

DECISION

NSUARB-P-887
2007 NSUARB 174

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE PUBLIC UTILITIES ACT

- and -

IN THE MATTER OF a hearing to determine whether or not it is appropriate to adopt a Fuel Adjustment Mechanism (FAM) for **Nova Scotia Power Incorporated**

BEFORE:

Peter W. Gurnham, Q.C., Chair
Margaret A. M. Shears, Vice-chair
Kulvinder S. Dhillon, P. Eng., Member

COUNSEL:

NOVA SCOTIA POWER INCORPORATED

René Gallant, LL.B.
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Anne-Marie Curtis
Carla Rowlings
Paul Casey

AVON VALLEY *et al.*

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Mark Freeman, LL.B.

CANADIAN MANUFACTURERS & EXPORTERS

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CONSUMER ADVOCATE

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HALIFAX REGIONAL MUNICIPALITY

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**MUNICIPAL ELECTRIC UTILITIES
OF NOVA SCOTIA CO-OPERATIVE**

Don Regan

**PROVINCE OF NOVA SCOTIA
(Department of Energy)**

James Gogan

Scott McCoombs

Richard N. Penny

**STORA ENSO PORT HAWKESBURY LIMITED and
BOWATER MERSEY PAPER COMPANY LIMITED**

George T. H. Cooper, Q.C.

David S. MacDougall, LL.B.

James MacDuff, LL.B.

HEARING DATES: November 5 & 6, 2007

FINAL ORAL SUBMISSIONS: November 13, 2007

LIST OF INTERVENORS: APPENDIX A

BOARD COUNSEL: S. Bruce Outhouse, Q.C.
Richard Melanson, LL.B.

DECISION DATE: **December 10, 2007**

DECISION: **Conditional approval; implementation date of
January 1, 2009, subject to all conditions being
successfully met.**

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I INTRODUCTION

[1] This decision is further to a public hearing conducted by the Nova Scotia Utility and Review Board (the "Board") on November 5 and 6, 2007, with final oral submissions on November 13, 2007, to determine whether or not it is appropriate to adopt a Fuel Adjustment Mechanism ("FAM") for Nova Scotia Power Incorporated ("NSPI").

[2] The List of Intervenors in the proceeding is attached as Appendix A. The Board has conditionally approved the application for a FAM to be implemented on January 1, 2009, subject to all conditions and prerequisites being successfully met.

II BACKGROUND AND POSITIONS OF THE PARTIES

1. What is a FAM

[3] A FAM is generally defined as a mechanism that allows periodic adjustments to customer rates, outside general rate proceedings, to reflect increases and decreases in the utility's fuel costs provided they are prudently incurred.

[4] These adjustments can be made at any interval set by the Board, but usually are set on a monthly, quarterly, bi-annual or annual basis. The design of the FAM includes the frequency and degree of adjustments.

[5] A FAM appears to have the following benefits:

1. Provides customers with timely price signals to reflect actual and prudent fuel costs.
2. Encourages timely conservation by customers.

3. Customers receive timely benefit of lower fuel costs.
4. Shorter (and, depending on circumstances, possibly fewer) general rate hearings resulting in time and cost savings which are ultimately passed on to customers.
5. Reduces risk to utility resulting in customer benefits with lower cost of capital.

[6] The following are some of the weaknesses in a FAM if not addressed in the design and implementation:

1. Reduces utility's incentive to pursue effective and efficient use of assets to minimize fuel costs.
2. The Utility may make inefficient investments which are biased towards lower capital and maintenance costs and higher fuel costs.
3. The Utility may earn excess return on investment by passing increases in energy costs and not passing savings in other areas of the utility to its customers.
4. May increase regulatory costs due to additional monitoring and auditing.
5. Frequent rate changes may lower the customers' understanding of such changes and, as a result, the potential savings which could be achieved from conservation.

2. The Process to the Hearing

[7] At the beginning of the hearing on the 2007 NSPI general rate application, NSPI filed a settlement agreement which was endorsed by most of the formal Intervenors, including the Consumer Advocate (the "CA"). The Board approved the settlement agreement in its March 8, 2007 Amended Order.

[8] For purposes of this decision, the most relevant clause of the 2007 rate case settlement agreement is number 4:

4. All parties agree in principle that the UARB should adopt a Fuel Adjustment Mechanism ("FAM"). The parties request the UARB to establish a process that commences as soon as possible to establish a FAM. The parties will work constructively on the content or elements of a FAM. A FAM hearing will begin no later than July 15, 2007.

[9] In its February 5, 2007 Decision for the 2007 NSPI general rate case, the Board provided the following comments on what it had, and had not, agreed to with respect to a FAM in accepting the rate case settlement agreement:

[44] The Board recognizes, as was noted in the 2005 decision, that FAM's exist in many other jurisdictions and operate satisfactorily. The Board has agreed to accept the Settlement Agreement and therefore has agreed to establish a process leading to a hearing to determine whether or not it is appropriate to adopt a FAM for NSPI. The Board wishes to make it clear that what it has agreed to do is establish a process and conduct a hearing: it has not agreed to implement a FAM. A decision on that point will, of course, be made at the conclusion of the process described in this decision.

[45] For the guidance of the parties, however, and without in any way prejudging the issue, in the Board's view there are several prerequisites that must be in place in order for the Board to consider the adoption of a FAM now or in the future:

1. an adequate and appropriate fuel procurement policy at NSPI in which the Board has confidence;
2. timely disclosure of complete and adequate information by NSPI so as to ensure confidence that the procurement policy is being appropriately administered;
3. disclosure and transparency with respect to the administration of the FAM;
4. a meaningful audit process under the administration of the Board.

[46] This list is not meant to be exhaustive.

[Board Decision, 2007 NSUARB 8, pp. 22-23]

[10] The Board's Decision included a timeline from the Decision date to the start of a FAM hearing in June 2007, which was subsequently extended at the request of the parties until November of 2007. The Board directed that the pre-hearing process be chaired by Dr. John Stutz ("Dr. Stutz"), assisted as needed by The Liberty Consulting Group ("Liberty"), Board Counsel consultants and Board Staff.

[11] Dr. Stutz, in his opening statement of November 1, 2007, provided a summary of the process followed since the Board's February 5, 2007 Decision to the November 5, 2007 start of the FAM hearing.

In its decision in the last General Rate Proceeding the UARB established a process, leading to a hearing to determine whether or not it would be appropriate to adopt a Fuel Adjustment Mechanism (FAM) for NSPI. Consistent with that process, there were three workshops which addressed FAM design and FAM-related issues including the Prerequisites stated in the UARB Decision. After the workshops there remained substantial differences among the parties. The Board's process led to a hearing starting on June 18. At the request of NSPI the timeline was extended and the hearing rescheduled to start November 5.

In the letter granting the extension I was asked by the Board to help facilitate constructive dialogue. As a first step in that process I spoke to a number of the parties participating in the FAM proceeding. My goal in these conversations was to gain insight into each party's issues and concerns. These conversations indicated that the differences could be approached most productively in a small group setting. A small group consisting of representatives of SEB, Other Large Customers (Grant & Rubin), HRM, the Consumer Advocate, and EAC took part in a conference call on July 11 and two meetings in Halifax held on August 30 and October 12. Much of the group's effort focused on the exploration of possibilities for settlement.

A meeting open to all participants in the FAM process was held on October 17, 2007. NSPI began that meeting with an update of their anticipated fuel and purchased power (F&PP) costs for 2008. The point of departure for NSPI's presentation was the 2007 Compliance (2007C) Filing. NSPI discussed the effects of a wide range of factors-lower net generation, a stronger Canadian dollar, higher prices for oil, and a host of others. The largest single effect was a \$26 million reduction in gas margins, due to lower gas prices and greater use of gas for generation. Net of the \$8 million deferral of gas margin revenue permitted by the Board's letter of July 23, the Company anticipated a 2008 cost of \$471 million, essentially the same as the \$470 million which the 2007C rates, which remain in effect for 2008, were designed to recover.

[Exhibit N-33, p.1]

3. The Framework Agreement

[12] At the commencement of the hearing NSPI filed a Framework Agreement ("Framework") for the proposed FAM which was signed by certain of the Intervenors.

