few units in the system. So we did review every unit.
Q.587 - Thank you. I take it if I was to ask you to list all the inputs you did not review that would be a pretty long list?
MR. PEACO: In terms of the individual data elements?
Q.588 - Yes.

MR. PEACO: Yes.
Q.589 - Thank you. And you would agree with me that any or all these individual inputs could have an impact on the budget and the pricing under the PPA?
MR. PEACO: In theory they could. Although in practice, based on the reviews we did, they would not be real consequential.
Q.590 - But you would agree that without a complete hard review of them, making that statement without some qualification would be perhaps too much?
MR. PEACO: Well, again within the context of seeking to determine whether the results were reasonable as opposed to whether they were precisely correct, that would be true.
Q.591 - What in general would be a reasonable -- zone of reasonableness for heat rates? Would it be within plus or minus 5 percent?
MR. PEACO: Well, we could. It would depend upon the unit, and the technology and the fuel.
Q.592 - Okay. And how much variation from historic review might be considered reasonable?
MR. PEACO: Well, again it depends upon the unit. If it's a cycling unit as operated, the resulting heat rates can vary some depending upon the capacity factor and the load

points.

Q.593 - Thank you. Would there be a zone of reasonableness for outage rates? And how much again would the variation from historic in your view be reasonable?

MR. PEACO: Well, what we looked at was the range of the experience that these units had had in their system and looked to see whether the data that was used in this run was consistent with the average of those, the operating history that they have had.

Q.594 - But you didn't look at the actual historic data yourself? You relied on the fact it was represented they were basing it on history?

MR. PEACO: In some cases we did have historic data --

Q.595 - Yes.

MR. PEACO: -- to look at. And I got to confess in phase 1 there were some -- some were historical records that we didn't have available to us that we looked at in subsequent phases.

So I'm not recalling exactly which of those was phase 1 and which was later. But there is historical data on many of the key variables here.

Q.596 - Okay. You can't recall whether outage rates was one of them or not that you examined?

MR. PEACO: In phase 1?

Q.597 - Yes.

MR. PEACO: I believe we did. But I would have to check.

Q.598 - Subject to check? Talk about NUGs, as hard as I work to get an answer on IR-115 in exhibit 54, I can't help but want to ask a question or two about it. With regard to the NUGs, I guess it has been explained that the Genco NUGs are taken on a must-take basis?

MR. KENNEDY: Yes, that is correct.

Q.599 - Right. And because of this, I do understand that in fact the normal economic dispatch that would normally result has been put out of sequence. Is that correct, Mr. Kennedy?

MR. KENNEDY: That's correct.

Q.600 - And if I were to refer you to exhibit A-95, and in particular page 15, do you have that, Mr. Kennedy?

MR. KENNEDY: Yes, I have that.

Q.601 - And either you or Mr. Peaco, who prepared this, can answer. But as I understand it, the column on the left-hand side of the page lists the different units of production on the basis of their dispatch taking into account the Genco NUGs as being a contractual obligation to take the electricity from. Is that correct?

MR. KENNEDY: That is correct.

Q.602 - And if we were to ignore the economic constraint of these contracts and just deal with it strictly from a matter of economics, would I be correct that the Genco NUGs would move from its position above Point Lepreau and would probably have itself sitting above the Coleson Cove section, Mr. Kennedy?

MR. KENNEDY: That would depend on the price of gas at the time, natural gas.

Q.603 - At least be sitting above the coal coke and orimulsion setting?

MR. KENNEDY: If they were dispatched, those were NUGs would be dispatched. Some of the NUGs are difficult to dispatch. Two in particular that are must-run are cogeneration arrangements.

Q.604 - Yes.

MR. KENNEDY: And the third one also is a contract that is for five months of the year, so there are seven months of the year that it is open to the market, that does not come in to the supply.

Q.605 - Sure. Now in IR-115, I -- after about three requests, I was able to get a calculation that said that because of these NUGs it cost $29,000,000 more for the -- than it would be through an economic dispatch but the answer was worked down to about 5,000,000 through a rather lengthy explanation.

My question, Mr. Peaco, is the actual difference in this cost, would that be something that would be able to be established through a PROMOD run?

MR. PEACO: Give me a second to look at the IR?

Q.606 - Yes. For the information of the Board, it is exhibit A-54 and it is exhibit PI IR-115.

MR. PEACO: This is background. Where in this IR are you referring to the --

Q.607 - Well it's not strictly a question of the IR, Mr. Peaco. What I am trying to determine is the effect of these NUGs being dispatched outside of their economic order because of contractual constraints. I am trying to determine if the cost of that could be determined through a PROMOD run?

MR. PEACO: This is purely a hypothetical question?

Q.608 - I appreciate it's purely a hypothetical question, yes.

MR. PEACO: And let me make sure if I understand. So your question would be if -- if these units could be purely economic dispatched and taken only when they are variable costs, their heat rate times the fuel price dictated to run in economic order?

Q.609 - Yes.

MR. PEACO: How could PROMOD determine how they would run?

Q.610 - Yes..

