STEWART McKELVEY
LAWYERS • AVOCATS

Cabot Place, 1100 – 100 New Gower Street, P.O. Box 5038
St. John's NL A1C 5V3 Canada tel: 709.722.4270 fax: 709.722.4565 stewartmckelvey.com

January 16, 2014

Stephen F. Penney
Direct Dial: 709.570.8881
spenney@stewartmckelvey.com

Ms. G. Cheryl Blundon
Board of Commissioners of Public Utilities
120 Torbay Road
P.O. Box 21040
St. John's NL A1A 5B2

Dear Ms. Blundon:

Re: An Application by Newfoundland and Labrador Hydro for approval of the terms and conditions applicable to the supply of electricity to North Atlantic Refinery Limited (NARL)

Enclosed please find an original plus 8 copies, of NARL's written submission in connection with the above referenced matter.

We trust this is satisfactory.

Yours truly,

Stewart McKelvey

Stephen F. Penney*

SFP/reh

*Law Corporation

Enclosures

C: Geoffrey P. Young, Newfoundland & Labrador Hydro
Gerard Hayes, Newfoundland Power Inc.
Thomas J. Johnson, O'Dea, Earle
Thomas J. O'Reilly, Q.C., Cox & Palmer
Dean A. Porter, Poole Althouse

DISTRIBUTION LIST FOR MAIL			
CHAIR & CEO	✓	LEGAL COUNSEL	✓
VICE-CHAIR	✓	COMPLIANCE AUDITOR	
COMMISSIONER	✓	FINANCIAL OFFICER	✓
COMMISSIONERS	✓	FINANCIAL ANALYST	
DIRECTOR-BOARD SECRETARY		IT OFFICER	
DIRECTOR-REGULATORY		OTHERS STEA SJB	✓
RA	MM	✓	

214329

IN THE MATTER OF the Electrial Power Control Act, 1994, RSNL 1994 c E-5.1 (the "EPCA") and the *Public Utilities Act*, RSNL 1990 c P-47 (the "Act") and regulations thereunder; and

IN THE MATTER OF an Application by Newfoundland and Labrador Hydro ("Hydro") pursuant to Section 71 of the Act, for approval of the terms and conditions applicable to the supply of electricity to North Atlantic Refining Limited ("North Atlantic").

WRITTEN SUBMISSIONS OF NORTH ATLANTIC

Introduction

These are the written submissions of North Atlantic in relation to Hydro's Application of November 19, 2013 seeking to have the Board of Commissioners of Public Utilities (the "Board") impose a clause limiting the liability of Hydro with respect to damages in their Service Agreement with North Atlantic (the "Service Agreement").

North Atlantic submits that the Application of Hydro should be dismissed. There is insufficient evidence submitted by Hydro to alter the Board's finding in Order No. P.U. 7(2002-2003), namely that the limitation of liability provisions of the standard service agreement applicable to the other industrial customers (Clause 9.04) does not apply to the Service Agreement.

- Firstly, the application of Hydro does not contain sufficient evidence of a lack of insurability, and insurability would not be a determining factor in any event.

- Secondly, the application of Hydro does not contain sufficient evidence of industry standards for a $1,000,000 limitation of liability.

- Thirdly, the reliance by Hydro on improperly characterized notions of "mitigation" are not relevant to the issue of the imposition of a limit of liability, and in any event, the steps taken in the circumstances by North Atlantic to reduce risk attributable to power outages are reasonable.

In the alternative, North Atlantic submits that if the Board is inclined to impose a limit of liability, on either a permanent or interim basis pending a full hearing on this matter, it ought to be either

a limitation to claims for direct damage with no monetary limit, or to a monetary limit of $10,000,000.

Order No. P.U. 7(2002-2003)

The Board's finding in Order No. P.U. 7(2002-2003) that Clause 9.04 does not apply to the Service Agreement has been in effect for over 11 years. Neither Hydro, nor the other Industrial Customers, has sought to have the Board reconsider its finding, prior to the present application.

Clause 9.04 states as follows:

> *9.04(1) Subject to Clause 9.04(2) hereof, Hydro shall be liable for and in respect of only that direct loss or damage to the physical property of the Customer caused by any negligent act or omission of Hydro, it servants or agents. Customer agrees that for the purpose of the Clause 9.04, "direct loss or damage to the physical property of the Customer" shall not be construed to include damages for inconvenience, mental anguish, loss of profits, loss of earnings or any other indirect or consequential damages or losses.*
>
> *9.04(2) Hydro's liability under sub clause 9.04(1) applies only when the direct loss or damage to the Customer arising from a single occurrence exceeds the sum of $100,000. In no event shall the liability of Hydro exceed the sum of $1,000,000 for any single occurrence.*
>
> *9.04(3) Customer further agrees that any damages to which it may be entitled pursuant to clause 9.04(1) shall be reduced to reflect the extent to which such losses or damages could reasonably have been reduced if the Customer had taken reasonable protective measures.*

The Board finding contained the following reasoning and conclusions:

> *In light of the importance of this issue upon both North Atlantic and NLH, and its other customers, it is imperative that sufficient evidence be offered to allow the Board to fully consider the two viewpoints. The Board sees merit in the argument that it is inappropriate for the other customers of NLH to bear the full cost of an industry specific sensitivity to power interruption, yet no evidence was called to show the impact upon the other NLH customers. It may also be argued that this risk is a cost of doing business, which should be absorbed by North Atlantic, yet no evidence was called to establish the costs and the impact upon North Atlantic of incurring these costs. No evidence was presented either as to potential sources of backup power or other ways in which damage from power interruption may be mitigated, nor was there any evidence on practices at other refineries. In addition, while there was some suggestion during the hearing that insurance is not available to cover this type of loss, the parties did not file any evidence on this point.*

> *The Board finds that the evidence presented was inadequate to allow the Board to impose the liability provision as proposed by either of the parties. The Board is not satisfied that the liability provision is reasonable and necessary and will not accept clause 9.04 as part of the rules and regulations of the provision of service to North Atlantic. The Board acknowledges that the decision to exclude this provision from the contract will result in the continuance of the current situation in that the liability of NLH will have to be established and limited according to common law. However, the Board notes that it has not decided upon the merits of the liability provision and that, under the* Act, *the parties may bring this issue back before the Board.*

It is worth bearing in mind that the Service Agreement imports elements of negligence. Article 12.01 and 12.02 provide that Hydro will be liable for damages to person or property caused by electronic current up to the point of delivery, and beyond the point of delivery where the damages arise from the negligence of Hydro's employees. Article 12.01 and 12.02 state as follows:

> *Article 12*
>
> *Responsibility for Damages*
>
> *12.01 Beyond the point of delivery, the Customer shall indemnify and hold Hydro harmless with respect to any and all claims that may be made for injuries or damages to persons or property caused in any manner by electric current or by the presence or use on the Customer's premises of electric circuits or apparatus, whether owned by Hydro or by the Customer, unless and to the extent that such injuries or damages are caused by negligence on the part of the employees of Hydro.*
>
> *12.02 Up to the point of delivery, Hydro shall indemnify and hold the Customer harmless with respect to any and all claims that may be made for injuries or damages to persons or property caused in any manner by electric current or by the presence or use on the Customer's premises of electric circuits or apparatus owned by Hydro and resulting from or arising out of the negligence of Hydro's employees or other persons for whom Hydro would in law be liable, unless and to the extent that such injuries or damages are caused by negligence on the part of the employees of the Customer.*

North Atlantic accepts that the Service Agreement does not guarantee a continuous source of power, and that for claims for service interruption, North Atlantic would have to prove negligence.

The Board's finding was not premised on Hydro being able to obtain Failure to Supply Insurance Coverage (which forms the thrust of Hydro's Application). It was merely noted that "there was

some suggestion" that insurance was not available to cover this loss. As is apparent from the submissions below, such insurance is, and has been available, and there is insufficient evidence to determine that Hydro cannot insure against this loss.

Another factor that the Board considered was that "no evidence was called to show the impact upon the other NLH customers." Hydro's application does not address this point.

A further factor that the Board considered was that "no evidence was presented either as to potential sources of backup power or other ways in which damage from power interruption may be mitigated, nor was there any evidence on practices at other refineries." North Atlantic addresses this issue below, and demonstrates that, insofar as notions of "mitigation" are relevant to this analysis, North Atlantic takes reasonable and appropriate steps to reduce the impact of power loss, and that having a full co-generation facility would be uneconomic.

In Order No. P.U. 7(2002-2003), the Board stated that "no evidence was called to establish the costs and the impact upon North Atlantic of incurring these costs." North Atlantic addresses this issue in detail further below. North Atlantic submits that allocating to North Atlantic the preponderance of the risk of substantial harm resulting from Hydro's negligence would be unfair, would be a disincentive to Hydro acting as a prudent and responsible monopoly supplier of power, and is not a result dictated by either the governing legislation (the Act or the EPCA) nor by any evidence of reasonable regulatory practice.

The Evidence at the 2002 Hearing

Glenn Mifflin, then Vice-President and Chief Financial Officer of North Atlantic, pre-filed written evidence, and he was cross-examined by counsel to Hydro (and others) on January 10, 2002. Attached to these submissions are copies of that pre-filed evidence and a transcript of Mr. Mifflin's cross-examination. Counsel for Hydro has indicated that it consents to the written evidence of Mr. Mifflin and a transcript of his cross-examination forming part of the record before the Board on this application.

The gist of Mr. Mifflin's evidence, which is still relevant and accurate, was the following:[1]

> *Q: Why does North Atlantic consider that the ceiling of $1 million of damage claims contemplated by Article 9 is inadequate?*
>
> *A: North Atlantic purchases all of its electrical energy from Hydro. That energy supply is critical to the efficient operation of the refinery and its equipment. When the energy supply to the plant is disrupted or discontinued, it generally requires an emergency shutdown of all process units and causes loss of product through emergency flaring. Once production is down as a result of a power failure, it takes 5-7 days to bring the refinery back up to full production. Certainly, any time there is an emergency shutdown there is greater risk to process equipment and catalysts.*

Mr. Mifflin provided an example of outages in 1995 and 1996 where the Refinery suffered damages of approximately $20,000,000 (approximately $9,000,000 is related to direct damages for repair costs, lost product and damages to catalyst). Mr. Mifflin provided another example of an outage in 1997 where the Refinery suffered damages of approximately $2,000,000 (approximately $650,000 is related to direct damages for repair costs, lost product, loss of chemicals, and physical damages to the Visbreaker Unit).[2]

Mr. Mifflin also stated in his 2002 testimony:

- There is sufficient backup power supply to power the control room to allow the refinery to be shut down on an emergency basis, and to keep the boilers and steam system running (at 30 line 58-63).
- That the demand is roughly 30 megawatts (at 30, line 79).
- That North Atlantic investigated building a co-generation unit, but it was cost prohibitive (at 30, line 17-85).

In 2012, the EPCA was amended to provide that Hydro has "the exclusive right to supply, distribute and sell electrical power or energy", and mandating industrial customers to purchase power exclusively from Hydro (s.14.1(1)). Accordingly, North Atlantic has no choice but to purchase power from Hydro. The construction by North Atlantic of its own 30 MW co-generation

---

[1] 2002 Pre-filed Evidence of Glenn Mifflin, at 2-3.

[2] *Ibid*, at 3-5.

facility could only approach economic feasibility if North Atlantic had a reliable market for the surplus power generated by such a facility. In the event that North Atlantic was to construct a co-generation facility, it would be prohibited from selling surplus power from that facility into the electrical grid.

The Board ought to be Cautious in Imposing a Limitation of Liability

It is extraordinary and significant to take away a person's common law right to claim compensation for negligence. Curtailments of a person's right to bring an action in cases of negligence are exceptional, and these rare curtailments typically arise under legislation[3], or by contract, where both parties have agreed to all of the contractual terms.

In 2002, the other industrial customers agreed with the contractual terms, including article 9.04 (the $1 million limitation of liability).

The effect of imposing a limitation of liability of $1 million on North Atlantic, which has no legal or practical ability to acquire power by other means, is stark. A unilateral limitation of liability would act as a disincentive for Hydro to take reasonable and prudent measures to avoid negligent service to North Atlantic, and would ignore the fact that, as between North Atlantic and Hydro, Hydro has the far greater ability to take such measures. To paraphrase Mr. Mifflin's testimony in 2002: North Atlantic is responsible for their negligent actions; Hydro ought to be responsible for their negligent actions as well.[4]

Further, the Board ought also to be wary in adopting the over-simplistic view advocated by Hydro that it is inappropriate for Hydro (and presumably, the rate payers) to bear this risk. By way of analogy, other public institutions such as the Provincial Government, the School Districts, the Health Boards and Memorial University do not have blanket limitations of liability, and are subject to civil law suits, for which the public ultimately bear the burden (whether for damage awards or increased insurance premiums, should insurance for the loss be available). The legislation governing Hydro places it in no more privileged position than the Province and Crown agencies with respect to liability for negligence.

---

[3] An example of this would be the *Limitations Act*, SNL c L16.1.

[4] January 10, 2002 Testimony of Glenn Mifflin at 30 (line 93) to 31 (line 9).

The fact that Hydro is regulated by the PUB does not completely insulate Hydro from any business risk. The Newfoundland Court of Appeal stated the following in *Re Newfoundland (Board of Commissioners of Public Utilities)*:

> *Although some of the activities of the utility are regulated within the framework of the statutory objectives,* ***the utility nevertheless remains subject to business risks and the effects of management decisions****. To the extent, the financial risks associated with the operation of the utility, just as in the case of any private business, are to be borne by the investors in the enterprise, not the consumer of the service. [emphasis added]*[5]

It is also worth bearing in mind that North Atlantic plays a significant role in the economy of Newfoundland and Labrador. It is the third-largest public sector employer in the province, employing approximately 460 to 470 employees, and is responsible for 20 to 25% of the hydrocarbon products (including gasoline, propane, jet fuel, and diesel fuel) in the province. Placing an undue risk on North Atlantic could have a significant impact on the public, given North Atlantic's importance to the Newfoundland and Labrador economy and fuel supply.

There is Insufficient Evidence of a Lack of Insurability

Hydro states that effective July 1, 2013, they no longer have insurance coverage for failure to supply claims by North Atlantic. Specifically, they state that: "[Hydro's] Failure to Supply Service Coverage remains in force with a specific exclusion removing all coverage for any such claims brought by [North Atlantic].[6]

Hydro asserts that the rationale for the exclusion is that "insurers typically offer Failure to Supply Service coverage to utilities on the basis that the utility's liability is limited under the regulatory contract." Hydro continues that "it was determined that since Hydro's liability to [North Atlantic] was not limited in any way, that the exposure was such that they were no longer willing to provide coverage going forward."[7]

However, this evidence is insufficient to change the *status quo*, which has been the case for over 11 years, for the following reasons:

---

[5] 164 Nfld & PEIR 60 ¶ 31 (NLCA).

[6] Hydro Application, ¶ 8.

[7] *Ibid.*

- Having a limit of liability was not a pre-condition to having to provide this coverage in any time from 2002-2013. It was only upon the reporting of the claim for damages from North Atlantic arising from the February 4, 2013 power outage that Hydro has asserted this as an issue.[8]

- No evidence has been provided to suggest the impact of the claim for damages from North Atlantic arising from the February 4, 2013 power outage on Hydro's insurability. In NA-NLH-003 Hydro indicates that their insurer initially wanted to exclude all Failure to Supply coverage, presumably because of the magnitude of North Atlantic's claim, and not because of the existence or not of a limit of liability.[9] Hydro indicates that "communications between Hydro and its broker with respect to the July 1st renewal terms were primarily verbal", but does not provide any evidence regarding the nature of those verbal communications and whether the claims history impacted the decision of the insurer.

- It does not appear that there was consultation with any other insurers about whether they would be prepared to insure this risk. The only documentation which appears relevant to this point contains an email from Hydro's broker that "Northbridge is 'hinting' that we might want to remarket your Umbrella due to their perception of unlimited liability to one or more industrial customers". [10] Hydro further states that "efforts focused on achieving the best terms from Hydro's current insurer" and makes the vague assertion that "proceeding to market with a large and recent claim outstanding would result in increases in premiums, restrictive coverage, higher deductibles and/or exclusions."[11] It does not appear that the insurance policy was ever remarketed, so there is no evidence whether other insurers would have insured this risk – merely speculation. Further these statements suggest that it is the magnitude of the outstanding claim that could cause difficulties with obtaining insurance.