[13] The Framework reads as follows:

Framework for the FAM

November 3, 2007

- **Setting Fuel Costs included in Base Rates** Absent a General Rate Proceeding prior to the implementation of the FAM, Base Cost of Fuel for 2009 and 2010 will be set initially on a \$/MWh basis at the 2007 Compliance level. The Base Cost of Fuel will be set by dividing

- a) Allowable Fuel plus Purchase Power costs, net of Off-System sales revenues, less GRLF revenues (excluding the administrative margin), by

- b) General System Requirements, less the energy requirements of all sales that are not subject to the FAM.

The figures in a) and b) will be as established in the most recent compliance filing, unless superceded and approved by the reset provision. The Base Cost of Fuel will be set to ensure that export (off-system) sales revenue are not double counted.

In subsequent years, a forecast of costs for a representative test year will be used to set the Base Cost of Fuel. The Base Cost of Fuel can be re-set in a General Rate Application or every second year as part of the FAM adjustment process (i.e., absent a General Rate Application, the Base Cost of Fuel will remain in place for a minimum of two years). The change in the Base Cost of Fuel will be reflected in customers' rates going forward and will be applied to each customer class in a manner consistent with the then-current Board-approved Cost of Service Methodology, Cost of Service Study and the application thereof, including the revenue and cost allocations thereunder. Parties will work together during 2008 to establish a standard methodology for NSPI fuel forecasts, to be presented to the Board for approval and incorporation into the FAM process. Stakeholders will be provided the opportunity (and access to information) to challenge the implementation of the methodology and the contents of any forecast prior to its use in re-setting the Base Cost of Fuel. Both the implementation of the methodology and the forecasts will be the subject of a formal Board proceeding in which stakeholders will have their current rights as in general rate cases.

- **Includable Fuel Costs** For purposes of the FAM, fuel costs will be as per section 2.1.4 of NSPI's Direct Evidence (April 30, 2007).

- **FAM Adjustment Calculation** Subject to the incentive (below), the FAM will recover fuel cost changes resulting from over/under-recovery amounts, including an Actual Adjustment and a Balancing Adjustment. The FAM Adjustment would apply to the difference between actual fuel costs and those in Base Rates and will be calculated on a dollar (\$) per MWh basis. The FAM adjustment will be consistent with how loss factors for each customer class are calculated in the Company's Cost of Service Study.

- **Incentive** The FAM would pass though only a portion of the actual versus forecast fuel cost difference to customers calculated on a \$ per MWh basis. For variances up to \$50 million on a \$ per MWh basis, 90% of any savings or increase would be passed from NSPI to customers. In other words, NSPI would remain responsible for 10% of the increase or keep 10% of the fuel savings. The portion of any variance that is in excess of \$50 million will be passed on to customers. Thus, the total maximum effect of the incentive in any given year would be \$5 million. Interest would be added to all over-/under-collection amounts and calculated at the rate in use for AFUDC.

- **Reporting, Transparency, Hearings, and Audits** The period for the true-up of actual versus forecast fuel cost would be annual. During 2008, FAM-related consultation would take place regarding FAM auditing processes and to develop standard filing templates for the monthly and annual information reports that NSPI will file with the Board and stakeholders. The formal timetable for stakeholder review and discovery would be developed along the timelines in Liberty's design evidence. Stakeholders would be entitled to challenge NSPI's fuel costs (and be provided access to information) at each annual hearing before the Board consistent with their current rights in general rate cases. The NSUARB would subject NSPI's FAM accounts to audits as required by the Board.
- **ROE adjustment** Coincident with the FAM implementation on January 1, 2009, NSPI's allowed Return on Equity (ROE) would be reduced by 0.2%, and its allowed earnings band would be reduced accordingly (9.1% to 9.6%, rates set at 9.35%). Over-/under-recovery of Fuel Costs due to the operation of the FAM incentive would be excluded when considering whether NSPI's return lies within the earnings band. The 0.2% adjustment would be made without any admission by either NSPI or stakeholders that this is the appropriate adjustment, and no parties (including NSPI) would seek any change, introduce any ROE evidence or support any change to ROE for a minimum of two years following the initiation of the FAM. After December 31, 2008 and until a General Rate Application to incorporate this change into rates, earnings equal to the value of 0.2% of the Company's equity will be returned to customers by incorporation into each yearly FAM adjustment.
- **Support for the Proposal before the UARB** Parties that support this proposal will cease adversarial litigation *inter se* in the FAM matter for the November 2007 hearing and, before the Board and otherwise, will support the implementation of the FAM as proposed on January 1, 2009. Parties will participate constructively in the development and preparation for implementation of the FAM during 2008.
- **Significant FAM Changes** Where, in the absence of a General Rate Application, an increase for any customer class of more than 10% compared with the rate payable in the prior year is caused by the application of the FAM procedures, the parties agree that the Board should consider appropriate measures to assist customers, such as whether part of the increase should be deferred for collection with interest.
- **Parties to the agreement** Support for the agreement and all of its provisions will be binding on the parties who agree, and their successors and assigns.

[Exhibit N-51]

[14] The Framework has the support of Nova Scotia Power Inc. ("NSPI"), Stora Enso Port Hawkesbury Limited and Bowater Mersey Paper Company Ltd. ("SEB"), Avon Valley *et al.* ("Avon"), Municipal Electric Utilities of Nova Scotia Co-operative ("MEUNSC") and Canadian Manufacturers and Exporters ("CME").

[15] The Intervenors which do not support the Framework are: Ecology Action Centre ("EAC"), the CA, Halifax Regional Municipality ("HRM") and Nova Scotia Department of Energy ("NSDOE"). The Board understands that these parties were participants in the meetings and discussions between NSPI and those stakeholders who support the Framework. The New Democratic Party of Nova Scotia ("NDP") opposes the Framework and provided reasons in its closing submission.

[16] NSPI, in presenting the Framework to the Board, stated that:

The Settlement required give and take on all sides. NSPI asks the Board to respect that the Settlement has an appropriate balance of competing interests and urges the Board to conclude that it is in the public interest. The Company respectfully requests the Board resist suggestions that this consensus agreement be altered. In respect of the concerns of the Consumer Advocate specifically, the Company respectfully suggests that most of his concerns have been addressed by this Framework, and remaining concerns can be addressed by the work that will be done in the coming months. The processes and agreements achieved in 2007 should demonstrate the willingness of the Company and customers to find reasonable solutions to substantive concerns.

[Exhibit N-44, p. 3]

[17] NSPI, in its closing submission, requested that the Board:

- Approve the Settlement Agreement (the "Framework for the FAM"), as being in the public interest;
- Confirm that the FAM will go into effect on January 1, 2009; and
- Direct and oversee a process for implementation of the FAM.

We ask the Board to state unequivocally that the FAM will begin to operate on January 1, 2009. ...

[NSPI's Closing Submission, p. 1]

[18] SEB, in support of the approval of the Framework, stated in its closing submission:

Due to the various built-in customer protections in the Settlement proposal, SEB believes the proposal is in the public interest and should be adopted by the Board.

...

Further, from the customers' perspective, the Settlement specifically provides that customers will maintain the same rights that they have today to challenge NSPI's fuel forecast each year, as well as its annual procurement decisions. Again, this will be within the context of a formal Board process in which the Board will be the final arbiter.

[SEB's Closing Submission, pp. 1-2]

[19] Avon in its closing submission stated that:

We believe that the FAM Framework which has been placed before the Board, and which we have signed on behalf of our clients serves the Board and stakeholders well as the foundation for a well-designed and transparent FAM. The Framework sets the stage for a change in the regulatory environment in Nova Scotia permitting NSPI partially to flow through changes in its fuel costs to its customers without a full rate case. It also contains some important safeguards for NSPI's customers.

[Avon's Closing Submission, p. 1]

[20] CME, in support of the Framework, recommended changes to the process in the development of the FAM.