MR. PEACO: Yes, you can do that with a PROMOD run.
Q.611 - Yes. And could the savings from that economic run be calculated as opposed to what the cost is taking into account the fact that these are contracted supply of electricity?
MR. PEACO: You could take the cost difference between those two cases and determine the difference. And I mean savings would only be if in fact they could run in that mode.
Q.612 - Okay.
MR. PEACO: Yes. So I think your hypothetical perhaps postulates a mode that they may not be able to operate in.
Q.613 - And I guess my question then is has this type of a PROMOD run ever been done to determine the cost of the effect of these NUGs contracts one way or -- being used according to their contractual obligation or according to their economic reality, Mr. Kennedy?
MR. KENNEDY: 115, we made an attempt at it, but we did not change the marginal cost. We kept the same -- the marginal cost the same to be compared at it.
Q.614 - You didn't do a PROMOD run though to calculate the 5 million you came up with there?
MR. KENNEDY: Yes.
Q.615 - You did do a PROMOD run?

MR. KENNEDY: Not a full PROMOD run. We just did an off balance sheet there analysis of it.

Q.616 - An off balance sheet analysis of a PROMOD run?

MR. KENNEDY: A full PROMOD run would have resulted in a different -- different dispatch that would have reduced the export benefits. So there is a fixed component that would have had to have been dealt with. And I am not sure how that was dealt with in this analysis.

Q.617 - Well, I won't pursue it. I was thinking of asking you to do a PROMOD run on some assumption. But I will leave it at that.

Talked a little bit about your Operating Committee, went through who was on the Operating Committee. And I won't go through that again. But are the Disco reps or are any of the Disco reps that are on the Operating Committee also employees of Genco or any other corporation?

MR. MAROIS: No. No.

Q.618 - No. Have any of the Disco reps that have been on the Operating Committee been also employees of other corporations at one time?

MR. MAROIS: Well before restructuring it was one corporation.

Q.619 - After restructured?

MR. MAROIS: No.

Q.620 - And do the Disco reps have experience in PROMOD?

MR. MAROIS: Yes.

Q.621 - And how frequently has the Operating Committee met since restructuring?

MR. MAROIS: Officially 24 times.

Q.622 - 24 times?

MR. MAROIS: Officially. But I mean these types of discussions are occurring almost daily.

Q.623 - They are occurring daily. I take it then the people that work for Disco and work for Genco on the PROMOD are located within the same building?

MR. MAROIS: Yes, they are.

Q.624 - Right. On the same floor?

MR. MAROIS: No, they are not.

Q.625 - Not on the same floor. When you are saying they are meeting unofficially, what type of issues do they cover? Or are any minutes kept of these unofficial meetings?

MR. MAROIS: No, my point was that as issues come up, they are discussed. The official resolution of meetings are discussed at official Operating Committee meetings.

Q.626 - And I recall looking at the minutes. I think they were up to meeting number 10 for the minutes in exhibit 7. If there has been 24 official meetings would that mean that there would be more minutes available from those meetings as well?

MR. MAROIS: 24 meetings are the meetings of the Genco Operating Committee, and Coleson and the Nuclearco.

Q.627 - Okay.

MR. MAROIS: Those are separate committees. The same Disco representative, but different representative. So they are different committees.

Q.628 - Could you subject to check just confirm to me that all the minutes of all the meetings were in Appendix 7? You don't have to do it now, but just advise me of that effect?

MR. MAROIS: Yes, I will.

Q.629 - Does Disco receive independent outside advice in any way with regard to issues relating to the Operating Committee?

MR. MAROIS: Yes, we do.

Q.630 - Who did you hire as an independent adviser?

MR. MAROIS: We used Ernst & Young to perform an audit of -- really the calculation of the charges going to Disco. And that was last year. And this year we are going to use Ernst & Young again to expand on their last year's work.

Q.631 - Did they file a report regarding last year's work, Mr. Marois?

MR. MAROIS: Yes, they did.

Q.632 - Right. And they were retained solely by Disco for Disco's purposes?

MR. MAROIS: Yes.

Q.633 - And would you undertake to file a copy of the report that they gave you?

MR. MAROIS: Yes.

Q.634 - Thank you. Deal with Article 6.12 in the vesting agreement?

CHAIRMAN: What is the page reference on that, Mr. Hyslop?

MR. HYSLOP: I am just finding it. Page 51, Mr. Chair.

Q.635 - Do you have that? Now this deals with hydro flow. And this is an adjustment that's made at the end of the year to the pricing under the PPA?

MR. KENNEDY: Yes, it is.

Q.636 - Right. And it starts off with a definition of assumed hydro production, which is 2654 gigawatt hours?

MR. KENNEDY: Yes. 2654. And actually I should emphasize that a settlement is done on a monthly basis.

Q.637 - Yes. I was just going to get to that. Because after where it says, allocated to PROMOD in each month in a fiscal year, and that's the monthly assumed hydro production, is that correct?

MR. KENNEDY: The monthly -- actual as compared to the forecast with respect to the long range hydro.

Q.638 - Yes. And what I am looking at is the forecasted, you call that in the contract, the monthly assumed hydro production?