---

[8] NA-NLH-002, Reference 4.

[9] NA-NLH-003, Reference 7.

[10] NL-NLH-002, Attachment 1, at 1.

[11] NL-NLH-006, Reference 7.

- Hydro acknowledges that it "did not canvass the markets to determine whether a different limitation of liability arrangement might have been available." There is no evidence whether insurance would be provided if there were a limitation of liability to direct damages, or some greater amount (for example, $10,000,000).[12]

- Lastly, Hydro admits that it is unaware of any insurer who has made a $1,000,000 limit of liability a condition of coverage.[13]

There is Limited Evidence of an Industry Standard

To support its position that there ought to be a $1,000,000 limit of liability, Hydro references the other industrial agreements. Hydro also references 3 other jurisdictions (Ontario, Quebec and British Columbia). However, Hydro is only able to point to one jurisdiction, British Columbia, which includes a standard supply contract that provides for a numerical limit of liability.

In Ontario, there are two limitations placed on liability claims from a customer. The distributor is only liable to the customer for claims "which arise directly out of the wilful misconduct or negligence". Secondly, the distributor is not liable for claims for damages in the nature of loss of profit or consequential damages. In other words, if they are negligent, a distributor is responsible for direct damages to a customer's property, without a monetary limitation on liability. Hydro is seeking protection greater than that offered in Ontario.

In Quebec, the limitation of liability clause of the Conditions of Electricity Service references "intentional or gross fault" and "material damage". Both of these concepts are Civil Code concepts. "Intentional or gross fault" roughly equates to common law concepts of wilful misconduct and gross negligence (something arguably requiring a greater level of fault than simple negligence).[14] "Material damage" is distinct from the Civil Code concepts of "bodily" or "moral" damages, and relates to damages that were foreseen or foreseeable at the time the obligation was contracted and can relate to both the loss sustained and the profit which has been deprived. Therefore, in Quebec, the claims are limited to "gross fault" but there is no

---

[12] NA-NLH-007, Reference 7 and 8.

[13] NL-NLH-008, Reference 8.

[14] Lewis Klar, *Tort Law*, 5th ed at 372 to 374. Klar points out that the concept of gross negligence is controversial, and that some courts have said "a man is either guilty of negligence, or he is not."

monetary limitation on liability, and material damage would relate to both what in common law would be considered direct and possibly consequential damages.[15] Hydro is seeking protection which is arguably greater than that offered in Quebec.

North Atlantic references Article 12 of the Service Agreement and notes that there is already an effective limitation of liability to negligent claims.

Hydro Mischaracterizes the Duty to Mitigate

By suggesting that North Atlantic take steps to mitigate its losses **prior** to a loss, Hydro mischaracterizes the common law duty to mitigate. In any event, notions of mitigation do not bear on whether the Board ought to impose a limit of liability.

The concept of mitigation considers the steps which a plaintiff takes after a loss has occurred. As was stated by the Supreme Court of Canada in *Janiak v Ippolito*, "mitigation has to do with **post**-accident events" [emphasis added].[16] The Newfoundland and Labrador Court of Appeal made a similar statement, confirming that: "the duty to mitigate arises **after** the breach or wrongful act and **after** the plaintiff becomes aware that the defendants' wrong acts have caused a loss" [emphasis added].[17]

Should a plaintiff neglect to take reasonable steps consequent to a loss, the plaintiff is prevented from claiming damages which are due to failing to take such steps.[18] In other words, in a law suit by a customer, Hydro would be entitled to raise mitigation arguments to limit their damages, regardless of an limitation of liability in the service agreement.

Furthermore, the law is clear that a plaintiff who takes reasonable steps to mitigate is to be compensated for taking those steps to mitigate as part of the damages. As the Supreme Court of Canada stated in *Southcott*:

> *On the other hand, a plaintiff who does take reasonable steps to mitigate loss may recover, as damages, the costs and expenses incurred in taking those*

---

[15] Civil Code ss 1607, 1613.

[16] [1985] 1 SCR 146 at ¶ 37.

[17] *Abitibi-Price Inc v Voith Hydro Inc*, (1992) Nfld & PEIR 1 ¶ 91 (NLTD).

[18] *Southcott Estates Inc v Toronto Catholic District School Board*, 2012 SCC 51 at ¶ 23-25 [*Southcott*].

> *reasonable steps, provided that the costs and expenses are reasonable and were truly incurred in mitigation of damages.*[19]

It would appear that Hydro is suggesting that North Atlantic ought to take prohibitively expensive steps to allow the Refinery to remain open in the event of a power outage caused by Hydro's negligence, and that the entire costs of those steps ought to be borne by North Atlantic. In this context as well, Hydro's position is not an accurate representation of the concept of mitigation, and ought not to be considered in considering whether to impose a limit of liability on North Atlantic.

The "Mitigation" Steps Suggested by Hydro are not Reasonable

In any event, and assuming that pre-loss actions can be considered "mitigation" (which position is contrary to the clear statements of the Supreme Court of Canada, as discussed above) the "mitigation" steps suggested by Hydro are not reasonable.

The burden falls on Hydro, "who needs to prove both that the plaintiff has failed to make reasonable efforts to mitigate, and that mitigation was possible."[20] Even if the Board were to accept, contrary to the clear statements of the Supreme Court of Canada, that the concept of mitigation can require a party to take certain steps prior to, or in anticipation of, a loss, Hydro would have to prove that such steps are reasonable. Hydro has offered no evidence in this regard.

North Atlantic has back-up generation in place to power the control room to allow the Refinery to be shut down on an emergency basis, and to maintain the boilers and steam system running for a period of time during an outage.[21] This is consistent with industry practice.

In response to NA-NLH-012, Hydro offered certain examples of backup power of other refineries. North Atlantic provides the following discussion of the evidence provided by Hydro below:

---

[19] *Southcott*, ¶ 25.

[20] *Ibid*, ¶ 24.

[21] January 10, 2002 Testimony of Glenn Mifflin at 30 (line 58-63).

Q1. Is the Oil Refinery connected to your transmission network by a single transmission line or two (or more) parallel lines? (i.e. single radial circuit or multi circuit)

Member 1. "Multi Circuit."

Member 2. "One of our subsidiary companies supplies an oil refinery with two 144 kV lines which makes it convenient for line maintenance. We also supply many oil and gas extraction/processing plants, some with a single line and some with 2 lines. The one with a single line usually have their own generation at site."

Member 3. "Hydro One has refineries on single transmission circuit with distribution back-up (i.e. Dx connected to provide a small amount of back-up power). We also have refineries connected via multiple HV circuits."

North Atlantic has 2 lines which come from different power sources, similar to what is described by Members 1, 2 and 3. North Atlantic further understands the reference by Member 3 to a "Dx" to mean a small generator which allows for an orderly shut-down ("a small amount of back-up power), similar to the sort of generator that North Atlantic maintains.

Q2. What, if anything, has your Utility done to improve the reliability of supply to the Oil Refinery? i.e., special protection systems on the transmission lines (eg., lightning arresters), special operating procedures, etc. If applicable, pleas provide additional detail.

Member 1. "Nothing outside of the norm. Sites are equipped with Lightning Arrestors and Lightning Arrestor monitors. Are also targeting them for the installation of Hydrans to monitor transformer oil quality."

Member 2. "We don't do anything special. If the line is 240 kV, we use A and B protection, each consisting of distance relays with teleprotection. On 144 kV lines, 2 distance relays are used without teleprotection, except in special cases of short lines where teleprotection and line differential and/or distance relays are used."

Member 3. "We install modern protection systems and coordinate P&C maintenance with season fuel refining change-overs for single circuit supply."

Like Member 1, the Refinery has lightning arrestors and monitors on the line that comes from Bay D'Espoir. North Atlantic's system is similar to that described by Member 2. Like Member 3, North Atlantic attempts to coordinate seasonal turn-arounds with protection and control ("P&C") maintenance.

Q3. Does the Oil Refinery have a backup or alternate power supply in the event of loss of supply from the transmission network?

Member 1. "No, not aside from the two transmission feeds. There exists an auto-transfer scheme at one of the sites to transfer all load to one transformer in the event of an outage to one of the transmission lines."

Member 2. "See above."

Member 3. "We have oil refinery with Dx connected back-up."

The auto-transfer scheme described by Member 1 is similar to that employed by North Atlantic. As noted above, the reference by Member 3 to "Dx" appears to refer to a back-up generator, which as noted in Q1, supplies a "small amount of back-up power".

Q4. If you answered yes to Q3 above – What type of the backup power supply is ultized?

i. Local generation at the Refinery (eg., diesel or gas turbine)

ii. Supply from another Utility (eg., emergency supply via distribution utiltity)

iii. Other (please provide details on type)

Member 1. N/A.

Member 2. "Usually, local generation."

Member 3. "Distribution supply at reduced capacity."

Member 1 does not have back up power. Member 3 has already been discussed above.

Q5. What are your Utility's best practices for transmission supply to Oil Refineries? Are there any special requirements?

Member 1. "Have substation operating procedures for each site addressing any unique scenarios or special considerations and how to respond accordingly."

Member 2. "None that I am aware of."

Member 3. "We would prefer double circuit supply from the HV system to feed two or more independent HV refinery transformers. Some refineries seem to choose a big burn off of fuel when their primary single circuit supply is interrupted."

Hydro does not provide any evidence of a refinery which maintains a co-generation facility, capable to provide sufficient power to maintain steady-state operations. Like the examples given above, North Atlantic has a multi-circuit system, and a back-up generation to allow for a safe shut-down. As well, the back-up systems of the Refinery are consistent with Hydro's and North Atlantic's own information on industry standards.

North Atlantic is aware of certain oil and gas extraction facilities in remote locations which have back-up power generation, which appear to be nature of the facilities described by Member 2, but much less power is required for that sort of facility, than for a refinery. North Atlantic is also aware of some refineries in North America which have a co-generation facility, but those facilities are close to an abundant source of natural gas, which makes co-generation economically feasible, unlike the situation at the Refinery.

North Atlantic requires approximately 30 MW of power to maintain steady-state operations. This is beyond a simple generator which can be switched on when there is a loss of power. Rather, a co-generation facility would be required.

In 1997, North Atlantic, studied the possibility of building a co-generation facility. North Atlantic concluded that it was not reasonable to simply build a 30 MW generator. The only way to properly finance such a power supply would be to create sufficient power for the Refinery, with the remainder to be sold into the electricity grid. The cost in 1997, of a 175 MW co-generation facility was estimated between $300 - $400 million, with annual operating costs of $18 million, and it was determined to have been uneconomic.[22]

Such a facility would be even less economically feasible in the present circumstances, since North Atlantic would not be able to sell surplus power to the electrical grid. NA-NLH-016 and Hydro's response are repeated below:

> *Q. Does Hydro agree that, if North Atlantic were to make necessary capital investment to provide essential backup power for its operations, it would be prohibited from utilizing that alternative generation capacity other than exclusively for emergency purposes, under subsection 14.1(4) of the Electrical Power Control Act, 1994?*
>
> *A. It is confirmed that the use of this generating capacity would, under that statutory provision, be limited to emergency applications. Hydro has not been made aware that NARL has any present intentions or desires to produce energy to displace its purchases of power and energy from Hydro or to use it in other applications.*

---

[22] Excerpt from Proposal for Supply of Additional Generation, RFP 000009, Capital Cost estimate summary.

There is no Basis to have a Limitation of Liability Identical to that negotiated by the Other Industrial Customers imposed on North Atlantic

In paragraph 19 of the Application, Hydro references Section 73 of the Act, and section 3(1)(a) of the EPCA asserts that since the other industrial customers have a $1 million limitation of liability, so should North Atlantic, and that Hydro ought not bear the commercial risk of its own negligence. Those assertions do not withstand scrutiny.

Firstly, there is no obligation under the relevant legislation requiring the industrial customers to have identical service agreements. Section 73 of the Act makes reference to "tolls, rates and charges" and not contractual terms. Likewise, section 3(1)9a) of the EPCA references "rates", and not contractual terms.

Secondly, there is precedent for separate contractual terms being imposed on an industrial customer – the present example of no limitation of liability, which has been in place for over 11 years, without complaint. Moreover, Order P.U. 1 (2007) is an example for where Aur Resources Inc. (now Teck Resources Limited) received a preferential base rate for power from Hydro.[23]

Thirdly, North Atlantic does not operate "under substantially similar circumstances and conditions" as is required by section 73(1) of the Act. The consequences of a power outage, as described in the testimony of Glenn Mifflin, are more severe than for the other industrial customers. A co-generation facility is uneconomic. While North Atlantic has to bear the business risk for non-negligent power outages (for example, in the case of power outages caused by severe weather events), it ought not to have its legal rights to sue Hydro curtailed as a result of this Application.

In the Alternative, North Atlantic seeks a limitation to Direct Damages or a Limit of $10,000,000

In the alternative, North Atlantic would seek a limitation to direct damages with no monetary limit. In the event of a negligent interruption of power supply, it is difficult to anticipate what direct damages North Atlantic might suffer. Moreover, this is the approach taken in Ontario.

---

[23] P.U. 1 (2007).

North Atlantic has currently made a claim against Hydro for damages arising from an outage occurring on February 4, 2013, which North Atlantic attributes to Hydro's negligence, for approximately $25,000,000 (approximately $8,600,000 is related to direct damages for replacement and repairs to damaged equipment and catalyst).

In at least two situations, the direct damages (damages to property, cost of repairs and lost product) suffered by Hydro have neared the $10,000,000 limit proposed by North Atlantic in 2002 ($9,000,000 as a result of the 1995 and 1996 outages, $8,600,000 as a result of the 2013 outage). North Atlantic asserts, as a further alternative argument, that should the Board be inclined to impose a limit of liability, either on a permanent or interim basis pending a full hearing, a reasonable limit of liability would be to limit claims to direct damages (as is the case in Ontario) or to $10,000,000, an amount which would result in fairer compensation to North Atlantic as a result of Hydro's negligence.

Summary

There is insufficient evidence submitted by Hydro to alter the Board's finding in Order No. P.U. 7(2002-2003), namely that the limitation of liability provisions of the service agreement applicable to the other industrial customers (Clause 9.04) does not apply to the Service Agreement. Accordingly, Hydro's application ought to be dismissed.

Alternatively, if the Board is inclined to impose a limit of liability, on either a permanent or interim basis pending a full hearing on this matter, such limitation ought to be either to claims for direct damage with no monetary limit (as is the case in Ontario), or to a monetary limit of $10,000,000 (a number which more accurately represents the exposure of North Atlantic to direct damages to property).

Costs

North Atlantic requests that the Board make an order in their favour for their costs of participation in the Application.

1 **All of which is respectfully submitted on behalf of North Atlantic.**

DATED at the City of St. John's, in the Province of Newfoundland and Labrador, this 16th day of January, 2014.

STEWART MCKELVEY
Solicitors for North Atlantic Refining Limited

Per: _____
Stephen F. Penney

TO: The Board of Commissioners of Public Utilities
Suite E210, Prince Charles Building
120 Torbay Road
P.O. Box 21040
St. John's, NL A1A 5B2
Attention: Board Secretary

TO: Newfoundland & Labrador Hydro
P.O. Box 12400
500 Columbus Drive
St. John's, NL A1B 4K7
Attention: Geoffrey P. Young,
Senior Legal Counsel

TO: Newfoundland Power Inc.
P.O. Box 8910
55 Kenmount Road
St. John's, NL A1B 3P6
Attention: Gerard Hayes,
Senior Legal Counsel

TO: O'Dea, Earle
323 Duckworth Street
P. O. Box 5955, Stn. C
St. John's NL A1C 5X4
Attention: Thomas J. Johnson, Consumer Advocate

TO: Cox & Palmer
Scotia Centre, Suite 1000
235 Water Street
St. John's, NL A1C 1B6
Attention: Thomas O'Reilly

NORTH ATLANTIC REFINING LIMITED
EVIDENCE OF GLENN MIFFLIN

Q. Would you please state your name, address and occupation?

A. My name is Glenn Mifflin. I reside at St. John's, Newfoundland. I am a chartered accountant and I am employed by North Atlantic Refining Limited ("North Atlantic") as Vice-President and Chief Financial Officer. I have been involved in electrical rate issues since 1992 and have been in my current position since about 1988.