The CME was not a participant in the smaller group that initially explored the possibility of development of consensus of a FAM. It recognizes the desire for efficiency by having a smaller working group but it was nonetheless disappointed it was not included. In large part, we were able to move quickly as negotiations at the 11th hour occurred because of the close working relationship with the other signatories throughout the process. For the development of the FAM, it is recommended that no one be excluded, should it be their desire to participate, subject to the normal requirements of confidentiality, etc. Perhaps parties will divide into working groups as agreed to by them with reporting back to the larger committee. All of this can be discussed and agreed to shortly.

...

In conclusion, the CME supports the concept of a FAM, confirms its acceptance of the agreement to which it was a signatory but acknowledges that if approval is given to proceed much work is required to be ready for 2009 and it is willing to participate and cooperate in achieving what is best for all Nova Scotians.

[CME's Closing Submission, pp. 2-3]

[21] MEUNSC supports the Framework, but indicated that it has concerns with respect to affiliate transactions as well as questions regarding the process by which municipal utilities can incorporate FAM adjustments into their customer rates.

[22] The CA did not sign the Framework and is opposed to NSPI's requested "unequivocal" approval of the FAM implementation date of January 1, 2009, stating that:

. . . our position is based on two fundamental points. First, there is still a need for Nova Scotia Power to demonstrate that there will in fact be appropriate disclosure. And disclosure, to us, is a fundamental prerequisite. Secondly, quite simply, the FAM still needs designing, and it's premature to ask this Board to approve the implementation of a FAM of which the features have yet to be determined. What this board should do as a result of the hearing that's taken place is determine what more needs to be done to continue our journey down the road to a FAM, set the time frames for that, and possibly, depending on your discretion, determine certain characteristics or your preference for certain characteristics as to what a FAM might contain. . .

[Transcript, November 13, 2007, pp. 83-84]

[23] The CA also noted its concern with respect to disclosure of information by NSPI:

. . . For us, disclosure of information relating to costs is the most important issue in a FAM. We can debate whether incentive mechanisms should be built in or not and we can debate what the return on equity figures should be, but ultimately the impact of those discussions would be minimal compared to the difficulties that we would encounter if there is a problem with information disclosure. And I don't want to sound pessimistic in a day when everybody is expressing cooperation and commitments to work together, but there have been concerns. . . .

[Transcript, November 13, 2007, p. 89]

[24] The CA initially supported the incentive provision in the design of the FAM, but based on the evidence provided in the hearing, now recommends that, should the FAM be approved, this issue be monitored by the Board to ensure that the incentive provision is achieving its intended purpose. The CA is also opposed to the provision in the Framework which provides that the current return on equity ("ROE") would not be subject to a request by the parties for a review for 2 years following the implementation of the FAM.

[25] HRM's position is generally the same as that of the CA and it opposes the approval of the FAM at this time. HRM believes that dialogue between the parties should continue until all parties are satisfied with the reporting protocol prior to approving the FAM.

[26] NSDOE stated that the implementation of a FAM is a "significant matter of public policy" and "would mark a significant departure from the current rate setting mechanism in Nova Scotia"¹ and provided comments on four specific issues for the Board's consideration.

[27] The first issue is the level of oversight by the Board if the FAM is approved. NSDOE recommends that a trial run should be conducted in 2008 before final approval of the FAM, during which time the Board will monitor the FAM reporting process. The NSDOE believes that if NSPI successfully "passes these tests", public confidence in the FAM process would be enhanced.

[28] The second issue is that of compliance with the Board's four prerequisites as outlined in the Board's 2007 NSPI Rate Decision, which is discussed in greater detail later on in this Decision.

[29] The third issue is cost shifting between rate classes. NSDOE is of the opinion that the calculations of fuel cost for FAM includes credits and debits for NSPI's avoided and incremental costs for Extra Large Industrial Two Part Real Time Price Rate (ELI 2P-RTP) and has the potential of cost shifting between rate classes.

¹ NSDOE Final Submission, p.2

[30] NSDOE's last concern relates to the provision in the Framework which sets out the level of rate increases the signatories agreed could occur prior to the Board's intervention. NSDOE's submission states:

The framework for the FAM (Exhibit N-45), at Page 2, contemplates scenarios where the operation of the FAM would result in significant rate changes:

"Significant FAM Changes

Where, in the absence of a General Rate Application, an increase for any customer class of more than ten percent (10%) compared with the rate payable in the prior year as caused by the application of the FAM procedures, the parties agree that the Board should consider appropriate measures to assist customers, such as whether part of the increase should be deferred for collection, within [sic] interest."

It is the respectful opinion of NSDOE that such general considerations are insufficient. The potential for the introduction of a FAM in the rate setting process in Nova Scotia is a significant policy shift in the establishment of electricity rates in this Province. In order that public confidence be maintained, NSDOE believes that imbedded trigger points must exist within the FAM. These triggers, if met, would, for example, result in the triggering of a General Rate Case proceeding. These triggers, NSDOE believes, should be tied to rate fluctuations within rate classes caused by the operation of the FAM. For example, where a rate increase in a particular customer class over the previous year exceeds a fixed percentage, or the rolling aggregate three year increase for a particular class exceeds a fixed percentage, a General Rate Case would be convened.

NSDOE believes that by establishing such automatic triggers, electricity customers would have enhanced confidence and comfort with the operation of the FAM on the understanding that where rates materially increased, the full oversight function of this Board would be brought to bear through a Rate Case proceeding.

NSDOE believes that the determination of the appropriate trigger points is best left to this Board to determine after having heard input on this matter from the proposed FAM Stakeholder Working Group.

[NSDOE Closing Submission, p. 8]

[31] The NDP did not participate at the hearing, but provided a written closing submission indicating that the proposed FAM is not in the best interest of the ratepayers at this time. The NDP based its position on the understanding that NSPI's ability to

effectively manage the risk associated with fuel costs has not yet been proven, and that a FAM would, therefore, transfer that risk to customers without any corresponding benefit.

[32] Dr. Stutz recommended acceptance of the Framework, subject to a trial run, including establishing standard reporting templates and modeling processes to assist all parties to review NSPI's fuel costs in a timely and effective manner. In response to a question from the Chair, Dr. Stutz stated:

Certainly, I know, from my participation in the process, that this notion of trial run had been discussed earlier, so I don't see it as inconsistent with what's written here. I would think it would be a helpful elaboration of the settlement if the Board would indicate that it wanted to see a trial run along the lines that were discussed today. I take it from what I heard today that there would be no one who would be opposed to a trial run. So if the Board could make it clear that the Board also wanted a trial run, then if it wasn't going to be possible to begin the trial run with respect to the use of the reporting templates by, let's say, the end of the first quarter, the Board should be informed that would lead to a more orderly process. It would in no way be inconsistent with what's here, just they didn't get that particular detail in here. But adding it wouldn't change what they've given you, I don't think...

[Transcript, November 6, 2007, pp. 227-228]

[33] Liberty made the following recommendations in its opening statement:

We recommended in our May 24, 2007 supplementary evidence that the Board not adopt a FAM at this time because, as we said, "The gaps between what those prerequisites entail and what current circumstances indicate are too wide, in our opinion, to justify serious consideration of a FAM until NSPI has taken satisfactory steps to narrow or eliminate those gaps." We are still not persuaded that a FAM can work effectively with a company with characteristics like those that NSPI has shown across the time we have been working in Nova Scotia.

We believe, however, that the use of 2008 as a trial period, during which commitments to: (a) timely data provision and regular reporting and (b) arm's-length dealing with affiliates can be demonstrated (or not) to exist at levels that make a FAM appropriate. That demonstration should occur through (a) collaboratively-developed data provision and reporting activities and formats, and (b) completion of efforts to meet the affiliate transaction recommendations described above.