MR. KENNEDY: That is correct.

Q.639 - Right. I assume that the sum of the 12 months equals 2654?

MR. KENNEDY: That is correct.

Q.640 - Right. And Mr. Peaco, I take it, you would have reviewed those particular factors as part of your audit?

MR. PEACO: That's correct.

Q.641 - Right. But you didn't examine any of the history to determine the validity of the 2654 gigawatt or any of the monthly assumed hydro production factors?

MR. PEACO: Well, the monthly hydro production factors based upon long term historical averages are the monthly allegation.

Q.642 - Yes. I understand that.

MR. PEACO: I reviewed that.

Q.643 - And I understand from my exhibit 5 though, the hydro was some information that wasn't made available to you?

MR. PEACO: Yes. In the official phase, yes.

Q.644 - That's right. Thank you. And in that regard, I guess what I am getting to, the amount of the adjustment is the number -- the variance from the monthly assumed hydro production times, as I understand it, essentially what might be the marginal cost of a megawatt hour of electricity in that month, is that correct? The difference?

MR. KENNEDY: The difference is formulated by an additional megawatt hour on an incremental basis above the in-province load firm -- in-province firm load settled at that point on the dispatch by going back and using a settlement system that uses the actual load, compares it to the actual generation that occurred to serve that load at that time.

Q.645 - Now if you had more hydro in a particular month, I understand that Disco gets a credit equal to the incremental cost avoided by Genco as a result of the higher actual net energy production during that particular month?

MR. KENNEDY: Yes.

Q.646 - Right. And in theory, more hydro would move you further down on the dispatch order, would that normally be the case, Mr. Kennedy?

MR. KENNEDY: Normally, what would happen with -- if you had done the PROMOD run and you knew that there was going to be more hydro, it would have resulted in more hydro going into the base and it would have resulted in a lower fuel component cost and therefore a lower average vesting energy price.

Q.647 - Right. And therefore the incremental cost of the next megawatt hour saved is lower when the hydro is running than when it is not running?

MR. KENNEDY: I don't follow your question?

Q.648 - Well what I am getting at is if you have the hydro running above what's predicted, then would it be my -- would I be correct in my assumption that the incremental cost of the next megawatt hour saved would be lower than if hydro was not running?

MR. KENNEDY: The result would be that if there is more hydro running that when you are determining the vesting energy price, it would result in cheaper units being used to set the vesting energy price. So this is a margin that is used to settle the difference between a higher hydro flow versus a lower hydro flow. And if it is lower, then it would result in a different vesting energy price with respect to the fuel component. And if it is lower, it would result in a higher. So it's settled on the marginal cost just above the in-province load, firm load, that marginal cost, the cost of that on an average cost for the month.

Q.649 - Now, I guess what I am trying to drive at is a gigawatt hour extra that would be in Disco's favour have a lower incremental value than a gigawatt hour that is being a gigawatt hour short, which would not act in the best interest of Disco? In other words, is the price difference if you are having too much hydro as opposed too little hydro, or is it the same price?
MR. KENNEDY: It's basically the same price. It can go either way at that particular point.
Q.650 - But is it the same price -- would it not be a higher price when the -- would not the incremental price be higher when there is a shortage of hydro than when there is a surplus of hydro -- the incremental price?
MR. KENNEDY: Yes. If there is an incremental price, it would be -- if there is less hydro, there would be higher incremental cost.
Q.651 - Yes. Okay. Just looking at exhibit A-96 if you would, Mr. Kennedy.
MR. MAROIS; Which schedule?
MR. HYSLOP: A-96.
Q.652 - It's the number of the purchase -- power purchase cost variance analysis that was done by Mr. Kennedy and presented in his direct evidence.
Now, I was wondering, Mr. Kennedy, there is nothing in

here, of course, about the hydro in regard to the purchase power budget, is that correct?

MR. KENNEDY: That's correct.

Q.653 - Right. Because it's something you calculate after the fact?

MR. KENNEDY: Yes. It's settled after the fact.

Q.654 - Right. I was wondering for actual 2005/2006 would you be good enough to show me the month-to-month settlements both in terms of the number of gigawatt hours and the financial settlement between Disco and Genco?

MR. KENNEDY: We had an undertaking where we were going to look at the actual for 05/06 budget.

Q.655 - Could you do that on a month-to-month basis for me?

MR. KENNEDY: I believe there is an IR on that with respect to on a month-by-month basis with respect to hydro adjustment.

Q.656 - Okay. I am not aware of it. If you can point me in the right direction, I won't ask you to if you could prepare it obviously, and I will take that subject to check.

MR. KENNEDY: Yes.

MR. HYSLOP: Mr. Chair, I have got about three to four more lines of questioning. I think it would take about an hour in the morning to finish it off. Do you want me to continue for the last five minutes? My voice has just about had it.

CHAIRMAN: No, we will save your voice till tomorrow. Don't speak to him, Mr. O'Rourke. We will reconvene tomorrow morning at 9:15.

(Adjourned)

Certified to be a true transcript of the hearing, as recorded by me, to the best of my ability.

Reporter