Q. Is there a power supply agreement in place between North Atlantic and Newfoundland and Labrador Hydro?

A. Yes. There is a power supply agreement dated December 16, 1987, in place between Newfoundland Processing Limited (now North Atlantic) and Newfoundland and Labrador Hydro ("Hydro") for the supply of power to the refinery at Come by Chance.

Q. What is the purpose of your testimony?

A. With one exception, North Atlantic's position is exactly the same as that of the other Island Industrial Customers.

In its proposed Industrial contracts filed in mid-December, 2001, Hydro included a revised Article 9 dealing with liability. Clause 9.04 of the proposed Article 9 proposes a floor of

$100,000 and a ceiling of $1 million on damage claims against Hydro arising from Hydro's own negligence, and, in addition, proposes restrictions on the kinds of damages which can be recovered.

In December, 2001, North Atlantic was contacted by counsel for the Island Industrial Customers with respect to the proposed floor of $100,000. Although, apparently, a draft of the clause with the proposed ceiling of $1 million was circulated to North Atlantic earlier, as part of a document outlining other proposed changes to the contract, North Atlantic did not focus on the adequacy of the proposed ceiling until the issue of a floor on damage claims was raised by Hydro in mid-December.

North Atlantic believes that the ceiling of $1 million on damage claims is inadequate to address North Atlantic's anticipated losses in the event that its energy supply is interrupted as a result of Hydro's negligence.

Q. Why does North Atlantic consider that the ceiling of $1 million on damage claims contemplated by Article 9 is inadequate?

A. North Atlantic purchases all of its electrical energy from Hydro. That energy supply is critical to the efficient operation of the refinery and its equipment. When the energy supply to the plant is disrupted or discontinued, it generally requires an emergency shutdown of all process units and causes loss of product through emergency flaring. Once production is down as a result

of a power failure, it takes 5-7 days to bring the refinery back up to full production. Certainly, any time there is an emergency shutdown there is greater risk to process equipment and catalysts.

Q. Can you give any examples of the extent of the damages which North Atlantic might suffer if it lost production as a result of Hydro's negligence?

A. Yes. In 1995, there were three occasions in July and August when the refinery experienced a complete power outage resulting in the shutdown of all refinery operating units. A similar outage occurred in August, 1996. North Atlantic estimates that it suffered direct damages in excess $19 million dollars as a result of those power outages.

As a result of those outages , product in the refinery units at the time of the power failure was damaged, a large quantity of product was destroyed as a result of excess flaring caused by the outage, various equipment located in the refinery was damaged, catalyst used in the refining process was damaged and, while the operational units were shut down or not operating at normal conditions, the refinery was unable to process feedstock located in storage at the refinery. North Atlantic's estimate of its damages from these incidents is as follows:

Overtime wages	$ 80,000.00

Wages and production loss removing large coke mass	$ 1,027,500.00
Product flared	$ 548,000.00
Damages to Catalyst	$ 7,000,700.00
Loss of profit	$ 68,500.00
Production losses including yield loss and lower feed rates	$ 11,124,400.00
Total	$ 19,849,100.00

On December 8, 1997 the refinery again experienced a complete power outage resulting in an almost complete shutdown of all refinery operations. As a result of that power failure, all of the operating units were shut down and could not be operated collectively at normal operating conditions until on or about December 15, 1997.

As a result of that outage, some product in the refinery units at the time of the power failure was damaged, a large quantity of product was destroyed as a result of excess flaring caused by the outage, various equipment located in the refinery was damaged and, while the operational units were shut down or not operating at normal conditions, the refinery was unable to process feedstock located in storage at the refinery. North Atlantic's estimate of its damages from that December, 1997 incident is as follows:

Overtime wages	$ 19,200.00 US
Fuel lost	$ 50,000.00 US

Product flared	$ 6,000.00 US
Damage to overhead finfan coolers and throughput losses due to lack of cooling capacity	$ 270,000.00 US
Propane yield losses from damage to depropanizer unit	$ 130,000.00 US
Damages to Visbreaker Unit	$ 150,000.00 US
Loss of chemicals and nitrogen usage	$ 15,000.00 US
Loss of profit	$ 130,000.00 US
Production losses including yield loss and lower feed rates	$1,291,000.00 US
Total	$2,061,200.00 US

At current exchange rates, the damages from that single incident were in excess of $3,000,000 in Canadian funds.

Q. What is North Atlantic's position in relation to the ceiling on damages recoverable from Hydro when Hydro has been negligent?

A. North Atlantic recognizes that there may be occasions when a power outage causing significant damages to North Atlantic will occur due to circumstances beyond Hydro's reasonable control. In such circumstances North Atlantic accepts that it will be unable to recover its losses from Hydro. However, North Atlantic believes that Hydro should not be able to limit its exposure for direct losses incurred as a result of a power outage due to Hydro's own

negligence. If there is to be a ceiling on damages claimable for such an occurrence, which North Atlantic does not believe there should be, then that ceiling should be set so that all Industrial Customers have the opportunity to recover their legitimate losses.

Q. What does North Atlantic propose?

A. North Atlantic proposes that there be no ceiling on the amount recoverable from Hydro if Hydro is negligent. In the alternative, if the Board determines that a ceiling is required, then North Atlantic proposes that the ceiling be set at $ 10 million per occurrence.

MS. HENLEY ANDREWS: Okay. Those are all my questions. Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Henley Andrews. Thank you, Mr. Dean and Mr. Backus, very much. This concludes your testimony, and I'd like to reiterate Mr. Browne's comments, thank you, once again, for the (inaudible) of the mill. It certainly added another dimension to the evidence for me. Thank you.

MS. HENLEY ANDREWS: Mr. Chairman, Mr. Mifflin is prepared to testify now.

MR. NOSEWORTHY, CHAIRMAN: When you're ready, Ms. Henley Andrews. Good afternoon, Mr. Mifflin, good to see you again.

MR. MIFFLIN: Thank you.

MR. NOSEWORTHY, CHAIRMAN: I wonder if you could take the Bible in your right hand, please? Do you swear on this Bible that the evidence to be given by you shall be the truth, the whole truth and nothing but the truth, so help you God?

MR. MIFFLIN: I do.

MR. NOSEWORTHY, CHAIRMAN: Thank you, sir. Ms. Henley Andrews, could I ask you to begin, please?

MS. HENLEY ANDREWS: Yes, Mr. Chairman. Mr. Mifflin, you are familiar with the written evidence filed yesterday on your behalf?

MR. MIFFLIN: I am.

MS. HENLEY ANDREWS: And are you prepared to adopt that evidence?

MR. MIFFLIN: I am.

MS. HENLEY ANDREWS: Mr. Chairman, Mr. Mifflin is available for cross-examination.

MR. NOSEWORTHY, CHAIRMAN: Thank you, very much. Ms. Greene? No, Mr. Young.

MR. YOUNG: Thank you, Mr. Chair.

MR. NOSEWORTHY, CHAIRMAN: I'd ask you to begin your cross.

MR. YOUNG: Good afternoon, Mr. Mifflin. Mr. Mifflin, my questions should be directed fairly closely to the fairly narrow issue that's left, I think, and you've described it in your evidence. I'd like to start with the present contract. When I mean the present contract, not the one that was filed today, which is the new proposal, but the one that Newfoundland ... North Atlantic Refinery is operating under at this time. I take it you're familiar with that contract?

MR. MIFFLIN: I am.

MR. YOUNG: And with the liability provision in that contract, also you would be familiar with that?

MR. MIFFLIN: I am.

MR. YOUNG: Is it your understanding that that one, that clause I'm referring to is similar to that which Hydro proposed in May that was filed in this application?

MR. MIFFLIN: Correct.

MR. YOUNG: And I also presume that you will agree with me that the liability provision that was filed in the revised contract, well, exactly, there was one today and there was also one in December, the clause hasn't changed here. It constitutes a fairly large concession in relation to liability here by Hydro?

MR. MIFFLIN: It constitutes a change from the previous contracts, yes.

MR. YOUNG: Well, for example, Hydro is, for the first time, acknowledging and willing to pay some claims where Hydro is found to be negligent of a certain character within a certain limit?

MR. MIFFLIN: That's correct.

MR. YOUNG: Correct? So I think it's fair to say that the narrow issue we're here to discuss, is it $1 million is the ceiling or $10 million is the ceiling, which is what we proposed?

MR. MIFFLIN: That's right.

MR. YOUNG: The point of power outages caused by Hydro's negligence, which is really all we need to talk about here. I just want to get some sense of what happens at the refinery if there is, say, a five minute outage, one which is not announced, unplanned outage. Could you give us a brief description of that?

MR. MIFFLIN: Anything, any power disruption, it could be a dip or it could be an outage ... let me back up a second. What the refinery is is it's a dynamic process under which flammable materials are being pushed through tubes in furnaces, and those furnaces are operated, and the reactors at the refinery are operated at very high temperatures in very high pressures. A loss of power stops the flow of that product through there and it becomes dangerous, so as part of the safety systems the control room, depending on the nature of the thing, will wait, I think, up to a maximum of about three minutes, and sometimes they don't wait that long, depending on the circumstances. At that point they go into an emergency shutdown and the entire ... they close down all the process units. Part of that process pushes all of the product in the units, the gas, through to flare and the whole thing gets flared so you have no

flammable liquid left to cause us a problem, so inside of about three minutes they have ... that's the window of opportunity to not do anything or beyond somewhere in that time period they will go to an emergency shutdown. At that point, all of the process units shutdown, the products go to flare, and all of the units then have to be inspected to see what sort of damage, if any, has happened, and then you call back people on overtime and you go through a restart procedure. The restart procedure can take anywhere between five to seven days because you have to, because they're high pressure and high temperature you have to ratchet up the pressure and the temperature on each of the units until you get back to a stable state of operation. The last unit is usually the hydro cracker unit, which is the extremely high pressure and high temperature.

MR. YOUNG: So am I to understand that for an outage of less than three minutes they don't have to go through this process?

MR. MIFFLIN: It may happen.

MR. YOUNG: It may happen?

MR. MIFFLIN: It may happen.

MR. YOUNG: So it could be a one minute outage, for example?

MR. MIFFLIN: Depends on the people with their hands on the switch, the guys in the control room. If they determine that this is an event that necessitates a shutdown, they will shut it down if they deem it to be unsafe.

MR. YOUNG: Are you aware of any other industrial customer, or for that matter any other user of electricity in this province or elsewhere who has that kind of a level of sensitivity to a short duration power outage of perhaps less than a minute to less than three minutes?

MR. MIFFLIN: I'm not aware.

MR. YOUNG: Anyone that comes close? I mean, are you the only one in this case?

MR. MIFFLIN: I really couldn't say anything about it.

MR. YOUNG: I'm just wondering if you have any knowledge of the way refineries may find themselves dealing with this kind of a problem elsewhere in the North American continent, for example, in the grid in the middle of the North American continent where their power supplies are from various points and it's a more robust system because it's not essentially a large isolated system as we have on the island. Do you have an understanding of the difference which may occur or may arise in that circumstance?

MR. MIFFLIN: I don't have specific knowledge. Certainly, power liability in the North American grid is less of a concern than it certainly was in 1995, '96 for us. Power liability is a very important issue for us.

MR. YOUNG: I'm just wondering, also you mentioned that the control room operators have up to three minutes and then they take steps. I take it there must be some processes which you've put into place to mitigate any loss in these circumstances. Do you have any backup power supply for that?

MR. MIFFLIN: There's sufficient backup power supply to power the control room to allow the refinery to be shut down on an emergency basis, and I believe there's sufficient activity to keep the boilers and steam system running, irrespective of the power outage, but those are the two main areas which would have some ability to continue.

MR. YOUNG: When you say ...

MR. MIFFLIN: From functionality.

MR. YOUNG: Yeah, sorry. When you say "activity" do you mean that there is, you know, sufficient energy still there or that ... I'm not talking about electrical energy, I'm talking about, you know, heat that must have been in place, or is it the fact that you have another generation source for electrical energy to fire those?

MR. MIFFLIN: No, we have no other generation.

MR. YOUNG: Okay. Have you looked at or considered having a backup system to supply your refinery for its electrical needs in an electrical outage?

MR. MIFFLIN: Our demand, I think, is somewhere in the range of ... now, you're really sticking me here.

MR. YOUNG: 30 megawatts?

MR. MIFFLIN: Yeah, 30 megawatts, and I know somewhere back in the early '90s we did look at, you know, putting in some sort of a co-generation unit, but, there's two issues. One, what we then have is essentially a redundant system, and we neither had the capital to do so and the payback on that was much too long. We had a greater need for capital to improve the refinery than build a co-generation.

MR. YOUNG: I guess the bottom line here is that you're asking Hydro to stand and Hydro's customers ultimately, I would suppose, to stand to the amount of $10 million as opposed to what's being proposed in the revised filing of $1 million, and that's the case even if it's just perhaps a one minute power outage?

(2:30)

MR. MIFFLIN: Well, I'm not quite asking that. What I'm basically saying that a commercial enterprise such as ourselves, we're responsible for our own negligence, and

there's no limit and we don't think Hydro should have a limit for their own negligence either. It's been suggested by counsel that the no limit option might be a little unpalatable, so for any one occurrence an alternate of 10 million was suggested, but what my position really is that Hydro, if it was in a commercial situation as I am, or the other industrial customers, they would be responsible for their own negligence and can't contract out a ceiling to that negligence.

MR. YOUNG: That's an interesting point, because if we had a choice to supply you or not we might say, well that $10 million limit is not on, it's too risky for us and we don't wish to, you know, take that risk, but, of course, we're a utility and you're charged as you ought to be, the same rates as everyone else, and I'm suggesting to you that one interpretation one could make to the proposal you're making is that you're asking for a different level of service than other customers.

MR. MIFFLIN: No.

MR. YOUNG: Well, just let me propose this hypothesis for a moment, that if you were to ask one of our rural customers what extra amounts they would be willing to pay to avoid one minute outages or to what extent a one minute outage causes them serious harm, I think they would look at you askance and say it's an inconvenience and it's a nuisance and we don't like outages, but I mean, that's that, isn't it?

MR. MIFFLIN: I can't speculate as to what other customers ... firstly, I don't know what the additional cost you're suggesting would be. Secondly, I can't anticipate what they would say, but, what we require, as an enterprise working in this province is we require reliable power. If the power is reliable then Hydro shouldn't ... and is competent in its reliability then through its own negligence ... or through good clean operation then it shouldn't be worried. If you cause something through your own negligence, like any other commercial operation, you should be responsible for that negligence, and that's really the issue, and the two things I'm after is reliable power and a (inaudible) to provide the power through an act of your own negligence you should be responsible for and pay us for the physical damage that happens to our plant.

MR. YOUNG: The willingness of Hydro to accept responsibility for their negligence, I think, has been demonstrated. I mean, we've said that ... and this is a change, we've acknowledged this. We've gone from a point that the contract didn't accept liability for negligence to one where it accepts it up to $1 million, so I don't think the issue is that. I think the issue is a matter of price and risk and what the nature of the service is. I mean, the part of the deal we've made with the ratepayers is that, you know, we have power available, you can take it at a certain rate. That assumes a whole lot of things about the system. Certain reliability standards we're able and willing to provide, some, you know, going beyond that may be extra costs and there may be extra costs we can pass on, but at this point, what we're offering to the customers of Newfoundland is a utility standard where it is now, but I'm suggesting from your point, this is the question I have for you, is don't you see that just asking us to take on all costs for which we might be liable for, and there's no contract, under negligence, is asking really for a different standard altogether?

MR. MIFFLIN: No. If I'm a householder in Davis ... or I don't know where you supply power, on the Northern Peninsula and you fail ... and I lose the motor in my fridge, you're going to pay 100 percent of that motor. In our case you're going to pay ten percent of the physical damage, so maybe the proper thing is to make it a proportionate representation in order to be fair so that you will pay the same proportion of damage to all ratepayers.

MR. YOUNG: Well, you don't pay a different rate, though.

MR. MIFFLIN: I'm mean, I'm just ... the fact is that if I'm a home owner, and you're talking about your rural home owner. I'm in a different class from a rural home owner. I've got an enterprise out there that have invested well over $300 million. I've got 700 families that depend on this, and you're suggesting that ... you're comparing me to a householder in, say well, look, I'll pay 100 percent of this householder's damage, but I know it's going to be less than $1000, but in my case, I'm in a very different circumstance and you're suggesting you pay one tenth of a possible $10 million occurrence. That's the range of difficulty I run into. And I think pointed out in my evidence that we did have one group of incidents where we did significant damage to catalysts and things like that, and that catalyst is $7 million, and so that could be an occurrence, so you're going to be paying me one tenth or up to a million, one seventh, in that case, of that catalyst, and yet you're going to pay your rural home owner the $200 for his fridge motor and that's inequitable.