[Exhibit N-34, p. 3]

[34] In response to a question from the Board, Liberty explained the process and timelines which in their view should be followed during the trial period for the FAM:

A. (Antonuk) Yes. Yes. And I think the way that part works is there should be a design of the forms, you know, the actual tables that will have the columns and the rows identified, and then that would be circulated among the stakeholders and they should all be expected to respond, I think, fairly promptly to that. And then the goal would be to have NSPI begin reporting, at the end of the first quarter of calendar '08, information that fills out all those cells in the reports so that parties would have a couple of reports to get comfortable that what they're seeing is what they expected, and also to establish a track record so that once we agree to it there should now be no more debate, when 1009 [sic] comes, about what's to be provided. On the forecast side, I think the company needs to convene a workshop that basically walks people through how their modeling works, what takes time to model, because it's actually a collection -- think about it as a collection of models with some manual inputs added at the end for things that can't effectively be modeled on an automated basis. The company should explain that process. The company should work towards identifying ways they can shorten the time frame. I believe we said in our testimony or in response to a data request that one week is optimum, two weeks is about the edge of what we think is acceptable for a turnaround time on models. My understanding from discussions with Mr. Janega is that there -- it's going to be hard right now to do that 2-week turnaround time but the company can make improvements that will get them much closer to that and maybe even within it if they are allowed to make some runs that are in a sense abbreviated so that you don't have to run all parts of the model to answer maybe a question about a change in only one variable. The goal there to me is within the first, say, two to three months of '08 there's pretty much a general agreement on what the company can do now model-wise and what it needs to be able to do by, say, the June time frame I'm talking about. So, that's the way I see the modeling part of it going. The other part of it, I think, is that the -- we've mentioned we see progress in the gas solicitations. We now have an agreement to provide affiliate transaction data. We don't have the data yet. So, my expectation is in that same time frame we'd work through the remaining questions about that whole issue, the whole issue of gas solicitation. Then the fourth issue is basically the -- what do we want to call them? -- the recommendations that we have outstanding that we think the company has probably already addressed but we don't have confirmation, and that's going to be the things that were addressed with the NSPI panel today. There's some risk management, some hedging, and some credit issues. What I heard today suggests to me that there may be no difference at all between us and the company on those. We need to see that. We need to see the documentation that establishes that. And it sounds to me like the company in some cases has those things already done in their opinion and in other cases they understand they have to do them. So, we need to turn that all into what I would still call the "show me" part. And then I think where we are by mid-June is either we all -- all the stakeholders are pretty much in agreement that everything looks -- the package looks good, the data is all there, there's agreement on turnaround times, all those things, in which case I would assume there is some sort of a presentation to you that says from the perspective of the stakeholders that it's a green light. And if there's not, then it seems to me -- I've heard some stakeholders at least imply through questioning -- and I would certainly agree -- if there's disagreement, there needs to be some way for you all to resolve that disagreement, hopefully from my perspective by sometime around September, so that, you know, in the last three months of the year we're all sort of preparing to make the FAM work and still not arguing about how it's going to work or what details and what software it needs to work. So, that's my general picture of how it should go. And I want to emphasize a point that's very, very important to me here, which is -- some parties have settled, some parties have not -- I think it should be

very clearly understood that, settle or not, every stakeholder has got a seat at the table and has an equal opportunity to be heard, because this FAM is going to be about everybody, not just the parties who have signed it, and some of the parties who haven't signed it are very important parties. So, I think care needs to be taken to make sure that those folks don't somehow end up on the periphery of all this, this implementation part.

[Transcript, November 6, 2007, pp. 187-191]

III THE BOARD'S FOUR PREREQUISITES

[35] In its decision dated February 5, 2007, NSPI P-886, 2007 NSUARB 8, the Board stated the following:

[45] For the guidance of the parties, however, and without in any way prejudging the issue, in the Board's view there are several prerequisites that must be in place in order for the Board to consider the adoption of a FAM now or in the future:

1. an adequate and appropriate fuel procurement policy at NSPI in which the Board has confidence;
2. timely disclosure of complete and adequate information by NSPI so as to ensure confidence that the procurement policy is being appropriately administered;
3. disclosure and transparency with respect to the administration of the FAM;
4. a meaningful audit process under the administration of the Board.

[46] This list is not meant to be exhaustive.

[36] In this section the Board will comment briefly on each of the prerequisites:

(1) Fuel Procurement Policy

[37] NSPI's fuel procurement policy has been the subject of much discussion and review spanning the last several rate proceedings. Essential to the Board's ongoing review has been the advice and comments received from Liberty and interested parties. In its Supplementary Evidence, Liberty opines on the state of the fuel procurement policy.

Q. ARE YOU NOW PREPARED TO OFFER A CONCLUSION WITH RESPECT TO THE NSUARB'S FIRST FAM PREREQUISITE, WHICH ADDRESSES THE ADOPTION OF AN ADEQUATE AND APPROPRIATE PROCUREMENT POLICY?

A. Yes. We believe that, with the exception of energy transactions with affiliates, NSPI has adopted an adequate, appropriate fuel procurement policy in which the Board can have confidence. This conclusion assumes that NSPI addresses the cited recommendations from the affiliate audit, and agrees to make moderate corrections to the documents governing hedging and risk management.

[Exhibit N-6, p. 12]

[38] The Board assumes that the parties to the Framework agree that NSPI's current fuel procurement policy is adequate for a FAM. While the CA, HRM and NSDOE express concern about unequivocally adopting a FAM, none of those parties raise serious concerns about Prerequisite #1, except as it relates to affiliate transactions. Indeed, HRM describes the fuel procurement policy favourably.

[39] The two areas of continuing concern expressed by Liberty are affiliate transactions and hedging and risk management. NSPI states that hedging and risk management issues have been addressed, albeit not yet reviewed by Liberty. The Board expects any outstanding concerns will be resolved.

[40] Affiliate transactions, on the other hand, have been a difficult and contentious issue beginning with a proposal several years ago to assign to an affiliate NSPI's gas supply contract. Most recently Liberty highlighted a series of transactions of concern in its Affiliate Audit. Relevant to this proceeding are transactions related to natural gas.

[41] The relationship between NSPI and its affiliates is a legitimate concern of various parties, Board staff and consultants. Further direction with respect to review of the Affiliate Audit will follow the release of this decision.

[42] However, for purposes of the FAM, Board Counsel and NSPI have entered into an arrangement which will allow affiliate transactions to occur and to be adequately monitored. Exhibit N-47 outlines that arrangement:

It is our understanding that under a FAM, NSPI may enter into transactions for natural gas or energy, including financial transactions (swing swaps) with an affiliate when the following conditions are met:

1. That affiliate must disclose to the UARB's auditor, in respect of transactions in Atlantic Canada (for gas, Maritimes and Northeast Pipeline) and New England (for gas, Maritimes and Northeast Pipeline - US) all information not subject to confidentiality provisions or for which confidentiality protection has been waived by counterparties of the affiliate. This includes individual transactions that have taken place more than 12 months prior to the disclosure request; and
2. That affiliate must use good faith efforts to obtain counterparties agreement to include consent to disclosure to the UARB and its auditors in future master trading agreements, and, subject to 4 below, the affiliate must not renew master trading agreements or enter into master trading agreements with new counterparties that do not contain such consent to disclosure; and
3. That existing counterparties that have not consented to disclosure will be "grandfathered", and the affiliate must direct its external auditor to review the confidential information and respond to specific questions from the UARB, or its auditor, on the condition that the external auditor would not be required to release confidential information; and
4. That the affiliate will be allowed sufficient time following a request to produce the necessary information, and may object to requests it considers unreasonable due to volume, cost, response time or otherwise. If any such objection remains unresolved, the affiliate, NSPI or Board Counsel may apply to the Board for direction in relation to same. All information provided by the affiliate will be subject to a confidentiality agreement; and
5. That NSPI may seek direction from the UARB about any aspect of these conditions, or future audits or any aspect thereof.

This confirms that NSPI, under a FAM, will operate in accordance with these conditions in respect of gas or energy transactions with affiliates in future.

[43] As it relates to fuel, the principal concerns outstanding were the management and resale of NSPI's gas portfolio. Liberty spoke favourably with respect to NSPI's most recent gas transactions.²

[44] The Board is prepared to accept for purposes of a FAM that Prerequisite #1, an adequate and appropriate fuel procurement policy, has been met.

**(2) Disclosure Related to Fuel Procurement and
(3) Disclosure and Transparency Related to the Administration of the FAM**

[45] The Framework states in part as follows:

Parties will work together during 2008 to establish a standard methodology for NSPI fuel forecasts, to be presented to the Board for approval and incorporation into the FAM process.

...

During 2008 FAM-related consultation would take place regarding FAM auditing processes and to develop standard filing templates for the monthly and annual information reports that NSPI will file with the Board and stakeholders.