MR. YOUNG: But if you look at the pool of ratepayers as a whole, if they were to look at you, I think you'd probably agree with me, they would see you as a very atypical customer of Hydro who's asking for coverage for a risk which were well out of the order of in the risks that we would incur if we were found liable for them, yet the rates are essentially the same and the standards of services as supposed to be about the same, so I'm suggesting to you that it's not really a one to one ratio for us to look at the motor of their fridge and your catalyst, I mean, it's a different order altogether, and that's why we are proposing the $1 million levelling point to restrict risk to that point.

Can you understand that?

MR. MIFFLIN: I understand it perfectly, and I understand exactly what you're saying. You're trying to ... I am atypical. I am a single refinery sitting in this province. I have a fair bit invested, and you have acknowledged that you want to recognize liability when you're trying to cap my physical damage liability to one tenth of the potential damage that could happen on any one occurrence. I don't think there should be any ceiling on paying for damage as a result of Hydro's negligence, and the answer to your question is, firstly, there was ... you know, A, you have agreed that there should be recognition of liability for your own negligence, that's fine, and now you're trying to cap that liability. There should be no cap. If you're negligent ... if I'm negligent I have to pay for it. I can't go out to my customers and say, you know, I'm sorry, I'm going to cap it at $150 or $1 million or $753.23, I can't do that. I'm responsible for my negligence.

MR. YOUNG: But if you had a delayed delivery of oil to one of your customers I don't see them coming to you with a $10 million claim for ...

MR. MIFFLIN: Absolutely.

MR. YOUNG: ... a very, very short delay.

MR. MIFFLIN: Absolutely, and you don't have the same problem with one of your rural customers, but with this customer you do, and if I run ... if I was supplying Newfoundland Hydro's plant at Holyrood and I ran Holyrood out of fuel then I would have to be responsible for my negligence in not delivering, and I'm sure Hydro would chase me for it, and I would say to Hydro, I'm sorry, I've got a cap of $1 million to the fact that you had to close your hydro plant down. It's ... I am an atypical customer and that's why the nature of my application and my evidence is that this $1 million is inadequate, it's inefficient, it's insufficient and inequitable with respect to my operations.

MR. YOUNG: So with respect to your very unique circumstances?

MR. MIFFLIN: Absolutely.

MR. YOUNG: That's all my questions. Thank you, Mr. Mifflin.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Young. Thank you, Mr. Mifflin. We'll move now, Ms. Butler, to your cross-examination, please?

MS. BUTLER, Q.C.: Thank you, Mr. Chairman. I wonder if I might, before I determine whether in fact I have any questions for Mr. Mifflin, ask for your indulgence for a moment. The unusual filing of Mr. Mifflin's testimony at this stage after Hydro has filed its complete case leaves me in a position of not really knowing, on the record, what Hydro's position is vis-a-vis this issue, and what Newfoundland Power would like Ms. Greene to state for the record, she's already communicated it to me verbally, is whether in fact Hydro does have insurance that covers these loses, and if not, then if such a loss were incurred, $1 million or $10 million, whatever, would that be treated by Hydro or sought to be treated by Hydro as a regulated expense?

MR. NOSEWORTHY, CHAIRMAN: Ms. Greene?

MS. GREENE, Q.C.: Certainly, the nature of the question certainly is relevant for Ms. Butler. As already have been indicated, the current contractual arrangements provide for no liability by Hydro for outages for any reason, and in looking at this issue we have explored the issue of insurance and we have been advised that it would be extremely difficult, if not impossible, to get insurance at an effective price. I can't say that it's impossible to get, the issue becomes at what price, but we have been advised by our risk insurance manager that insurance of this type of coverage is not readily available to Hydro, and the other question obviously would be in our minds as to whether ... how it would be treated as a regulated expense and whether it would be passed on to other customers. And our first position would be, yes, that that is the position that we would take. That would have to be reviewed in the circumstances if there were an event, so the answer to the question is my advice or the advice Hydro has received is we would not be able to get insurance for this type of liability at a rate that would be cost effective, if at all, and the issue whether it's a regulated expense, I don't think has been an issue this Board has dealt with, but our position would be it should be treated as a regulated expense, depending on the circumstance of the claim.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Greene. Does that satisfy your inquiry?

MS. BUTLER, Q.C.: Thank you, Mr. Chairman, it does, and that being the case, I have no questions for Mr. Mifflin. Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you. Mr. Browne, please?

MR. BROWNE, Q.C.: Thank you, Mr. Chairman. Mr. Mifflin, North Atlantic Refining Limited of which you're vice-president, chief financial officer, how many employees do you have there?

MR. MIFFLIN: About 700.

MR. BROWNE, Q.C.: And is that full-time jobs?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: That's constant?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: On that issue of insurance, do you have insurance in place in the likelihood you can't produce oil?

MR. MIFFLIN: Yes, we do. We have several layers of insurance. We have product liability insurance and we have business ...

MR. BROWNE, Q.C.: I'm not sure the microphone is picking you up.

MR. MIFFLIN: Oh, sorry. We have, for example ... these chairs move around. We do have product liability insurance, we do have business interruption insurance, we do have insurance against property damage, you know, and we have several layers, so ... and I don't have the insurance program in front of me so I can't talk at it in detail, but the initial layer of insurance which would be the highest frequency of use would be the most expensive, but incremental layers of insurance to cover the very low probability, but high dollar amount risk items, that incremental insurance is usually, certainly for us, is less expensive, significantly less expensive.

MR. BROWNE, Q.C.: Less expensive than what?

MR. MIFFLIN: If, for example, I paid my insurance premium is $1 million for $100 million worth of property insurance and I wanted to get another $1 million worth of property insurance, then that additional layer of $1 million would not cost me $100,000, it would cost me $50,000. If I wanted to get the next million it would cost me 25 and the next million would cost me, you know, 15 and so on, so each additional layer for that high dollar amount but lower risk eventualities, each layer would cost you less per dollar of risk assumed than the first layer. I don't know if that answers your question.

MR. BROWNE, Q.C.: Well, the loses you're describing in your evidence, are these insurable losses, do you have insurance for those?

MR. MIFFLIN: We have insurance for losses, yes, for physical damage.

MR. BROWNE, Q.C.: But do you have insurance for interruption of supply? If you can't produce and you have a ship, a tanker out there ready to move to market your product to California somewhere and you can't give supply, for some reason or another, do you have insurance for that eventuality?

(3:00)

MR. MIFFLIN: Well, certainly. Let me address it two ways. We do have liability for non-performance, so we can't cap it at $1 million, and we do have insurance in respect of certain non-deliveries, yes, not all circumstances.

MR. BROWNE, Q.C.: The premium you've paid for insurance for non-performance, do you have any idea of what you would be paying there?

MR. MIFFLIN: I don't.

MR. BROWNE, Q.C.: Can you ball park it?

MR. MIFFLIN: I can't even ball park it, not without the figures in front of me.

MR. BROWNE, Q.C.: Because wouldn't that be the similar insurance that Newfoundland Hydro would require if they can't provide?

MR. MIFFLIN: You're asking me about the insurance market, and that's beyond my field.

MR. BROWNE, Q.C.: Okay.

MR. MIFFLIN: I really can't answer the question properly.

MR. BROWNE, Q.C.: Okay, fair enough. These matters between yourself and Hydro and these allegations of negligence for past losses, are they the subject of an action currently before the Supreme Court of Newfoundland?

MR. MIFFLIN: There are two actions filed with the Supreme Court from four incidents in 1995, '96, the total of that one is about 19 million, and another one in 1997, the total of that is, I think, somewhere in the range of 2 million US, about 3 million Canadian. Those matters have not, to my knowledge, gone to trial.

MR. BROWNE, Q.C.: And who's taking the action on your behalf, are you taking it in your own right or is an insurance company involved?

MR. MIFFLIN: We're taking it in our own right.

MR. BROWNE, Q.C.: And Hydro is defending these actions?

MR. MIFFLIN: They have defended the actions, yes.

MR. BROWNE, Q.C.: And is Hydro defending it in their own right or through an insurer?

MR. MIFFLIN: Their own right, I believe.

MR. BROWNE, Q.C.: And what is the potential liability there, what are you claiming?

MR. MIFFLIN: On the first action comprising the first four incidents, I think it's something like 19 million ...

MR. BROWNE, Q.C.: How much?

MR. MIFFLIN: Nineteen million, Canadian.

MR. BROWNE, Q.C.: Nineteen.

MR. MIFFLIN: And the second one in 1997, I think, is

about 3 million, Canadian.

MR. BROWNE, Q.C.: And when are these actions to be concluded?

MR. MIFFLIN: Again, I wouldn't be able to comment on that one.

MR. BROWNE, Q.C.: Not in the test year, not in the 2002 or 2003, you don't know?

MR. MIFFLIN: That's right.

MR. BROWNE, Q.C.: Okay. It's my understanding, based on the evidence we heard this morning, that you sell Bunker C fuel?

MR. MIFFLIN: We do.

MR. BROWNE, Q.C.: And you sell Bunker C fuel to the Abitibi companies?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: Okay. Can you tell us about the supply, generally, you have any knowledge about the supply in the market of Bunker C product?

MR. MIFFLIN: Other than Labrador, on the island there's the major customers for Bunker C are the hospitals, Newfoundland and Labrador Hydro and the three paper mills. Hydro has a bidding process or a tender process under which they go to the market with respect to their supply. We do supply certainly the Abitibi mill in Grand Falls, and I think the one in Stephenville and Corner Brook have the opportunity and the luxury of some great storage to, upon occasion, take advantage of the spot market.

MR. BROWNE, Q.C.: The contract you have with Hydro, how does that work?

MR. MIFFLIN: Well, we don't have the contract with Hydro for the supply of bunkers to Holyrood. I'm just aware that's the big users of Bunker C. We supply most of the hospitals. We don't supply Newfoundland Hydro.

MR. BROWNE, Q.C.: Oh, you don't supply Newfoundland Hydro?

MR. MIFFLIN: No.

MR. BROWNE, Q.C.: Have you the capability, the capacity of supplying Newfoundland Hydro?

MR. MIFFLIN: We wouldn't, from our refinery. The quality of fuel that they use at Holyrood, I think, is 2.2 percent sulphur, which is the fairly good quality Bunker C. We generally make a higher sulphur content Bunker C, most of which we export.

MR. BROWNE, Q.C.: You also have a marketing division for consumers for home heating products, is that true?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: That market, is it all across the island or is it at specific locations?

MR. MIFFLIN: It's breadth is through the entire island. We do not go above, I think Port au Choix. We're not in Burgeo or Bay d' Espoir and we're not through the Springdale loop, that area up through Fleur de Lys.

MR. BROWNE, Q.C.: And is this for home heating fuel?

MR. MIFFLIN: That's all for home heating fuel, yes.

MR. BROWNE, Q.C.: Now, when you have increases in your product in the cost of oil or the cost of production do you normally pass that on to your consumers?

MR. MIFFLIN: Only where the market can bear it. If the price of product increases today and the market doesn't increase I absorb that increase.

MR. BROWNE, Q.C.: I guess you can absorb it up to a point?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: In terms of the payment options, what options, if any, do you have for your customers, your consumers?

MR. MIFFLIN: Well, there's a variety of options. The normal terms are 30 days. Notwithstanding that we do have equal payment plans for somebody who wants to budget their payments out, but other than that the normal terms are 30 days including most commercial ... both residential and commercial customers. We do have commercial customers that have significantly tighter credit terms, but that's a credit decision we would make.

MR. BROWNE, Q.C.: The equal payment plan, how does that work?

MR. MIFFLIN: Fundamentally we would take the estimated consumption by a consumer and just divide it by 12 months and they would pay it over that 12 month period, times an average price.

MR. BROWNE, Q.C.: They pay it over the year?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: Be similar, I guess, to Newfoundland Power's equal payment plan for their electricity?

MR. MIFFLIN: I believe so, yes.

MR. BROWNE, Q.C.: Okay. Are you familiar with the Rate Stabilization Plan?

MR. MIFFLIN: I am aware of it, yes.

MR. BROWNE, Q.C.: From an industrial perspective, are

you aware of the consequences for your industry within the Rate Stabilization Plan if one member of your class of industrial customers exits the system that you as one of the remaining customers could be responsible for their portion of the plan, are you aware of that?

MR. MIFFLIN: That's correct, yes.

MR. BROWNE, Q.C.: You're aware of that liability?

MR. MIFFLIN: I am.

MR. BROWNE, Q.C.: Does that have any concern for you?

MR. MIFFLIN: Well, it does, it has significant concern. It really ... I get more concern when I hear Mr. Backus talking about becoming a high cost mill, and you know, my blood pressure went up a bit after that testimony, but I am aware of it. It's not a pleasant prospect to think that all the parties to the current plan may not be there to fund that deficiency.

MR. BROWNE, Q.C.: From the consumers' perspective, your own customers, where consumers of electricity have the benefit of a Rate Stabilization Plan which effectively defers cost into the future. How do you see that from a competitive perspective where you're into the home heating business, Newfoundland Power is into the home heating business and indeed Newfoundland Hydro is as well, where people are not paying for their electricity costs as they go, there's a deferral there in payment?

MR. MIFFLIN: I'll answer it two ways. It depends on what hat I'm wearing. If I'm wearing my marketing hat and there's an apparent subsidy of the electricity rates to keep them in a high oil price period, the electricity lower than it would otherwise be, I would suggest that even in those circumstances oil is cheaper, but having said that, the pendulum swings around again and oil is very cyclical, so the electricity customers will be paying for that higher priced oil in their electricity rates, even in the lower oil price cycle, and that just makes us much more competitive, so from a ... you know, so although in the short period there may be some element of subsidization that a strict oil customer wouldn't have and the strict oil customer would get all the shocks, it does come around eventually. If I switch over to my refining side, I'm one of those customers that's a very big consumer of electricity and I do enjoy the effect of the smoothing, particularly when you have a large expensive operation like ours.

MR. BROWNE, Q.C.: From the industrial perspective?

MR. MIFFLIN: From the industrial perspective. Wide swings in costs are not good for business. You really want to have a stable cost structure in order to be able to run your operation properly. Wide swings, you know, we get the full impact of the oil price when we're buying the product, but on the electricity side, again, the pendulum will swing and that smoothing makes those costs a lot more even for our manufacturing operation over the long term.

MR. BROWNE, Q.C.: From the consumers' side, again, your customers side, do you see the Rate Stabilization Plan as a form of unfair competition, a subsidization?

MR. MIFFLIN: I hadn't looked at it that way. I hadn't looked at it that way and really hadn't given it any particular consideration. It may be suggested that in a low oil price time when the rate subsidization is trying to collect high oil price periods in a low oil price time that I have a competitive advantage, so ... but I hadn't given it any thought, no.

MR. BROWNE, Q.C.: You're the chief financial officer of a large company. Can you tell us a little about your budget process, your capital budgeting process? On an annual basis I would imagine you have a capital budget in place year over year, do you?

MR. MIFFLIN: Yes. Excluding capitals it's about $35 million a year.

MR. BROWNE, Q.C.: $35 million a year?

MR. MIFFLIN: Yes.

MR. BROWNE, Q.C.: And how do you determine projects on a go ahead basis?

MR. MIFFLIN: The capital process is frankly very rigorous. Capital dollars are scarce, and there's a very ... competition for those capital dollars is also very aggressive. In a general sense, what we're looking for are we prioritize all of our projects so that the ones that meet our strategic goals get the higher priority. One of those strategic goals, of course, is profit, and the sort of floor for acceptance for any project would be an internal rate of return of 30 percent or more, which is about a three year payback. If you're at the 30 percent return you probably won't get your project approved because there's people, you know, ahead of you with a 40 percent return or a 50 percent return.

MR. BROWNE, Q.C.: Can you tell us about the approval process? This Board here has the burden of approving Newfoundland Hydro's capital budget, and just from a private enterprise perspective can you tell the Board a little about the approval project (sic.) that you would go through?

MR. MIFFLIN: Each department will go through its capital requirements and they go through a ...