[46] NSPI has agreed to file monthly and annual information in accordance with the recommendations of Liberty in its April 30, 2007 evidence³, and its evidence dated June 11, 2007.⁴ In a subsequent portion of this decision the Board sets out the timeline for resolving those issues.

[47] With respect to disclosure and transparency, Mr. Tedesco stated as follows:

² Transcript, November 6, 2007, p. 209

³ Exhibit N-2

⁴ Exhibit N-25

50. Q. Are you at least prepared to commit to providing full evidence, full factual access and review to determine all relevant factors that went into the company's fuel procurement decisions?

A. (Tedesco) That we will absolutely do. I think that's an important part of a FAM.

51. Q. So that as we go into 2008 and we begin to design what the specifics will be of the reporting mechanisms, the audit mechanisms, the hearing mechanisms, the company's stated position is that all relevant information is accessible?

A. (Tedesco) I think that's what we've said, yes, subject, of course, to confidentiality provisions in some of the contracts with parties who may be conflicted and that sort of thing, which is the normal procedure. But absolutely, I mean, to someone -- certainly to the consumer advocate that information will be available and to most parties that information will be available.

[Transcript, November 6, 2007, pp. 27-28]

[48] Other company representatives agreed and proper disclosure is clearly a theme of NSPI's final submission.

[49] By virtue of the nature of the Framework more work remains to be done before Prerequisites 2 and 3 can be satisfied. The Board however interprets Mr. Tedesco's statements and the submissions of NSPI to be an unequivocal undertaking that there will be:

- timely disclosure of complete and adequate information by NSPI so as to ensure confidence that the procurement policy is being appropriately administered;
- disclosure and transparency with respect to the administration of the FAM.

[50] The Board is satisfied that there is sufficient progress on Prerequisites 2 and 3 to allow the FAM process to continue. Future monitoring by the Board as part of the conditions outlined later in this decision will occur.

(4) Auditing Process Under a FAM

[51] Again, details of this are to be worked out pursuant to the terms of the Framework and included in the FAM tariff to be approved by the Board. However, the Board wishes to make it clear that there will not be final approval of the FAM until "a meaningful audit process under the administration of the Board"⁵ is in place.

IV CONTEXT OF DISCLOSURE CONCERNS

[52] The Board wishes to make some further general observations with respect to disclosure.

[53] In the Board's view, the provision of full and timely disclosure of information by NSPI to the Board, consultants and appropriate Intervenors forms the basis of the justification for a FAM. In the absence of same, no meaningful review by parties of NSPI's fuel costs and the manner in which fuel is procured could occur. Disclosure of information relating to affiliate transactions has been a particularly controversial issue in the months leading up to this hearing. In fact, NSPI's unwillingness or inability to provide certain requested information persisted until just prior to the commencement of the FAM hearing. The Board believes it would be helpful to more fully explain the context in which the concern relating to disclosure arose.

[54] The Board's concern in this case relates primarily to fuel-based transactions between NSPI and its "affiliates" — unregulated companies which, like NSPI, are owned

⁵ Decision, 2007 NSUARB 8, p. 23

by Emera Inc. Affiliates were created in the years following the 1992 privatization of Nova Scotia Power Corporation, the former Crown Corporation. In an effort to protect the interests of ratepayers and provide high-level guidelines to NSPI on such matters, the Board and NSPI worked on a Code of Conduct, intended to govern affiliate transactions.

The purpose of the Code was to:

... ensure that the customers of Nova Scotia Power Inc. (NSPI) are not harmed by transactions between NSPI and its affiliates.

[Board Order, NSPI-P-167, March 16, 2001, Schedule A]

[55] The Code was subsequently amended to provide that:

NSPI's management will conduct the company's transactions with affiliates in such a way that its utility customers benefit from such transactions.

[Board Order, NSPI-P-167, November 9, 2004, Schedule A]

[56] The Board's concern about the potential of ratepayers subsidizing NSPI affiliates was underscored in August of 2001, when NSPI requested Board approval to assign a ten year gas supply contract to Emera Inc. The contract provided for 60 million cubic feet of natural gas per day to be supplied to NSPI at an established price. The assignment request proposed by NSPI indicated that since the contract provided no value to NSPI, it was not necessary for Emera Inc. to compensate NSPI for the assignment of same. The Board was very concerned with respect to the assignment of a contract that had the potential of creating benefits for NSPI and ratepayers with no compensation in return. The Board found the "no value" assessment to be dubious at best and, following further questions and interaction between NSPI and the Board, the proposal was informally

withdrawn. Since that time, the value of the gas supply contract to NSPI and its customers has been demonstrated on a number of occasions. Under the contract, NSPI has the ability to either sell the gas at a profit or use it for generation, depending on the current price. This has resulted in overall lower fuel costs to NSPI and, consequently, to ratepayers.

[57] From that time on, the Board has more closely monitored affiliate transactions, particularly those involving fuel, requiring yearly reports as well as audits by independent third parties. Intervenors in subsequent rate hearings have also raised affiliate transactions involving fuel as a major concern and the Board has, in the past, disallowed expenditures by NSPI to affiliates when the Board believed it to be inappropriate. The issue of disclosure relates directly to the FAM, as without full disclosure of these transactions, NSPI's fuel procurement practices cannot be adequately examined.

[58] The most recent affiliate transactions audit was conducted by Liberty and its report dated May 17, 2007 (as well as its evidence in this proceeding) makes it clear that significant problems were encountered in accessing, what Liberty believed to be necessary information, in order to complete the thorough and comprehensive audit it had been retained to perform. Under questioning by the CA, John Antonuk described the problem as follows:

243. Q. Just going back a moment to the discussion that you and I had about the importance and how critical it was to have transparency. Can you make any comment as to the need for the company to display the correct approach to that or a cooperative approach?
- A. (Antonuk) I have an answer and I want to organize my thoughts a little bit, because that's a broad and, I think, a very important question.
244. Q. And it's an important question to us.

- A. (Antonuk) Our experience in rate cases and [in] the affiliate audit with the company's willingness to provide information has been not a good one. In our experience it has, in fact, been probably at the poorest level of cooperation with what we have found in the past. We continue to have concerns about whether that cooperation level will rise to the level we think is necessary. We are encouraged by the fact that this settlement -- and I think it's the strongest aspect of the settlement -- is that it provides what I think is a foundation for testing whether that cooperation level is going to improve in ways that are tangible. And by "tangible" I mean the establishment of a course of dealing between the company and stakeholders and the creation of documents during 2008 that will do two things; allow the Board to decide before January 1, 2009 whether that level of cooperation has been shown, and (b) to establish the roster and the contents of specific documents, specific forecasting information, that will allow us down the road, namely 2009 and beyond, to test whether, in fact, that level of cooperation is continuing. I think I said to you a number of times in the stakeholder meetings we were kind of in the "show me" mode with respect to the company's cooperation and responsiveness. I think now is the time for them to show that through 2008 if, in fact, the Commission -- or the Board decides to accept the settlement.
245. Q. Can the Board not give a commitment for the FAM before being shown?
 A. (Antonuk) For my own part I can answer that I would like to see an opportunity before the FAM begins to affect customer rates for that confirmation of appropriate level of transparency and cooperation to exist, and I think that confirmation should come after a demonstration of what is going to happen and does happen in 2008 and what doesn't happen, although obviously I'm in the camp of hoping that it does happen.

[Transcript, November 6, 2007, pp. 106-108]

[59] NSPI now indicates it is committed to transparency and timely disclosure.

[60] The Board wishes to make it clear to NSPI that if full and timely disclosure of complete and adequate information to assess its fuel procurement practices continues to be a problem, the implementation of a FAM will not occur. NSPI has the opportunity during the 2008 "trial run" to demonstrate its willingness to ensure that this new commitment is carried out in a manner which is satisfactory to the Board.

V COST SHIFTING BETWEEN RATE CLASSES (ELI 2P-RTP)

[61] The Framework provides that for the purpose of the FAM, fuel costs will be calculated as per section 2.1.4 of NSPI's direct evidence.

2.1.4 Costs included in Fuel

All expense items included as "Fuel" in recent rate applications will be recovered through the mechanism. These will include ...