MR. BROWNE, Q.C.: Excuse me, Mr. Mifflin, can you speak up a little?

MR. MIFFLIN: Each department goes through a very vigorous competition for funds within their own

department, and most of the projects get filtered out or vetted at that point. Any projects that make it through that screening process get collected and presented to the ... to essentially the managers, and then there's a competition among the managers to make sure that the priorities suggested by another manager with respect to a project and the return is correct in the circumstances so that, for example, if you and I are competing for $100,000 I want to make sure that I get as much of that 100,000 to get my projects off the ground before you do, so it's a very vigorous, competitive process to make sure that projects are justified, supported, the benefits are properly outlined and they go through very rigorous screening. At that point then it goes to our board and they go through a similar process where they make sure that they meet the priorities that we need as a company and that any projects are properly justified and supported with ... and they have to be justified in a whole bunch of things. You have to not only look at the financial return, but there are other benefits. For example, what safety objectives do you want, what environmental objectives are you trying to achieve, are you trying to achieve operational savings, and then similar to Mr. Abitibi, those projected savings on operations would be deducted from next year's capital budgets ... operational budgets.

MR. BROWNE, Q.C.: In terms of computers and your purchase, do you purchase or lease your computers?

MR. MIFFLIN: We lease them.

MR. BROWNE, Q.C.: And just give them up at the ... have you done an analysis of that which is better, to lease or purchase?

MR. MIFFLIN: We have. We've gone through a very rigorous process and we lease all of our computers, and essentially, we turn them over every three to four years. We have a contract with one of the computer, fairly large computer companies and we turn them over on a regular basis. They do all of our maintenance, that sort of thing.

MR. BROWNE, Q.C.: Because if we can go to Newfoundland Hydro's ...

MR. NOSEWORTHY, CHAIRMAN: Excuse me, Mr. Browne.

MR. BROWNE, Q.C.: ... capital budget project is over $50,000 ...

MR. NOSEWORTHY, CHAIRMAN: Excuse me, Mr. Browne. The absence of any objection here, we gave leave to Mr. Mifflin here on a very specific piece of evidence. I wasn't aware that Mr. Mifflin was going to get into any of these areas or that line of questioning was going to be brought forward actually. I think we've been ... I've been fairly tolerant to date. We strayed, I think, from the evidence as before us considerably. I would ask you to either bring it back on the evidence or to clue up your questions please in this area.

MR. BROWNE, Q.C.: Thank you, Mr. Chairman. I guess that's the lawyer coming out of me. If you see a witness in front of you you're going to get whatever you can out of him. Well, there's just one question that I would have for you which may be of some assistance in, just in that budgeting process. I'll ask you one last question. If you can go to **B-74** for a moment, please? It's just in these hearings there's always some discussion concerning replacement of vehicles and when they need to be replaced. Just as one last questions, can you tell us your practice? You must have a number of vehicles, a fleet there of some sort. What's your practice?

MR. MIFFLIN: With respect to the movement of product we hire a person who's good on that side, so all of the fleet, the large bulk delivery trucks, there's independent contractors who handle those. There's two other sets of fleet vehicles, one is the sales vehicles. We generally lease those for the sales people, I think three years, because they tend to ratchet up the miles fairly quickly, and on the refinery vehicles we evaluate it every ... we evaluate each vehicle yearly, but at the end of a lease period, which is usually four years, we'll then evaluate whether we buy out the lease and keep the vehicle until it's usefulness is marginal or we'll return the vehicle back to the rental company and lease a new one.

MR. BROWNE, Q.C.: But you operate on a lease basis for vehicles, as well?

MR. MIFFLIN: We do.

MR. BROWNE, Q.C.: Okay. Thank you, Mr. Mifflin. Thank you, Mr. Chairman.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Browne. Mr. Kennedy?

MR. KENNEDY: Thank you, Chair. Mr. Mifflin, you've raised this one narrow issue in your pre-filed evidence regarding the amount of the cap that Hydro is proposing under its contract with the refinery, but I note under the provision, it's Article 9 of that contract, which I think has been filed, and it's 9.04 is the relevant provision, and 9.04(2) is the offensive clause, I guess, the one with the $1 million cap for a single occurrence, but I just wanted to ask you some questions about 9.04(1) first. That initial paragraph under 9.04 states that Hydro shall be liable for only direct loss or damage to the physical property of the customer, and then it says the customers agrees that for the purpose of this clause that direct loss or damage to the physical property of customer shall not be construed to include damages for inconvenience, mental anguish, loss of profits,

loss of earnings or any other indirect or consequential damages or losses. Just before I ask the question, in your pre-filed testimony, soon as my computer comes alive here, you've provided a listing of the quantification of the two damage claims that you speak of specifically, and if I can just find the charts on ... one of them is on the bottom of page 4. Stretching over to page 5, that's the roughly $2 million claim, and I notice in that compilation there's, for instance, loss of profit, $130,000 US, and production losses of 1.29 million, and in the other claim which I believe is above that, yes, just at the bottom of page 3 beginning of page 4, Mr. O'Rielly, you have loss of profit, 68,500 and then there's a production loss, including yield loss and lower feed rates of 11,000,124. Now, I'm not going to ask you for your legal opinion, but it's, I'd suggest, possible that some of these claims that you're currently listing here in this agreement would, regardless about the $10 million or $1 million cap, be potentially excluded from being claimable against Hydro under the proposed language under 9.04(1)?

MR. MIFFLIN: That's possible, yes.

MR. KENNEDY: Okay, and I guess can you provide us with some information about what, if any, participation Newfoundland Refinery had in negotiating or working out the language of this provision and in turn the entire contract that's bring proposed?

MR. MIFFLIN: You mean the current working of Clause 9?

MR. KENNEDY: Yeah. Well, I guess we could start from the general and move down to that specific, and I'm not looking for actually the specific, I'm looking more for the general about whether Newfoundland Refinery through its representatives entered into some process of negotiation or discussions with Newfoundland Hydro concerning the terms of this contract?

MR. MIFFLIN: Yes.

MR. KENNEDY: Okay, and so would Newfoundland Refinery through its representatives have negotiated the language of some of these provisions that are included in the contract?

MR. MIFFLIN: Yes, they would have.

MR. KENNEDY: Okay.

MR. MIFFLIN: As part of the negotiation process, yes.

MR. KENNEDY: Okay, and for instance I notice under Article 12 of the contract there's what you would refer to as the cross indemnity provision. The customer, being Newfoundland Refinery, indemnifies and holds Hydro harmless from any claims that it may sustain as a result of something you do wrong, and vise versa, Hydro indemnifies you against any claims you may sustain by third party as a result of something Hydro does wrong?

MR. MIFFLIN: Okay. I don't have it in front of me.

MR. KENNEDY: Okay. No, fair enough, but the language that I spoke of in 9.04, for instance, the excluding from the definition of direct loss or damage, damages for inconvenience or mental anguish, would this have been terminology language that was subject to discussions or negotiations that took place between Hydro and ...

MR. MIFFLIN: Our legal counsel, yes, it would have been.

MR. KENNEDY: Okay, so I guess it sort of begs the question then if this contract is as a result of a process of negotiation between Newfoundland Refinery and Newfoundland and Labrador Hydro and how is it that the Board knows where to step in and make a decision about a specific provision in that contract?

MR. MIFFLIN: The Board becomes aware of where to step in as a result of the process to get me at this table today. The negotiation process finished when Hydro said that's as far as we're going to go with respect to that clause, and we're not finished negotiating because we're saying you've got a ceiling in there and there should be no ceiling, should be no ceiling on Hydro's negligence, and Hydro's ... you know, and I want to continue to talk about that no ceiling, $1 million ceiling, and Hydro is saying, well, I don't want to talk about it any more, so at that point ...

MR. KENNEDY: Okay.

MR. MIFFLIN: ... the Board understands that there is an impasse and that specifically and particularly my circumstance, that's a very important issue.

MR. KENNEDY: So I can appreciate that the clause, as it's being proposed under 9.04(2) is offensive to Newfoundland Refinery. I guess the question I have though is how is it ... how does the Board not know whether that was being put in by Hydro as the quid pro quo for a concession that they made on another provision of the contract? You know, if the contract is treated on a global perspective, some sort of global negotiation or global settlement of all the issues within the contract, isn't it difficult then to isolate a particular issue and then ask the Board to wade in on that particular issue without being conscious or having knowledge of the overall negotiations that took place between the parties?

MR. MIFFLIN: I'm not sure how to answer your questions. I mean, it's speculative. The ...

MS. HENLEY ANDREWS: I don't think ... Mr. Chairman, I've been going to interrupt, in any event, but I mean Mr. Kennedy is asking questions with respect to potential legal consequences which is outside the area of expertise of Mr. Mifflin. If he wants to ask Mr. Mifflin what he knows or to what extent he participated in the negotiations, then Mr.

Mifflin can answer with respect to what he knows, but you know, the question really is quite speculative, and I presume that at the end of the day the parties will present their positions to the Board on how the Board should consider that issue.

MR. KENNEDY: I respect the statement of counsel for the industrial customers. Maybe I can ask the question, rephrase the question slightly and get the desired effect, if you will. Do you have any knowledge, Mr. Mifflin, of whether this issue of the cap on liability was a new issue that was raised at the end of the negotiations that took place between Newfoundland Refinery and Newfoundland and Labrador Hydro, or was it an issue that was in play during the entire set of the negotiations over this contract?

MR. MIFFLIN: That question is more properly directed at our legal counsel, Janet Andrews, but it was certainly during Hydro's cross-examination they did point out that it was not on the table at the beginning of the negotiations and it did get entered into the contract laterally. Certainly from the refinery's point of view, one of our objectives from the beginning was the insertion of and the recognition that reliability is a very key component of our relationship with Hydro, A, and B, that we, I guess, asserted from our initial discussions going into the contract negotiations that this whole matter of Hydro's liability with respect to their own negligence was high on our list of, you know, objectives that we needed to achieve. The point at which the negotiators actually tabled and strategized about tactically when to put things in or out and Hydro used to tactically move things in and out of the negotiation process, I was not part of that and I can't comment on it, but I will say that the issue of liability and that cap on liability is important and it causes us considerable concern. It puts more risk on us than we need with respect to that issue, and it was something that we had felt very strongly about before we went into the negotiations. I don't know if that helps or answers your question.

MR. KENNEDY: That helps. Thank you, Mr. Mifflin. That's all the questions that I have, Chair. Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Kennedy. Ms. Henley Andrews, redirect, please?

(3:15)

MS. HENLEY ANDREWS: I just have a couple of questions. Mr. Mifflin, in terms of North Atlantic's position on a cap on Hydro's liability for negligence, if a power outage occurs of longer than whatever the minimum amount of time is, occurs in spite of Hydro's best proper treatment of its system, let's assume a tornado goes through, you're not asking Hydro to bear your losses in that circumstance, correct?

MR. MIFFLIN: That's correct.

MS. HENLEY ANDREWS: You're not asking Hydro to bear your loses in that circumstance, correct?

MR. MIFFLIN: That's correct.

MS. HENLEY ANDREWS: So you're only asking Hydro to cover those headings of damage if Hydro is negligent?

MR. MIFFLIN: Correct.

MS. HENLEY ANDREWS: And you heard Ms. Greene suggest in answer to a question from counsel for Newfoundland Power that if Hydro had to pay a damage award resulting from its own negligence out of its own pocket, then it would be seeking to recover that amount from its ratepayers. As a ratepayer of Newfoundland and Labrador Hydro's how would North Atlantic feel about an amount included in its rates resulting from Hydro's negligence?

MR. MIFFLIN: You're asking that if Hydro were negligent and paid us that we would then fund out own negligent claim through the rate in the future?

MS. HENLEY ANDREWS: That's right.

MR. MIFFLIN: Yeah, and the answer is that that's improper. Hydro should be taking that out against their own bottom line and it's not a matter of something that should be passed on to any ratepayer.

MS. HENLEY ANDREWS: Okay. At ...

MR. MIFFLIN: That's my view, sorry.

MS. HENLEY ANDREWS: One other question, and, Mr. Chairman, it has to do with Mr. Browne's questions on the RSP, and I think it's important for clarification since the questions were asked and answered. It's only one question, and that is, do you agree ... wearing your industrial customer hat, do you agree with the RSP as it now stands?

MR. MIFFLIN: I can't speak to the real detailed specifics of the plan. It's very ... it's an unusual, complicated plan. There's three elements to it, as I understand. There's load, water and oil, and they don't mix, and the issue of the load, I'm not sure why ... I mean, that's a keep hold provision for Hydro in all circumstances, and I don't see how that crept into the ... this is, again ... I don't see how that crept into the plan in the first place and it should be expunged. The matter of water and oil are now so combined that you really can't determine the impact of one as against the other, so if you have a high oil price offset by high water they really ... you really can't tell the impact of the plan of the water versus the oil. The second thing is that water seems to me to be a longer term event that should probably be amortized over a longer period of time and oil is much more faster,

more cyclical and it should be, you know, down to maybe two years, but really, the elements of the plan should now be ... you know, am I happy with the plan? The answer is no. The concept is fine, but the way it's constructed is not appropriate in my view. I don't know if that answers your question.

MS. HENLEY ANDREWS: That answers my question. Those are my questions. Thank you, Mr. Chairman.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Henley Andrews. We'll move now to Board questions. Commissioner Powell?

COMMISSIONER POWELL: Thank you, Chair. I only have a couple of points on the insurance. Mr. Mifflin, you're a chief financial officer of a fairly large corporation. Would you think it's prudent that a company such as yourself or Hydro that it was going to expose itself to an unlimited liability should have some sort of an insurance provision to cover it?

MR. MIFFLIN: If you have a risk in terms of your operations then you have to figure out, as your company, how you want to deal with that risk and what the frequency and the magnitude of the risk is. In our case, we insure against most of the risks that we have, so we do have business interruption, we do have property damage, we do have liability, we have theft, we have, you know, product loss insurance, we have product failure, you know, negligence insurance, so even though we have procedures in place to manage and to mitigate the possibility that an event can happen through controls and procedures and policies and other things, there is still an element of risk and we feel it prudent to ensure against that risk. Now, other enterprises may deal with that risk in a different way by self-insuring or determining another way to deal with ... you know, adding even more procedures, but we have done both.

COMMISSIONER POWELL: But it would be prudent?

MR. MIFFLIN: Absolutely.

COMMISSIONER POWELL: To have some form of insurance, whether it's internal or external that's a costing exercise that you would go through using experts to give you the parameters in which you should measure those risks?

MR. MIFFLIN: Correct.

COMMISSIONER POWELL: Okay. You, as you said, that Come By Chance is a unique customer of Hydro in the sense that there is only one refinery, and you have probably some unique demands on Hydro because of the way you operate, so if Hydro were to let the revision in a contract to have a higher limit or an unlimited liability for damages they would have to go and either to ... prudence would dictate they would either put a mechanism of self-insuring within their system or purchasing the insurance. Would that not, from a regulatory point of view, be a specifically assigned cost to your operation because it would be put in specifically for you because of your uniqueness?

MR. MIFFLIN: I don't think so. What the issue ... there's two issues. One is are they accepting responsibility for paying damages in respect of their own negligence, and the answer is yes. Most of the customers ... and what they've done is they've covered, by placing in the $1 million cap, they've essentially taken in 90 percent or 99 percent of the customers and they're paying them 100 percent of loss in respect of a potential claim. What they've done to us is specifically excluded us and said we understand your operations are unique, we understand that you ... if we were a normal commercial enterprise we could not put in a cap. For example, if they're an oil refinery we can't impose a cap on our customers. What they've said is that instead of treating us like other ratepayers they're excluding us, and we're saying even though the potential for a single occurrence event is greater than $1 million we're going to limit you as against your losses or your losses as a result of our own negligence, and so it's discriminatory in its application.

COMMISSIONER POWELL: But if they said we're going to erase the discrimination if they were to allow unlimited ... and they acquired a mechanism to ensure that specifically for North Atlantic, my question is from a regulation point of view that should be a specifically assigned cost to North Atlantic because of the cost incurred specifically for your potential liability?

MR. MIFFLIN: I don't agree with that. I think the treatment of particular damages for me, my damages may well be less than $1 million, and in fact I don't think with respect to Hydro's operation we've had an incident since 1987 or `88 ... sorry, wrong year. `97 or `98, so we've had a long period now of very clean reliable operations from Hydro.