Fuel (F) will also include credits and debits associated with the ELI 2P-RTP rate. These credits and debits are as a result of increments or decrements from the CBL and represent fuel costs and savings required to serve the load. GRLF and net export sales revenues will be subtracted from NSPI's fuel costs (and the associated kWh sales would be subtracted from the divisor).

[Exhibit N-1, p. 10]

[62] NSDOE, in its closing submission, raised concern regarding cost shifting between rate classes:

As a general principal of rate setting, NSDOE strongly believes that costs associated with a particular rate class should be born by that rate class in their entirety. NSDOE would note that to the extent that there may, in the future be, over or under recoveries within the ELI 2P-RTP rate class, the impact of the operation of the rate can, and should, be dealt with among those parties on the rate, or NSPI, all of whom are in a position to petition this Board for direction.

To the extent that the current proposal by NSPI, allows for the possibility of costs associated with ELI-2P-RTP to be shifted from that rate class to other rate classes through the inclusion of the rate class debits and credits as fuel costs, that portion of the proposed methodology should be disallowed.

[NSDOE Closing Submission, p. 7]

[63] The Board, in its Decision 2006 NSUARB-97, approved the ELI 2P-RTP rate and stated that:

[190] The rates which have been approved by the Board in respect of this application are cost-based rates, set in accordance with the Board's fundamental responsibility to ensure that rates charged to all customers of NSPI are fair and reasonable. The Board is satisfied, based on the evidence before it and the structure and conditions imposed on the operation of these rates by the Board, that these rates are not preferential to, or subsidized by, any of NSPI's customer classes.

[191] The two rates approved by the Board to be available to SEB are:

Rate:

(a) a 2P-RTP rate (with a flat CBL) based on NSPI's approved cost of service study with increments and decrements priced at marginal cost subject to a 20% annual energy band and certain other restrictions;

(b) Dr. Stutz's proposed rate (as amended by the Board) including his proposal that the frequency and duration of interruptions are as outlined in the Board's letter of December 23, 2005.

[Decision, 2006 NSUARB 97, p. 66]

[64] The Board questioned NSPI during the hearing to clarify the impact of ELI 2P-RTP on fuel costs included in the FAM .

... I guess just final question, the fuel costs for 2-part RTP is based on agreed CBL I guess in the rate. And that's the fuel cost in the base rate now. And any above and below changes was supposed to be covered in that rate based on the actual cost, I guess, up and down. So what this happens now, as I understand is that any difference on those up and costs, actual costs and the fuel will be part of the FAM.

A. (Tedesco) Yes.

[Transcript, November 6, 2007, p. 93]

[65] Having reviewed the transcript and the submissions of the parties the Board is uncertain about the issue raised by NSDOE which is whether the current proposal allows for the possibility of costs associated with the ELI 2P-RTP to be shifted from that rate class to other rate classes through the inclusion of the rate class debits and credits as fuel costs. NSPI is to file a complete explanation of the relationship between this real time price rate and the FAM as it relates to this question by January 15, 2008. Other parties may respond by January 31, 2008. If necessary the Board will issue a supplemental decision clarifying its views on this issue.

VI DECISION AND CONDITIONS

The Public Interest

[66] The main question to be addressed in this matter is whether the approval of a FAM at this time is in the public interest. The Board, in previous decisions, has indicated that it does not view the concept of a FAM as being contrary to the public interest. For example, while the Board refused NSPI's request for a FAM in its March 31, 2005 decision, it did so as a result of its lack of confidence at that time in NSPI's fuel procurement ability, rather than opposition to a FAM in general:

[131] The Board shares the views of the intervenors with respect to the FAM proposed by NSPI. The Board recognizes that FAMs exist in many other jurisdictions and can, potentially, be a positive and useful regulatory tool. However, in view of the Board's findings with respect to imprudence and inadequacies in NSPI's fuel procurement practices, it would be quite inappropriate to approve a FAM at this time. The Board does not believe it is in the public interest to transfer the risk of fuel price volatility to ratepayers when NSPI's ability to achieve the best possible fuel price is in question.

[Board Decision, March 31, 2005, para. 131]

[67] Subsequently, in its March 31, 2006 decision, the Board stated that:

While the Board has concluded in this decision that NSPI has made significant improvements in its fuel procurement procedures, the Board still has reservations about incorporating, at this time, an adjustment mechanism with respect to NSPI's fuel budget. As noted above, there remain elements of the Company's Fuel Procurement Policies and Procedures Manual which require improvement, most notably as it relates to natural gas, and improving the transparency of its decision-making in relation to its fuel. In these circumstances, the Board is reluctant to vary from its current regulatory practice of setting the fuel budget.

[Board Decision, 2006 NSUAR 23, p.109]

[68] In its February 5, 2007 decision, the Board identified the circumstances which it believes are necessary to be in place in order for a FAM to meet the public interest test.

Clearly, the decision as to whether a FAM should be approved and implemented depends on whether the Board is satisfied that NSPI has successfully met these prerequisites.

[69] The term "public interest" is often referred to, not just in proceedings for this Board, but on a wide range of matters. In the Board's view, it may be helpful to set out how the Board carries out its responsibility to protect the public interest and how this responsibility is applied in the present case.

[70] The Board has the statutory authority to carry out significant regulatory oversight of NSPI. For example, the following sections of the *Public Utilities Act* (the "Act") read as follows:

Supervision of utility by Board

18 The Board shall have the general supervision of all public utilities, and may make all necessary examinations and inquiries and keep itself informed as to the compliance by the said public utilities with the provisions of law and shall have the right to obtain from any public utility all information necessary to enable the Board to fulfil its duties. R.S., c. 380, s. 18.

Approval of improvement over \$25,000

35 No public utility shall proceed with any new construction, improvements or betterments in or extensions or additions to its property used or useful in furnishing, rendering or supplying any service which requires the expenditure of more than twenty-five thousand dollars without first securing the approval thereof by the Board. R.S., c. 380, s. 35; 2001, c. 35, s. 30.

Duty to furnish safe and adequate service

52 Every public utility is required to furnish service and facilities reasonably safe and adequate and in all respects just and reasonable. R.S., c. 380, s. 52.

Equal rates and charges for similar services

67 (1) All tolls, rates and charges shall always, under substantially similar circumstances and conditions in respect of service of the same description, be charged equally to all persons and at the same rate, and the Board may by regulation declare what shall constitute substantially similar circumstances and conditions.

[71] The reasons for the Board's role in this regard are explained in its March 31, 2005 decision as follows:

... NSPI is not like an unregulated retailer. It is a virtual monopoly which operates its business on a cost-of-service basis. Providing electricity to all communities in the Province was not (and likely still is not) financially feasible for private, competitive companies. For that reason, the Province's electric service supplier is a cost-of-service monopoly. In return for undertaking and continuing the costs of electrification of the Province, the Utility is permitted, under the Act, to recover the reasonable and prudent costs of providing this service. Because it is a monopoly, regulation operates as a surrogate for competition. One of the regulator's tasks is to balance the need for the Utility to recover its reasonable and prudent costs with the need to ensure that ratepayers are charged fair and reasonable rates.

[18] It is in the interests of all Nova Scotians to ensure that NSPI continues to be a stable and financially sound company. This is a reality which the Board must consider when determining what, if any, rate increase is warranted.

[19] In short, rates charged to customers are based on costs incurred by the Utility in providing service. If the Board finds certain costs to be imprudent or unreasonable, it can (and has) disallowed such expenditures and reduced proposed rate increases accordingly...

[Board Decision, March 31, 2005, 2005 NSUARB 27, p. 7]

[72] Electricity is an essential service. The cost of providing electricity to all areas of the Province is in excess of \$1 billion per year. These costs are passed on to each category of ratepayer (e.g., residential, small commercial, industrial, etc.). In order to protect the public interest, the Board must ensure that NSPI, a monopoly providing an essential service to the public, does not abuse its monopoly status by overcharging its customers. The Board meets this responsibility in two ways. During a general rate application, the Board reviews the revenue required by NSPI to comply with the sections of the *Act* noted above (as well as others), and satisfies itself that the costs NSPI proposes to recover from ratepayers reflect only those expenditures NSPI must or should incur, and that the costs of same are reasonable, justifiable and reflect a price which is as low as reasonably possible. The rates include an appropriate return to NSPI. Between rate

hearings, the Board applies a similar test when considering expenditures proposed by NSPI which exceed \$25,000.