COMMISSIONER POWELL: So therefore the insurance costs based on that should be relatively low?

MR. MIFFLIN: Absolutely, yes.

COMMISSIONER POWELL: One other question. You personally have a contract with Hydro?

MR. MIFFLIN: Yes.

COMMISSIONER POWELL: I noticed in the draft contract it has an arbitration clause for disagreements and disputes within the contract. Is there anything in the present contract under the arbitration section that would allow for some sort of an arbitration process to come into play where

there's a condition, difference between the old contract and new contract to resolve this issue rather than us?

MR. MIFFLIN: No. There's no bridging, there's no bridging provision.

COMMISSIONER POWELL: Okay. Just a thought. That's all my questions, Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Commissioner Powell. Commissioner Sanders?

COMMISSIONER SAUNDERS: Just one, I think, Mr. Chair. Mr. Mifflin, good afternoon, and it may be something that Mr. Powell mentioned, because I didn't have any questions before he asked his last one, but Hydro has proposed a contract to your company which, amongst other things, includes a price for the energy that they have said they will supply you. One of the other provisions is that they propose as well that $1 million cap that's dealt with in the insurance ... or liability provision. Have you offered or has Hydro proposed a higher rate for what it is you want to achieve in respect of the liability?

MR. MIFFLIN: No.

COMMISSIONER SAUNDERS: There hasn't been any discussion in respect of?

MR. MIFFLIN: No.

COMMISSIONER SAUNDERS: You're not prepared, I gather then to pay a higher rate for what you want in terms of their liability coverage?

MR. MIFFLIN: I don't think that it is a specifically assigned charge, no.

COMMISSIONER SAUNDERS: Okay, I see. Okay, Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Commissioner Saunders. Commissioner Whalen?

COMMISSIONER WHALEN: Yes, I, like Commissioner Saunders, thought I didn't have any questions but now I do. I find this is a very difficult issue, I think, for me as a commissioner, I think, to deal with now, and I echo Ms. Butler's comments that it's so late in the process that I think had this come up earlier I think I would have had a lot more questions throughout the entire process about this and perhaps would have asked some questions of other witnesses, but having said that, I'm intrigued by Mr. Young's observation at the beginning of his cross-examination that you're a unique customer and Hydro is the only supplier of electricity, and under legislation they have no choice but to supply you and you have nowhere else to go to get your electricity, so here we are. I guess I'm ... the whole issue of the liability and the cap, I'm not sure that I appreciate what the concern is. I mean, I appreciate the concern that, you know, the cap in terms of $1 million versus ... and you've got a $19 million ... one claim alone that's $19 million, but in terms of what portion of the responsibility for the liability, I guess, rests in North Atlantic Refining in the sense of I heard a three minute window is what we're dealing with, is three minutes where it turns from a zero dollar cost to potentially a 19 or 20 million dollar liability. Is that really what I heard, that that's what we're dealing with, that's your window?

MR. MIFFLIN: That's our window. If we have a power loss at that point, at that point the refinery will go into an emergency shutdown. I mean, this is an unusual situation as a refiner, as an industry coming to this province. This is not something that another refinery in anywhere else in North America has to ... it doesn't even come on the table. It's not an issue that if I was a refinery going into New Jersey, going into Sarnia, I wouldn't even think of it, and in fact when our current shareholders came here it's not something that they would ... it's something that didn't even enter their minds because it's not an issue anywhere else in North America. We've come here, we've invested our money and the Crown corporation that's responsible for providing that power was found not to be reliable. Now, we went into a very ... we've met numerous times, a very good relationship with Hydro with respect to their reliability issue and in the last few years with reliabilities has been absolutely marvellous, but the consequence of that window of opportunity, once that ... it's very ... it's a dangerous situation. They have three minutes in order to make that decision. At that point they have to go to emergency shutdown. I can't recall other refineries in North America going through that process and being subjected to those operating circumstances and those losses anywhere else in North America.

COMMISSIONER WHALEN: Why isn't it an issue with other refineries, is it because of the utility or is it because of the processes that those refineries use or ...

MR. MIFFLIN: Our refinery is probably one of the ... it was built in 1976 using, you know, using modern codes that are used today. There's been no refinery, I don't think, in North America built since our refinery, so it's not an ... you know, we're not an old, crepitant refinery, but it does ... and the circumstances under which we operate our refinery and the circumstances of a loss of power in our refinery is no different from any other refinery. It comes down to a matter of reliability, and certainly I'd have to let Hydro offer as to what those circumstances are, but one of the issues may be the fact that the North American grid is a little more interconnected, so if one area declines another grid section can make it up, but that's beyond my expertise. My concern here is that there is a possibility that I would have damages greater than one million, and if it results from a tornado or a hurricane or something that's beyond Hydro's

control, that's not what I'm asking for, but if Hydro are negligent should I suffer damage or be limited in my damage as against any other ratepayer, and the answer is no.

COMMISSIONER WHALEN: Yeah, I think it isn't... I don't have ... I don't think I have as much an issue with that aspect of it. It's more the ... it's probably the magnitude that comes out at you that I have a question about, and I guess my only other question deals with because the impact on your operations is so severe and so time sensitive, have you explored, recently, the idea of putting in your own generation source, has that come up?

MR. MIFFLIN: The last time we looked at co-generation was the period, I'm not sure what time period, when Voisey Bay were ... when Hydro put out tenders to look for additional ...

COMMISSIONER WHALEN: That's a couple of years ago.

MR. MIFFLIN: And we looked at it very ... in fact, we invested, you know, a million or so dollars in a proposal to do a co-generation using a gasification process, but again, the requirement for that load or that generation is not there, and so the proposal is dormant. In the meantime, we've used capital to improve the refinery itself, and so we haven't explored it since that time, and sorry, and then to add to that I will say that reliability in the last several years, we've not had any issues with ... in fact, we were meeting with Hydro, I think, every single month for a period of time, and now we've ... because of the reliability issues and to make sure that we were talking to each other. We're now down to meeting every semiannually, so Hydro has been very responsive and that.

COMMISSIONER WHALEN: And there's nothing that North Atlantic Refining can do in terms of its processes or its system or plant itself to widen that three minute window of going into emergency shutdown to five or ten so that you actually have more time to assess what's actually happening?

MR. MIFFLIN: No. It would be several hundreds of millions of dollars to do that.

COMMISSIONER WHALEN: Okay. That's all the questions I have. Thank you, Mr. Mifflin.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Whalen. I had a couple of questions but I think both of them have been answered. Mr. Mifflin, I think you said earlier, as I recall, you did say there were no incidents since '97 of this nature, is that correct?

MR. MIFFLIN: I would say 199- ... either seven or 1998, and since that time we've had no ... I believe that to be the correct time period.

MR. NOSEWORTHY, CHAIRMAN: The other question I had related to precedents elsewhere and I think you've answered that just a little while ago. This is a question that I didn't have but Mr. Saunders was good enough to pass it on to me so I'll ask it in any event. Is there a rate that, I guess that North Atlantic Refinery is willing to pay and Hydro is willing to accept that provides this coverage and gives Hydro a satisfactory rate? I think I know the answer from what you've said, you're at an impasse and you're not, there doesn't seem to be any middle ground, but I'll let you respond to that.

MR. MIFFLIN: I don't think my, I don't think my response will change. I just want to go back and say that I don't think there should be any ... fundamentally there should be no cap, there's no cap on my, the liability in respect to my own negligence, and there shouldn't be any here, and if the system is reliable and if there's proper processes and procedures in place, then that mitigates a good, significant portion of the risk. It may be that some other portion of the risk could be insured against. One of the other measures that can be put in to mitigate the risk is to put a ceiling on it, and the ceiling in our view should be a minimum of $10 million, and not $1 million, and that makes it easier to manage that risk in any event. The price that we're paying is the price that is similar to all ratepayers, and I would argue that if a ratepayer, the issue of negligence has been accepted by Hydro, what we're talking about there is should one ratepayer be excluded from getting, or discriminated against in respect of recovering their damages, so if 99.9 percent or 99.5 percent of their ratepayers are getting 100 percent of their damages, and you come to a significant enterprise like ourselves where we can't, where our business risk is significantly greater than that of Hydro, then Hydro is asking us to assume a greater portion of the business risk that Hydro should have in respect of their own negligence. Now I have enough business risk now in the oil industry without assuming that additional business risk by a regulated enterprise which can apply for and get approved for its rates. I can't do that.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Mifflin. It's 20 to 4:00 now. We normally break well before this but I was hoping to conclude. I suspect there are some questions on matters arising, so I think we'll ...

MR. YOUNG: Just a couple, that's all as regards to ...

MR. NOSEWORTHY, CHAIRMAN: Okay, well we'll try to push it through if there's only a couple.

MS. GREENE, Q.C.: That's only from Hydro's perspective now. I don't know about the other counsel.

MR. NOSEWORTHY, CHAIRMAN: No, okay, we'll try it and give Mr. Mifflin the benefit of leaving if he so chooses. Mr. Young.

MR. YOUNG: Thank you, Mr. Chair. Mr. Mifflin, just a couple of questions. The first one relates to a question that you were asked by the panel, and I believe it referred to the experiences of refineries in other provinces or other places in North America, and then there was a follow-up question by the panel which seemed to refer to the contractual circumstances that refineries face in other jurisdictions, and I'm not sure if you ever intended to answer the second one because of the way the question was posed.

MR. MIFFLIN: Correct, I cannot comment on the contractual circumstances of refineries in other jurisdictions, you're correct.

MR. YOUNG: Okay, and may have misheard the question because I was confused on that one. My only other question relates to your use of the word discrimination because Hydro is charging the same rates and is applying the same clauses with the same cap. It strikes me that you're using the word discrimination from the point of view of it having a different magnitude when you pass it on to you as a customer from a risk point of view, not terribly different. I would suggest to you than one customer saying well it's all very well for you to charge me that many mills, but with my load that will cost me more money, and it's the same kind of thing, is it not?

MR. MIFFLIN: It's completely different. I'm paying ...

MR. YOUNG: You really think that this is a discriminatory approach that we're taking?

MR. MIFFLIN: I'm not arguing about the fact that I have more consumption than you do in your household and I'm paying for that and that's built into the contract. I'm saying as a result of your negligence, if I suffer a loss, not only do I bear all of my own risks but I'm also bearing the portion of your negligence, the damage to my property as a result of your negligence that you are going to not cover because of the ceiling and I think that's discriminatory. Now maybe I'm using a wrong word. I could probably find a stronger word but I'm ...

MR. YOUNG: Yeah, I mean it occurs to me that we provide the power and the energy at the rate and it has different effects on different people, but I mean to call that discriminatory in effect, well it stretches that word, at least, beyond what we understand the word to mean in this setting, a regulatory setting. That's really all the questions I had, thank you, Mr. Mifflin.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Young. Ms. Butler please?

MS. BUTLER, Q.C.: Mr. Chairman, I have no questions.

MR. NOSEWORTHY, CHAIRMAN: Thank you. Mr. Browne?

MR. BROWNE, Q.C.: Yeah, that discrimination that you're referring to has caught my attention. Are you claiming you're being discriminated against because I think you used the example in reference to one of your answers there, that if there's a power surge and someone gets their refrigerator knocked out, they make a claim and Hydro gives them another refrigerator, whereas they won't give you your value, is that what you're stating?

MR. MIFFLIN: Yes, that's the essence of it. Maybe discriminatory might be strong. The concern ...

MR. BROWNE, Q.C.: That's the nature.

MR. MIFFLIN: The nature of it is that we potentially have, the consequence of something like that, it will expose us to damages that may exceed the $1 million. The probability that it will exceed the $10 million on any one occurrence is less probable, but it's highly probable that it's going to be more than $1 million. For most of Hydro's customers, I would argue that the $1 million will fully fund 100 percent in all probability all the losses with respect to their other customers, but the reason for our application is that we're caught in a circumstance that physical damage to the plant, to the refinery is much more probable to be greater than $1 million and less probable to be more than $10 million.

MR. BROWNE, Q.C.: Yeah, I understand that but where are you getting your evidence to suggest that Hydro is paying out 100 percent of their other smaller claims to ordinary consumers?

MR. MIFFLIN: There is no evidence, I'm speculating that most ... and I sort of gleaned it from the discussion from Hydro. I can't state what the damages that all Hydro customers could be potentially exposed to. I'm really here representing my case that the $1 million is inadequate.

MR. BROWNE, Q.C.: Because there was evidence when we were in Labrador, and some people came forward to say they weren't paying out claims in reference to the destruction of appliances because of power surges and blips and the like, so I don't know if that gives you any consolation, but they mightn't be paying out any claims. Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Browne. Mr. Kennedy?

MR. KENNEDY: No questions, Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you, re-direct, Ms. Henley Andrews?

MS. HENLEY ANDREWS, Q.C.: One question. Commissioner Saunders may have mentioned, and then the Chairman also mentioned this concept of a premium or a

rate or an extra payment in order to get a higher cap, and there was a suggestion I think, or perhaps an assumption that that might have been discussed, that concept might have been discussed between the parties. To your knowledge, has the issue of any payment for a higher cap ever been discussed?

MR. MIFFLIN: To my knowledge it's never been discussed.

MS. HENLEY ANDREWS, Q.C.: Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Henley Andrews. Thank you very much for your testimony, Mr. Mifflin. It's now 10 to. We'll take a 15 minute break and return with the capital budget please.

(break)

(4:15 p.m.)

MR. NOSEWORTHY, CHAIRMAN: Ms. Greene, I wonder could I ask you to speak to the December 28th application please?

MS. GREENE, Q.C.: Thank you, Mr. Chair. This is Hydro's third application with respect to its capital budget for 2002. Hydro filed the original, of course, as part of the May 31st filing, and that submission was made in accordance with Hydro's past practice since its first budget was approved in 1997, and when it became clear to us that we would not finish the rate hearing in sufficient time to allow the Board to consider all matters including the capital budget prior to year end, we filed the second application with respect to the capital budget on November 20th, and at that time Hydro had sought an order approving all parts of the 2002 capital budget which were not objected to by the other parties. The other parties did file replies in response to the application of November 20th setting out their position on projects over $50,000, projects under $50,000, and leases as well. When the Board issued the order on December 20th, and that's order number PU-30, the order dealt specifically with projects over $50,000, and I guess in light of Hydro's past practice before the Board and in the way in which the original application was framed, as well as as the November the 20th application, that created uncertainty, at least in Hydro's mind with respect to the directions of the Board. It is our submission that in light of the fact that the other parties have set out objections to only certain projects under $50,000 listed in Section A and have not objected to any of the leases in Section D, that we are asking the Board to consider approving those as well and that is those projects under $50,000 which have not been objected to by any party and all of the leases in Section D.

I would point out that this is consistent with how Hydro has treated its past capital budgets and it has not proceeded with even projects under $50,000 without the prior approval of the Board. It is my understanding that the other parties are consenting to this application as well, so at this time I will make no further comments, but I think I've outlined what our position is at this time.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Greene. Mr. Alteen?

MR. ALTEEN: We don't have any issue if the Board chooses to grant the order requested in the application, Mr. Chairman, I would just point out two things. One is there is no prohibition in the Public Utilities Act, and particularly under Section 41, which would in any way restrain Hydro from commencing capital projects that are listed in the 2002 budget but not objected to, which are less than $50,000. That is our view of the effect of ... I think it's 41(3)(A). With respect to the second part of the application, which is the approval of leases, it is my understanding that each and every one of the leases set out in, I believe it's Schedule D to the capital budget, has been previously approved by the Board. Now I understand Hydro's practice is to bring those forward each year for reapproval. It is Newfoundland Power's position on this that once approved, it's approved. It doesn't have to be reapproved. However, given our interpretation of the Act, it may not be shared by the Board, we would not stand in the way of the order requested by Hydro, but we would not see it as necessary.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Alteen. Ms. Henley Andrews?

MS. HENLEY ANDREWS, Q.C.: Mr. Chairman, we would consent to the order requested by Hydro given that all of the parties had indicated that they had no objection to those particular projects. I don't see any difficulty with it, and although I do appreciate and agree with what Mr. Alteen has said, I suppose there would ... I also understand Hydro's caution because there would always be the possibility that a party might object that Hydro had broken down one project into three in order to get it under the $50,000, and that would raise a problem for them if it was objected to later, so I do think that they're not being over-careful in asking for the order.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Henley Andrews. Mr. Browne?