[73] In this case, the Board is applying the same test to the proposed FAM. A FAM, in the Board's view, does not in any way change or diminish its power to oversee NSPI's operation on an ongoing basis, nor does it lessen the Board's ability to protect the public interest.

[74] The statutory requirements NSPI must meet when seeking higher rates do not change under a FAM. A FAM simply changes the process by which an increase (or decrease) in that portion of rates which relate to fuel can occur. At present, NSPI must file a general rate application when seeking an increase in rates. Recent legislation enacted by Government limits NSPI to one such request per year.

[75] Fuel costs are the single largest variable expense incurred by NSPI, and subsequently passed on to ratepayers, when rates are set by the Board. In its evidence, NSPI also states that, in 2007, the projected cost of fuel is \$470 million dollars—a cost which is volatile, a factor beyond the control of NSPI.⁶

[76] The Board views a FAM as a tool which can actually provide a closer and more timely oversight of NSPI's fuel costs than is presently the case. As noted elsewhere in this decision, under a FAM, assessments as to the reasonableness of fuel expenses and NSPI's performance in obtaining fuel at the lowest price reasonably possible, will be carried out by the Board, as well as Intervenors, on an ongoing and more frequent basis than in

⁶ Exhibit N-1, p. 53

the past. In the last ten years, this form of fuel costs examination has occurred four times—always in conjunction with general rate applications. Under a FAM, fuel costs will be determined on an annual basis, following the reporting, analysis and stakeholder involvement in the FAM process throughout the preceding year, which forms the basis for any adjustment.

[77] Customers should also understand that, under a FAM, the rate they pay to NSPI will not go up and down every time the cost of fuel fluctuates. In other words, a FAM will not operate in the same manner as they experience at the gas pumps, where prices can change every week.

[78] Even under the proposed January 1, 2009 implementation date of the FAM, the earliest time a fuel adjustment change to rates could possibly occur would be January 1, 2010. Also, it could only occur then if the previous year's fuel costs passed all the reporting, auditing, and review tests designed to ensure that the cost to be passed on to ratepayers is as low as reasonably possible—a result which, in the Board's opinion, improves its ability to protect the public interest.

[79] In addition, the Board believes that the approval of a FAM may not result in fewer general rate applications. For example, NSPI must incur significant costs to upgrade its generating facilities in order to comply with new environmental emission standards. These costs are unavoidable as the continued operation of these plants remain necessary while alternative renewable energy sources are more fully developed. While there is no question that protection of the environment is a necessary and positive requirement, it is not inexpensive and these costs will, ultimately, be borne by ratepayers.

[80] Accordingly, NSPI can be expected to file a general rate application(s) over the next few years to recover these costs, at which time all aspects of NSPI's revenue requirement will be the subject of a full examination by all interested parties.

[81] In terms of further addressing customers' concerns as to how the approval of a FAM may impact them, the Board wishes to specifically address the following component in the Framework:

Significant FAM Changes

Where, in the absence of a General Rate Application, an increase for any customer class of more than ten (10%) compared with the rate payable in the prior year as caused by the application of the FAM procedures, the parties agree that the Board should consider appropriate measures to assist customers, such as whether part of the increase should be deferred for collection, within interest.

[Exhibit N-45, p. 2]

[82] It should be clearly understood that while the signatories to the Framework have determined that increases in the manner described above should cause the Board to intervene, the Board is in no way limited by this clause. To the contrary, as set out in more detail in this decision, the Board may intervene for any reason it deems appropriate.

[83] Finally, when questioned by the Board at the public hearing, Dr. Stutz succinctly set out the reasons why a FAM, operating under the conditions he and Liberty have recommended to the Board, is in the public interest:

26. Q. I only really have one question, and that is I understand the benefit of having a Fuel Adjustment Mechanism for Nova Scotia Power. They certainly perceive it as a benefit. They've asked for it before. And now we're at a further stage down the road where at least a number of stakeholders believe it's an option that they should be able to exercise with a trial run year in between. I'm not quite so clear on what the benefit to the ratepayers is. I understand there's an indirect one with respect to the risk that the company faces and correspondingly higher cost to them to borrow money, and indirectly ultimately that would filter down. But to be able to adjust rates

based on the volatility of fuel prices, particularly in terms of that 10-percent benchmark that's included in the framework for a FAM settlement, I just wonder how -- how in your view the public interest is protected and how benefits would accrue to ratepayers if the Board were to approve this.

- A. I think that rates have, all else equal, been higher than they might otherwise have been because you don't have a FAM. And the way this comes about can be seen in Exhibit JS-4 that's attached to my evidence. Basically what it shows -- you don't have to turn it up, but what it shows is that despite the Board's best efforts in this regard, we've tended to err on the high side when we've set the fuel costs that are included in base rates. And when that happens, all else equal, customers pay more than they otherwise would. So to the extent that we can bring things together, have customers pay only actual fuel costs, there is an improvement...

[Transcript, November 6, 2007, pp. 223-224]

[84] Accordingly, the Board is satisfied that, subject to NSPI successfully meeting all the conditions set out in this decision, approval of the FAM application is in the public interest.

Conditions

[85] Based on the submissions of the various parties who appeared before the Board and participated in the hearing and oral argument, there appears to be a range of views as to the speed of proceeding to institute a FAM and the conditions that might be attached. None of those parties are adamantly opposed to a FAM.

[86] The parties to the Framework have adopted a common position. The CA sees the FAM as an appropriate rate mechanism for Nova Scotia if certain conditions are met.⁷ HRM adopts a position similar to the Consumer Advocate. The Province recommends a trial run be utilized by the Board to evaluate the proposed operation and

⁷ Transcript, November 13, 2007, p. 104

administration of a FAM. Dr. Stutz, in his November 6th opening statement, says as follows:

While I still prefer a full passthrough Fuel Adjustment Mechanism ("FAM"), the Settlement, as well as my discussions, shows that most parties prefer a built-in incentive. For a major change in regulatory arrangements, such as adoption of a FAM, public acceptance—part of Bonbright's Criteria #1—is important.

Turning to fuel forecasting, the Settlement calls for development of a Board-approved standard methodology, as well as effective oversight of its application. This helps address my issues with the incentive. It is important that the standard methodology be settled early enough in 2008 so that its suitability for use within the FAM process, with its tight time lines, can be fully evaluated before the Board is called upon to approve it.

The Settlement calls for consultation on auditing requirements and "standard filing templates". One needs a general set of filing requirements in order to develop templates. As Liberty points out on pp. 4-6 of its reply evidence (N-25), it and NSPI have proposed such general requirements. The Board could help the process of template development along by indicating that one of these sets of general requirements should be followed. Because Liberty's requirements reflect the perspective of audit and review, adoption of its general requirements seems reasonable. At a minimum, changes in, or omissions of, items included by Liberty should require justification.

It would be good to have the standard filing templates approved early in 2008. That would allow at least a few quarters of "trial run" to help address time lines and transparency, before the proposed FAM start date of January 1, 2009.

Assuming that my comments related to fuel forecasting and reporting requirements are adequately addressed, I would recommend approval of the Settlement.

[Exhibit N-54, p. 1]

[87] Liberty sees a FAM as the best way to deal with fuel and energy costs. Mr.

Antonuk further states:

269. A. (Antonuk) It does. And we're very much influenced in that regard by the fact that what started as a sort of chaotic array of opinions about a FAM have coalesced at least to some extent -- to us, enough of an extent to say that if we're going to get to a FAM, which in the long run we think is the best way to deal with fuel and energy costs at a hypothetical utility -- if we're going to get to a FAM here, I think we've got maybe what to me is the last really good opportunity to make it happen. And if we don't, maybe it won't for a long time. So I guess what I'm saying is I want to be an optimist, but I still want -- I'm still in the "show me" mode.

...