MR. FITZGERALD: Mr. Chairman, we consent to the application of Hydro.

MR. NOSEWORTHY, CHAIRMAN: Thank you. Mr. Kennedy?

MR. KENNEDY: Chair, it seems the application raises an issue which seems to turn on the interpretation of Section 41 of the Public Utilities Act and what specifically requires Board approval and what doesn't and also, I guess, in relation specifically to the leases. When a utility receives

approval in one year for a lease, whether it requires subsequent approvals in each year, or whether once a lease is approved it's approved, I think that the Board may be able to assist Hydro and in turn other parties if it rendered an order or decision that provided its interpretation of those provisions specifically, so that that would provide comfort to Hydro. I'm assuming that that's based on the submission of Hydro, what the purpose of this application, that it hasn't taken that comfort in interpreting the sections themselves and so is seeking confirmation from the panel about how it interprets the provisions so that it can go forward from that point. That's all the comments I have, Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you very much. Any comments on anything, Ms. Greene?

MS. GREENE, Q.C.: Yes, Mr. Chair. I just wanted to read Section 41.1 of the Act. It says that a public utility shall submit an annual capital budget of proposed improvements or additions to its property to the Board for its approval not later than December 15th. I don't think there's any doubt that at some stage the Board has to approve all of the capital budget for Hydro or for any utility. I know there is a difference in Section 41.3 which says that a public utility shall not proceed with the construction, purchase, or lease for those over $50,000 without prior approval and there may be a distinction between Section 41.1 and Section 41.3 as to what the meaning of prior would mean. However, a I said, our past practice has always been to get prior approval and in view of this hearing with the arguments that have been raised about our projects and where the issue had not been dealt with in the Board order, we thought it would be prudent. And also where it had hadn't been argued before the Board at the application that as there's no doubt the projects under $50,000 must also be approved, and where the parties had clearly indicated their approval for a number of those projects, with only limited exceptions, that it would be prudent for Hydro to seek the specific approval of the Board before it started construction of any of those projects, so I just wanted to point out there is no doubt that the Board must approve all projects, even those under $50,000, the question is does it have to be prior to commencement of the work, or can we start the work and run the risk of it not being subsequently approved, and we did not want to incur that risk in the context of a contested hearing. So as the parties have all consented to the order as requested in the light of the circumstances, and as Mr. Kennedy has pointed out, it might be helpful if, not to hold up this order, but if the Board did give direction to both utilities how they would expect the utilities to approach the capital budget with respect to both projects over $50,000 and those under $50,000 would be very helpful.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Greene. Are there any particular questions or issues that you want to ...

COMMISSIONER WHALEN: I just wanted to point, Ms. Greene, that in the application, Item No. 4, where it refers to Section A ...

MS. GREENE, Q.C.: And this is the December 28th ...

COMMISSIONER WHALEN: The December 28th application, that the projects less than $50,000, the last sentence, that the total there actually should be $1,090,000 ... that your projects less than $50,000 I don't think total $14,740,000.

MS. GREENE, Q.C.: I would have to confirm that, Commissioner Whalen. When I had talked about the 60 percent of the budget, and actually if we could bring it up on the screen, I think you will see it is a significant portion. Mr. O'Rielly, if we could look at the capital budget, and I just want to show you the sections. Of course, I also did this by myself on the 28th without anyone checking my math, so ... if you look at the first page of the budget you'll see that the total budget is $48,000,000, and then if we go to the Section B projects, which are over $50,000, which were 33, I subtracted the 33.3 from the 48.

COMMISSIONER WHALEN: I think you also have to subtract your Section C projects which are $13,650,000.

MS. GREENE, Q.C.: Oh the ... can I just see Section C, Mr. O'Rielly, and that may be, I'm sorry, Commissioner Whalen.

COMMISSIONER WHALEN: Just in terms of looking at the application and what we're actually looking, what you're actually seeking approval of. I think by my calculations it looks to be about $730,000 of uncontested under $50,000 capital projects.

MS. GREENE, Q.C.: It would be those ... if we could go back to Section A, Mr. O'Rielly, and we subtract the ... they are actually listed, and the difficulty with these is they're not in a specific section. You have to go through Section A and take them out.

COMMISSIONER WHALEN: Actually it took me about an hour to come up with that $730,000.

MS. GREENE, Q.C.: I trust your math, because as I said, when I did it I was alone on the 28th and ...

COMMISSIONER WHALEN: But just to point out that the Section C projects have been approved, and $13.5 million approximately under Section B projects have been approved, so you are seeking specifically approval of the under $50,000 ...

MS. GREENE, Q.C.: Section A projects and the ... and at this point to be consistent with past practice, the leases that were listed in Section D, because any prior year the

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

Newfoundland (Board of Commissioners of **Public Utilities**), Re

In The Matter of Section 101 of the **Public Utilities** Act, R.S.N. 1990, c. P-47

In The Matter of a case stated by the Board of Commissioners of **Public Utilities** to the Court of Appeal for its hearing consideration and opinion on questions of law affecting the jurisdiction of the Board of Commissioners of **Public Utilities**

Newfoundland Court of Appeal

O'Neill, Cameron, Green JJ.A.

Heard: March 11, 1997
Heard: March 12, 1997
Judgment: June 15, 1998
Docket: 96/141

Counsel: *V. Randell J. Earle, Q.C.* Counsel for the Board of Commissioners of Public Utilities.

Ian F. Kelly, Q.C., Counsel for Nfld. Light & Power Co. Ltd.

Mark Kennedy, Counsel for the Consumer Advocate.

Subject: Public; Civil Practice and Procedure

Public utilities --- Regulatory boards — Regulation of rates

Utilities board stated case to Court of Appeal for determination of "just and reasonable" return on rate base of utility — Board had jurisdiction to fix rate of return that public utility could earn annually — Board did not have jurisdiction to fix rate of return on common equity or shares — Board had jurisdiction to set rate of return as range — Board had broad jurisdiction to regulate how excess revenue was dealt with in situation where utility earned rate of return greater than that determined to be just and reasonable — Board had jurisdiction to define excess revenue for purpose of maintenance of reserve account and set out how excess, if not ordered to be paid into reserve account, was dealt with — In setting rate, board had jurisdiction to consider type and level of projected expenses of utility and determine whether such expenses were reasonable — Board did not have jurisdiction to require public utility to maintain debt-equity ratio or ratio within stated range — Board did not

have jurisdiction to require utility to obtain its capital requirements by issue of specific financial instruments — Board did not have jurisdiction to intrude into day to day financial or managerial decision-making of utility with respect to capital structure.

The Board of Commissioners of Public Utilities stated at case to the Court of Appeal with respect to the jurisdiction and powers of the board as they affected the board's approach to the determination of a "just and reasonable" return on the rate base of a utility. A number of question were posed.

Held: The board had broad jurisdiction with respect to the determination of a just and reasonable return on the rate base of a utility.

Per Green J.A. (Cameron J.A. concurring): The board had jurisdiction to fix the rate of return that a public utility could earn annually but it did not have jurisdiction to fix the rate of return on common equity or shares. The board had jurisdiction to set the rate of return as a range and it had broad jurisdiction to regulate how any excess revenue was dealt with in a situation where the utility earned a rate of return greater than that determined to be just and reasonable. The board had jurisdiction to define what excess revenue was for the purpose of maintenance of a reserve account and had the jurisdiction to set out how that excess, if not ordered to be paid into the reserve account, was dealt with. In setting the rate, the board had jurisdiction to consider the type and level of projected expenses of a utility and to determine whether such expenses were reasonable. The board did not have the jurisdiction to require a utility to obtain its capital requirements by issue of specific financial instruments, nor did it have jurisdiction to intrude into the day to day financial or managerial decision-making of a utility with respect to its capital structure.

Per O'Neill J.A. (dissenting): The determination of the rate on common shares of a utility is very much a part of the rate making process. Rates to be charged should provide sufficient revenue to enable the producer or retailer of the power to earn a just and reasonable return so that it is able to achieve and maintain a sound credit rating in the world's financial markets. The board had the jurisdiction to fix the rate of return on the rate base as well as the rate on common shares. Revenues generated after the rates, tolls and charges were set belonged to the utility and thus the board did not have the jurisdiction to order rebates to customers. The Board did not have the jurisdiction to set rates in a manner that would compensate for prior excess earnings.

Cases considered by *Green, J.A.*:

Acker v. United States (1936), 298 U.S. 426, 56 S. Ct. 824, 80 L. Ed. 1257 (U.S. Ill.) — considered

Bell Canada v. Canada (Canadian Radio-Television & Telecommunications Commission), 38 Admin. L.R. 1, [1989] 1 S.C.R. 1722, 60 D.L.R. (4th) 682, 97 N.R. 15, [1989] 1 R.C.S. 1722 (S.C.C.) — considered

Bell Telephone Co. of Canada, Re (1966), 56 B.T.C. 535 — considered

Bluefield Waterworks & Improvement Co. v. Public Service Commission of West Virginia (1923), 262 U.S. 679, 43 S. Ct. 675, 67 L. Ed. 1176, P.U.R. 1923D 11 (U.S. W. Va.) — considered

British Columbia Electric Railway v. British Columbia (Public Utilities Commission), [1960] S.C.R. 837, 33 W.W.R. 97, 82 C.R.T.C. 32, 25 D.L.R. (2d) 689 (S.C.C.) — considered

Edmonton (City) v. Northwestern Utilities Ltd., [1929] S.C.R. 186, [1929] 2 D.L.R. 4 (S.C.C.) — considered

Federal Power Commission v. Hope Natural Gas Co. (1944), 320 U.S. 591, 64 S. Ct. 281, 88 L. Ed. 333, 51

P.U.R. (N.S.) 193 — considered

Montana-Dakota Utilities Co. v. Northwestern Public Service Co. (1951), 341 U.S. 246, 71 S. Ct. 692, 95 L. Ed. 912, 88 P.U.R. (N.S.) 129 (U.S. S.D.) — considered

Newfoundland Light & Power Co. v. Newfoundland (Public Utilities Commissioners Board) (1987), 25 Admin. L.R. 180, 37 D.L.R. (4th) 35, 63 Nfld. & P.E.I.R. 335, 194 A.P.R. 335 (Nfld. C.A.) — considered

Northwestern Utilities, Re (1978), [1979] 1 S.C.R. 684, 7 Alta. L.R. (2d) 370, 12 A.R. 449, 89 D.L.R. (3d) 161, 23 N.R. 565 (S.C.C.) — considered

Union Gas Ltd. v. Ontario (Energy Board) (1983), 43 O.R. (2d) 489, 1 D.L.R. (4th) 698 (Ont. Div. Ct.) — considered

Wabush (Town) v. Power Distribution District of Newfoundland & Labrador (1988), 71 Nfld. & P.E.I.R. 29, 220 A.P.R. 29 (Nfld. C.A.) — considered

Statutes considered by *Green, J.A.*:

Electrical Power Control Act, 1994, S.N. 1994, c. E-5.1

s. 3(a) — considered

s. 3(a)(i) — considered

s. 3(a)(ii) — considered

s. 3(a)(iii) — considered

s. 3(b) — considered

s. 3(b)(i) — considered

s. 3(b)(ii) — considered

s. 3(b)(iii) — considered

s. 4 — considered

Public Utilities Act, R.S.N. 1990, c. P-47

s. 16 — considered

s. 37(1) — considered

s. 58 — considered

s. 59 — considered

s. 59(2) — referred to

s. 64(1) — considered

s. 64(2) — considered

s. 68(4) — considered

s. 69 — considered

s. 69(3) — considered

s. 70 — considered

s. 70(1) — considered

s. 75 — considered

s. 75(3) — considered

s. 76 — considered

s. 78(1) — considered

s. 78(2) — considered

s. 78(2)(h) — considered

s. 80 — considered

s. 80(1) — considered

s. 80(2) — considered

s. 80(4) — considered

s. 84(1) — considered

s. 84(2) — considered

s. 87(1) — considered

s. 91 — considered

s. 91(1) — considered

s. 91(3) — considered

s. 91(5)(a) — considered

s. 101 — pursuant to

s. 102 — referred to

s. 117 — considered

s. 118 — considered

s. 118(2) — considered

Statutes considered by *O'Neill, J.A.*:

Electrical Power Control Act, 1994, S.N. 1994, c. E-5.1

Generally — considered

s. 3 — considered

s. 4 — considered

Public Utilities Act, R.S.N. 1990, c. P-47

Generally — considered

s. 16 — considered

s. 37 — considered

s. 37(1) — considered

s. 58 — considered

s. 59 — considered

s. 69 — considered

s. 69(1) — considered

s. 69(2) — considered

s. 69(3) — considered

s. 69(4) — considered

s. 70 — considered

s. 70(1) — considered

s. 76 — considered

s. 80 — considered

s. 80(1) — considered

s. 80(2) — considered

s. 80(4) — considered

s. 84(1) — considered

s. 85 — considered

s. 86 — considered

s. 87(1) — considered

s. 91 — referred to

s. 101 — pursuant to

RULING on stated case.

Green, J.A.:

1 The Board of Commissioners of Public Utilities has stated a case for the opinion of this Court, pursuant to s. 101 of the *Public Utilities Act*[FN1]. The questions posed concern the jurisdiction and powers of the Board as they affect the approach of the Board to the determination of a "just and reasonable return" on the rate base of a utility, as well as related matters.

The Stated Case in Context

2 The Board is the statutory body which has the authority and duty for the "general supervision of all public utilities" in Newfoundland and Labrador and in the course of exercising that supervisory role has general authority to "make all necessary examinations and inquiries and keep itself informed as to the compliance by public utilities with the law" and, as well, it has the right "to obtain from a public utility all information necessary to enable the Board to fulfil its duties"[FN2].

3 One of the Board's primary functions with respect to electrical utilities is the regulation and approval of rates, tolls and charges[FN3]. In so doing, the Board must take account of the statutory requirement that the utility is entitled to earn annually a "just and reasonable return" as determined by the Board on the rate base as fixed and determined by the Board.[FN4] The process essentially involves the fixing and determining of the appropriate rate base, the determination of a "just and reasonable return" on that rate base and then the approval of a schedule of rates, tolls and charges that would be appropriate to generate the revenue which, in the Board's estimation, would be necessary to provide the determined rate of return. Once rates, tolls and charges are set by the Board they continue to apply until altered under the Act, as a result of a reapplication by the utility for an increase, a complaint by the public or an order for a reexamination initiated by the Board itself.

4 It is important to remember, however, that in addition to its periodic adjudicative role which itself involves a large measure of policy implementation in arriving at its decisions, the Board has, because of its duty of "general supervision of all public utilities", an ongoing supervisory role of the activities of the utility between hearings as well, which is facilitated by statutory requirements for periodic reporting of financial information to the Board.

5 In 1991 the Board made Orders[FN5] determining a just and reasonable return for Newfoundland Light

and Power Co. Ltd.[FN6] and approving a schedule of rates, tolls and charges based on estimated revenue requirements necessary to cover operating expenses and to provide that level of return. The essential features of the 1991 order determining the just and reasonable rate of return were that:

(a) The just and reasonable return was determined to be between a stated range (10.6% - 11.19%) of the company's average rate base;

(b) The rate base was determined on the basis of a hypothetical test year (1992);

(c) The Board determined that the just and reasonable return, as defined, would provide an opportunity to NLP to earn a rate of return on common equity between a certain stated range (13% to 13.5%);

(d) The schedule of rates, tolls and charges was determined applying a rate of return equal to the mid-point between the stated range of returns on rate base;

(e) The Board ordered that a particular capital structure of NLP be adopted and continue to be the basis of NLP's financial plan.

6 The Board had previously adopted a policy allowing NLP to retain earnings above the allowed range of return on rate base, provided those earnings were within the allowed range of rates of return on common equity. Where the earnings exceeded the allowed rate of return on common equity, the Board, in purported exercise of its statutory powers to regulate NLP's accounting procedures, as well as other powers, required NLP to set up a reserve account in which these excess earnings would be held and dealt with in accordance with subsequent direction by the Board.

7 In April of 1996, NLP petitioned the Board for another order fixing and determining a new rate base, determining a just and reasonable return and approving a revised schedule of rates, tolls and charges, amongst other matters. One of the parties represented at the hearing was the "Consumer Advocate", who was appointed [FN7] by the Government of Newfoundland and Labrador to represent the interests of domestic and general service consumers in respect of the rate hearing.