508. Q. Okay. And whatever you've seen so far and the exchange of letters between Nova Scotia Power and Mr. Outhouse has allowed you to suggest that -- taking into account all the evidence you've given us today, that we proceed on this path based on Exhibit N-45.

A. (Antonuk) Yes.

[Transcript, November 6, 2007, pp. 126, 127 & 211]

[88] Because the FAM rate changes reflect real cost changes, the FAM will ensure customers receive more timely and accurate price signals. The Board notes Dr. Stutz's evidence that rates may have been higher in the past than they might have been with a FAM. Recent history has shown that general fuel costs and customer rates have been higher than the cost incurred by NSPI, so customers may have paid more for the fuel to generate their electricity than necessary. This historical situation has been driven, in large part, by the need to forecast uncommitted fuel costs for a future test year.

[89] All parties will now have input into the design of, and an understanding of, a standard methodology for future NSPI fuel costs. This methodology will be subject to future Board approval. The Board believes this will mitigate concerns with respect to high fuel forecasts and will result in a more appropriate approach to the setting of fuel costs and rates than in the past.

[90] Customers will continue to have the right to challenge NSPI's fuel forecasts in each year as well as its procurement decisions.

[91] The concern of some is that there will be less oversight of NSPI. As noted, while implementation of a FAM will change the oversight of NSPI, it does not impair the Board's oversight powers. In fact, with respect to fuel, the Board and stakeholders will have additional and more frequent disclosure. The Board will continue to have all of the

powers to obtain information, scrutinize and approve capital investments, scrutinize costs, respond to customer complaints and summon the company for a general rate application when it believes one is required.

[92] If the FAM operates properly with respect to fuel, the Board and parties will receive more information on a more timely basis than we have before.

[93] The Board, having considered the matter, is prepared to give conditional, but not unequivocal, approval to a FAM to become effective January 1, 2009. The Board also approves the Framework with the following conditions:

- (1) **Standard Filing Templates.** Approval by the Board of standard filing templates to be developed in a stakeholder process as contemplated by the Framework (the Liberty recommendations noted in paragraph 46 are to be followed).
- (2) **Standard Methodology and Filing Requirements.** Approval by the Board of a standard methodology and filing requirements with respect to NSPI's fuel costs as contemplated by the Framework is required.
- (3) **Tariff Document.** Approval of a tariff document outlining the final tariff design and which will include audit provisions satisfactory to the Board.
- (4) **Adequate protection against rate shock.** While the Board notes the provision in the Framework that the Board should consider appropriate measures to assist customers in the event of an increase for any class of customers of more than 10%, the Board will monitor the operation of a FAM closely and reserves the

right to intervene in any circumstance where it believes an increase to a customer class is not acceptable or in the public interest and take such steps as it considers appropriate to assist such customers including deferring a part of the increase for collection in a future time period.

(5) **A meaningful stakeholder process.** Dr. John Stutz will continue to oversee the stakeholder process on behalf of the Board. Liberty will continue to be the Board's fuel consultant. On December 1, 2008, Dr. Stutz will file with the Board and interested parties a report and opinion as to the status of the Prerequisites and Conditions. By December 15, 2008, the Board will either give final approval to commence the FAM on January 1, 2009 or, if there has not been satisfactory progress on the Conditions and Prerequisites, delay implementation of the FAM.

(6) **An adequate process for monitoring.** In addition to the filing requirements to be approved in the Tariff and the Audit, the Board will seek input from stakeholders and review the operation of the FAM on June 30, 2009 and December 15, 2009.

(7) **A trial run.** NSPI is to begin filing of the standard monthly information by April 1, 2008 and all filing requirements by August 1, 2008, related to both the monthly and annual information reports and the standard methodology for fuel forecasts. If the methodology templates are available prior to these dates then these filings can occur earlier. In this way parties and the Board can see these filings and see how they will work on a trial basis prior to operation of the FAM. An

assessment of this will be part of Dr. Stutz's December 1, 2008, report. This responds in part to requests made by the CA, NSDOE and HRM.

(8) **Fulfillment of the Board's Prerequisites.**

(9) **A time frame.** The Framework and the trial run of the FAM should occur in accordance with the following timeline:

March 31, 2008	Filing of templates for monthly and annual information reports following stakeholder consultation
April 1, 2008	Filing of standard monthly information to begin
May 2008	<ul style="list-style-type: none"> • Filing of standard methodology for NSPI fuel forecasts and filing of the FAM tariff document(s) • Stakeholder comments
June 2008	Hearing (if necessary, to determine matters not resolved by the parties)
July 2008	Board decision on any matters in issue
August 2008	Commence all monthly and annual filings in advance of effective date
October 15, 2008	Filing annual report for 2008 (including forecast for 2009), for information only
December 1, 2008	Updated opinion from Dr. Stutz as to NSPI's compliance with the Prerequisites and Conditions
December 15, 2008	Decision of the Board
January 1, 2009	Tentative FAM effective date
June 30, 2009	Board review of operation of FAM to date including filing requirements. Input from stakeholders to be sought.
December 15, 2009	Board review of operation of FAM to date including filing requirements. Input from stakeholders to be sought.

Stakeholder Process

[94] The Board encourages attempts by parties to resolve their differences in advance of a hearing. The Board observes that the stakeholder process overseen by Dr. Stutz and in which many parties participated has been a very useful addition to the process of regulating NSPI. It has facilitated settlement among some of the parties. It has also provided a forum for the parties to understand the issues and come to a common understanding on many points so that the issues that remain to be litigated in the hearing were clearly defined and based upon a high level of knowledge and understanding of a FAM and its various features. In the Board's view this improves the regulatory process. The Board very much appreciates the work of all parties who participated in the pre-hearing process. Board members were not present at these meetings and in most cases did not see correspondence exchanged between the parties during the pre-hearing process. Therefore, the Board's members are viewing it from afar but, viewed from afar, it would appear to the Board to be a success.

[95] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 10th day of December, 2007.

Peter W. Gurnham

Margaret A.M. Shears

Kulvinder S. Dhillon

APPENDIX - A FORMAL INTERVENORS

Affordable Energy Coalition

Megan Leslie, Claire McNeil and Alasdair Sinclair

Avon Valley et al.

(Avon Valley Greenhouses Ltd.)
(Canadian Salt Company Limited)
(CKF Inc.)
(Crown Fibre Tube Inc.)
(Halifax Grain Elevator Limited)
(High Liner Foods Incorporated)
(Imperial Oil Limited)
(J. D. Irving Ltd., Saw Mills Division)
(Lafarge Canada Inc.)
(Louisiana Pacific Canada Ltd.)
(Maritime Paper Products Ltd.)
(Michelin North America (Canada) Inc.)
(Minas Basin Pulp & Power Company Ltd.)
(Oxford Frozen Foods Limited)
(Statia Terminals Canada)

Robert G. Grant, Q.C., Nancy G. Rubin and
Mark Freeman

Canadian Manufacturers & Exporters

Ann E. Janega, Robert Patzelt, Q.C. and Kristin Harris

Consumer Advocate

John Merrick, Q.C., Nancy Brockway and William
Mahody

Ecology Action Centre

Brendan Haley and Steve Zubalik

Energy Research Group ("ERG")

Larry Hughes, PhD and Mandeep Dhaliwal

GasWorks Energy Corp.

Dwight Jeans

Halifax Regional Municipality

Mary Ellen Donovan, Martin C. Ward, Q.C., and Julian
Boyle, P. Eng.

KnAP Energy Consultants

Terry MacDonald, P. Eng.

Liberal Caucus Office (Nova Scotia)

Michel Samson and Ryan Grant

**Municipal Electric Utilities Co-operative of
Nova Scotia**

Don Regan and Albert Dominie

New Democratic Party Caucus Office (NDP)

Frank Corbett, MLA and Lorraine Glendenning

**Province of Nova Scotia - Department of
Energy**

Scott McCoombs, Richard Penny, James Gogan, Paula
Zarnett and Trent Winestone

Mr. Allan F. Smith

Sierra Club of Canada

Bruno Marcocchio

Stora Enso Port Hawkesbury Limited
and
Bowater Mersey Paper Company Limited
("SEB")

George T. H. Cooper, Q.C., David S. MacDougall and
James MacDuff