8 During the years between the making of the 1991 orders and the 1996 hearing, NLP had filed annual returns with the Board, as required by s-s. 59(2) of the Act, which indicated that in the years 1991, 1992 and 1993 the company's rate of return on rate base was in excess of the range determined in the 1991 Order. However, as calculated by NLP, the rate of return on common equity was always within the range that had been stipulated by the Board. The rates of return on rate base and on common equity were calculated based on actual expenses and on the actual capital structure of NLP.

9 In its periodic reports to the Board, NLP disclosed that its actual advertising costs in 1992 exceeded the amounts projected to the Board as a forecast for 1992 which had been approved as reasonable and prudent by the Board in its 1991 Order in the course of fixing and determining the rate base.

10 During the course of the 1996 hearing, certain submissions were made to the Board respecting, amongst other things,

(a) whether NLP should be regarded as having earned revenue in excess of its allowed range of rate of return where its rate of return on common equity was nevertheless within the stated allowable range;

(b) whether the manner of calculation of excess revenue and the proposed manner of the disposition of any excess was permitted;

(c) whether NLP could and should be required to alter its capital structure so as to obtain its capital requirements in a manner other than the way in which it was presently doing;

(d) whether the Board could and should take account, in setting future rates, of past expenditures which were in excess of amounts deemed reasonable and prudent at the time of a previous hearing.

11 Questions arose as to the jurisdiction and power of the Board to entertain and act on the sorts of submissions that were made. This prompted the Board to state the current case to this Court. NLP and the Consumer Advocate were granted standing to appear and be heard at the hearing.

The Specific Questions

12 The Stated Case poses for consideration by this Court the following questions:

(1) Does the Board have jurisdiction pursuant to the Act to set and fix the return which a public utility may earn annually upon:

(i) the rate base as fixed and determined by the Board for each type of service applied by the public utility; and/or

(ii) the investment which the Board has determined has been made in the public utility by the holders of common shares.

(2) Does the Board have jurisdiction to set the rates of return referred to in Question (1) as a range of permissible rates of return.

(3) Should a public utility earn annually a rate of return which is in excess of the rate of return determined by the Board to be just and reasonable, either on:

(i) the base rate as fixed and determined by the Board for each type of service applied by the public utility; or

(ii) the investment, which the Board has determined, has been made in the public utility by holders of common shares,

does the Board have jurisdiction to:

(i) require the public utility to use the excess earnings to reduce revenue requirements for the succeeding year; or

(ii) require the public utility to place the excess earnings in a reserve fund for the purpose of adjusting rates, tolls and charges of the public utility at a future date, or

(iii) require the public utility to rebate the excess earnings to customers of the public utility.

(4) Does the Board have jurisdiction to order that the rates, tolls and charges of a public utility shall be

approved taking into account earnings in excess of a just and reasonable return upon,

(i) the rate base as fixed and determined by the Board for each type of service applied by the public utility, or

(ii) the investment, which the Board has determined, has been made in the public utility by the holders of common shares,

in prior years.

(5) Does the fact that the Board has advised the public utility that it is permitted to retain earnings in excess of the rate of return determined by the Board to be a just and reasonable return, upon the rate base as fixed and determined by the Board for each type of service supplied by the public utility, but not in excess of the return determined by the Board to be a just and reasonable return upon the investment which the Board has determined has been made in the public utility by the holders of common shares, affect the jurisdiction of the Board to approve rates, tolls and charges on the basis queried in Question (4).

(6) Does the Board have jurisdiction to order the rates, tolls and charges of the public utility shall be approved taking into account the amount of expenses previously incurred by the public utility which the Board may now consider inappropriate to be allowed as reasonable and prudent and properly chargeable to operating account notwithstanding that such classes of expenses were allowed as reasonable and prudent and properly chargeable to operating account.

(7) Does the Board have jurisdiction to require a public utility to maintain:

(i) a ratio; or

(ii) a ratio within a stated range of ratios

of equity and debt, as the means of obtaining the capital requirements of the public utility.

(8) Does the Board, upon an application pursuant to Section 91 or otherwise, have the jurisdiction to require a public utility to obtain its capital requirements by the issue of specific financial instruments, whether common shares, preferred shares, stocks, bonds, debentures or evidence of indebtedness payable in more than one year.

Although the questions are stated above as they appear in the Stated Case filed with the Court, there are several obvious typographical errors in the language used. This was recognized by the participants in references to the questions in their written arguments. In particular "supplied" was at times substituted for the word "applied" in questions 1(i), 3(i) and 4(i) and "base rate" in Question 3(i) was replaced by "rate base." In addition, the phrase "In the event that a public utility should ..." at the beginning of Question 3 was used at times in the written submissions in preference to the phrase "Should a public utility ..." Nothing turns on these informal changes. They do, however, make the import of the questions clearer and I will interpret the questions in that light.

The Legislative Framework

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

13 The answers to the questions which have been posed must, of course, be given taking account of the legislative framework within which the Board operates. The Board is a creature of statute and its jurisdiction and powers to deal with matters brought before it, and the manner of dealing with such matters, must be found, either expressly or impliedly, within the statutes conferring jurisdiction on and governing the operation of the Board.

14 While a number of specific provisions of the Act and related legislation will have to be referred to in the course of this opinion, certain legislative provisions, which are central to this analysis, can be conveniently set forth here:

Public Utilities Act

58. The board may prescribe the form of all books, accounts, papers and records to be kept by a public utility and a public utility shall keep its books, accounts, papers and records and make its returns in the manner and form prescribed by the board and comply with all directions of the board relating to those books, accounts, papers, records and returns.

69.(1) A public utility, if so ordered by the board, shall, out of earnings, set aside all money required and carry it in a depreciation account.

(2) The depreciation account shall not, without the consent of the board, be spent otherwise than for replacements, new constructions, extensions or additions to the property of the company.

(3) The board may by order require a public utility to create and maintain a reserve fund for a purpose which the board thinks appropriate, including the improvement of the public utility's status as a borrower or seeker of funds for necessary maintenance or expansion of its operations.

(4) The board, in a case where it has made an order which has the effect of increasing a public utility's revenues, may require the public utility to refrain from distributing as dividends until further order the whole or a part of the extra revenue which is in the board's opinion attributable to the order.

(5) An order under this section shall be made only after hearing the public utility concerned.

70.(1) A public utility shall not charge, demand, collect or receive compensation for a service performed by it whether for the public or under contract until the public utility has first submitted for the approval of the board a schedule of rates, tolls and charges and has obtained the approval of the board and the schedule of rates, tolls and charges so approved shall be filed with the board and shall be the only lawful rates, tolls and charges of the public utility, until altered, reduced or modified as provided in this Act.

75.(1) The board may make an interim order unilaterally and without public hearing or notice, approving with or without modification, a schedule of rates, tolls and charges submitted by a public utility, upon the terms and conditions that it may decide.

(2) The schedule of rates, tolls and charges approved under subsection (1) are the only lawful rates, tolls and charges of the public utility until a final order is made by the board under section 70.

(3) The board may order that the excess revenue that was earned as a result of an interim order made under subsection (1) and not confirmed by the board be

(a) refunded to the customers of the public utility; or

(b) placed in a reserve fund for the purpose that may be approved by the board.

76. The board may upon notice to the public utility and after hearing as provided in this Act, by order rescind, alter or amend an order fixing rates, tolls, charges or schedules, or other order made by the board, and certified copies of the order shall be served and take effect as provided in this Act for original orders.

78.(1) Except as otherwise provided in this Act, the board may fix and determine a separate rate base for each kind of service provided or supplied to the public by a public utility, and may revise the base.

(2) In fixing a rate base the board may, in addition to the value of the property and assets as determined under section 64, include

. . . . .

(h) other fair and reasonable expenses which

(i) the board thinks appropriate and basic to the public utility's operation, and

(ii) has, with the approval of the board, been charged to capital account,

but the expenses shall be allowed only to the extent not amortized in previous years.

80.(1) A public utility is entitled to earn annually a just and reasonable return as determined by the board on the rate base as fixed and determined by the board for each type or kind of service supplied by the public utility but where the board by order requires a public utility to set aside annually a sum for or towards an amortization fund or other special reserve in respect of a service supplied, and does not in the order or in a subsequent order authorize the sum or a part of it to be charged as an operating expense in connection with the service, the sum or part of it shall be deducted from the amount which otherwise under this section the public utility would be entitled to earn in respect of the service, and the net earnings from the service shall be reduced accordingly.

(2) The return shall be in addition to those expenses that the board may allow as reasonable and prudent and properly chargeable to operating account, and to all just allowances made by the board according to this Act and the rules and regulations of the board.

(3) Reasonable payments each year to former employees of a public utility who have retired and are receiving payments of supplemental income from the public utility are expenses that the board may allow as reasonable and prudent and properly chargeable to the operating account of the public utility.

(4) The board may use estimates of the rate base and the revenues and expenses of a public utility.

84.(1) Upon a complaint made to the board against a public utility by an incorporated municipal body or the Newfoundland and Labrador Federation of Municipalities or by 5 persons, firms or corporations, that the rates, tolls, charges or schedules are unreasonable or unjustly discriminatory or that a regulation, measurement, practice or act affecting or relating to the operation of a public utility is unreasonable, insufficient or unjustly discriminatory or that the service is inadequate or unobtainable, the board shall

proceed, with or without notice, to make the investigation that it considers necessary or expedient.

(2) The board may order the rates, tolls, charges or schedules reduced, modified or altered, and make other orders as to the reduction, modification or change of the regulation, measurement, practice or acts that the case may require, and may order on the terms and subject to the conditions that are just that the public utility provide reasonably adequate service and facilities and make extensions that may be required, but an order shall not be made or entered by the board without a public hearing or inquiry.

87.(1) Where upon an investigation the rates, tolls, charges or schedules are found to be unjust, unreasonable, insufficient or unjustly discriminatory, or to be preferential or in violation of this Act, the board has power to cancel those rates, tolls, charges or schedules and declare void all contracts or agreements, either oral or written, dealing with them upon and after a day named by the board, and to determine and by order substitute those rates, tolls or schedules that are reasonable.

91.(1) A public utility shall not issue shares, which for the purposes of this section shall include preferred shares, stocks, bonds, debentures or evidence of indebtedness payable in more than 1 year from the date of issue, except as provided in subsection (2) until it has obtained approval from the board for the proposed issue;...

. . . . .

(3) After hearing the application and where satisfied that the proposed issue by a public utility of its shares, stocks, bonds, debentures or other evidence of indebtedness is to be made in accordance with law and for a purpose approved by the board, it is the duty of the board to make an order approving the proposed issue to the amount that it considers appropriate, and also to prescribe the purpose to which the issue or the proceeds of the issue are applied.

. . . . .

(5) Without first obtaining the approval of the board,

(a) a public utility shall not make a material alteration in the characteristics of its stocks or shares, or its bonds, debentures, securities, or other evidence of indebtedness as those characteristics are described by the board in granting its approval of the issue;...

Electrical Power Control Act, 1994[FN8]

3. It is declared to be the policy of the province that

(a) the rates to be charged, either generally or under specific contracts, for the supply of power within the province

(i) should be reasonable and not unjustly discriminatory,

(ii) should be established, wherever practicable, based on forecast costs for that supply of power for 1 or more years,

(iii) should provide sufficient revenue to the producer or retailer of the power to enable it to earn a

> just and reasonable return as construed under the *Public Utilities Act* so that it is able to achieve and maintain a sound credit rating in the financial markets of the world, and
>
> . . . . .
>
> (b) all sources and facilities for the production, transmission and distribution of power in the province should be managed and operated in a manner
>
> (i) that would result in the most efficient production, transmission and distribution of power,
>
> (ii) that would result in consumers in the province having equitable access to an adequate supply of power,
>
> (iii) that would result in power being delivered to consumers in the province at the lowest possible cost consistent with reliable service,...
>
> . . . . .
>
> 4. In carrying out its duties and exercising its powers under this Act or under the *Public Utilities Act*, the public utilities board shall implement the power policy declared in section 3, and in doing so shall apply tests which are consistent with generally accepted sound public utility practice.

Approach to Interpretation

15 The Court was not referred to any decisions in this or other jurisdictions which directly addressed, let alone answered, the specific types of questions which have been posed. To answer the questions, therefore, it is necessary to develop a theoretical frame of reference within the context of the general language of the existing legislation so as to determine the approach to be taken to its application in concrete situations.

16 It is necessary to examine the specific legislative provisions in the larger regulatory context and against the background of the purposes of the legislation and the general principles which have been developed as part of regulatory practice[FN9]. This approach follows from s. 118 of the Act which provides:

> 118.(1) This Act shall be interpreted and construed liberally in order to accomplish its purposes, and where a specific power or authority is given the board by this Act, the enumeration of it shall not be held to exclude or impair a power or authority otherwise in this Act conferred on the board.
>
> (2) The Board created has, in addition to the power specified in this Act, all additional implied and incidental powers which may be appropriate or necessary to carry out the powers specified in this Act.
>
> (3) A substantial compliance with the requirements of this Act is sufficient to give effect to all the rules, orders, acts and regulations of the Board, and they shall not be declared inoperative, illegal or void for an omission of a technical nature.

17 In addition, the EPC Act[FN10], provides that the Board, in carrying out its duties and exercising its powers under the *Public Utilities Act* must implement the power policy of the province, as declared in s. 3 of the

Act, and in so doing must "apply tests which are consistent with generally accepted sound public utility practice".

18 It follows from these provisions that a literal and technocratic interpretation and application of the provisions of the Act is to be avoided, in favour of an interpretation which will advance the underlying purpose of the legislation[FN11] as well as the power policy of the province and be consistent with generally accepted sound public utility practice.

19 In answering the questions posed, therefore, it is necessary to identify generally accepted principles of sound public utility practice and to give to the legislation an interpretation which follows those principles and advances the stated legislative policy of the Province.

20 The trade off for the regulation by the state of the rates, tolls and charges of monopolistic utilities in the interests of consumers is the statutory recognition that the utility should be entitled to earn a fair return for its efforts. Although differing in details, the regulatory statutory regimes existing throughout North America can, as a generalization, be said to be broadly similar in approach[FN12], although in recent years the regulatory schemes and their coverage are being affected more and more by the trends towards deregulation.

21 The regulatory body in question (in Newfoundland, the Board of Commissioners of Public Utilities) is generally charged with balancing the competing interests of consumers and the investors in the utility[FN13]. As deGrandpré[FN14] observed:

> This involves the Board attempting to make sure that, in the consumers' interests, the service provided is adequate and provided at just and reasonable rates and, for the utility and its investors, that those rates provide a sufficient income.

22 This balancing of interests is found in the province's stated power policy in s. 3 of the *EPC Act* where, emphasizing the interests of the utility, it is declared that the rates charged for the power should provide sufficient revenue to the utility to enable it to earn a just and reasonable return "so that it is able to achieve and maintain a sound credit rating in the financial markets of the world"[FN15] while at the same time declaring that the rates should be "reasonable"[FN16] and that the utilities' facilities should be managed and operated in a manner that would result in power being delivered to consumers "at the lowest possible cost consistent with reliable service"[FN17]. This policy finds legislative expression in the regulatory mechanisms of the Act itself, which provides that a utility must provide service and facilities which are "reasonably safe and adequate and just and reasonable"[FN18] and prohibits a utility from charging rates, tolls and charges unless they have been approved by the Board[FN19] while at the same time stating as a general principle that the utility is entitled to earn annually a just and reasonable return on its rate base[FN20].

23 This statutory entitlement of the utility to earn a "just and reasonable" return is the linguistic touchstone for the balancing exercise. This phrase emphasizes the fairness aspect, both to the utility, in earning sufficient revenues to make its continued investment worthwhile and to maintain its credit rating in financial markets, and to the consumer, in obtaining adequate service at reasonable rates. It also emphasizes the need for a tempering of each interest group's economic imperative by consideration of the interests of the other.

24 Having said that, the entitlement of the utility to a fair return on its investment is always regarded as of fundamental importance[FN21]. In the United States, controls which fail to allow a fair return have the potential of running afoul of constitutional strictures against confiscation of property without due compensation. While

the same constitutional concerns may not be present in Canada, the case law has at times nevertheless referred to the entitlement to a fair return as a "common law right"[FN22] which should be read into the legislation even where it is not specifically expressed.

25 There is no uniform methodology employed in the regulatory jurisdictions in North America for the determination of a just and reasonable rate of return[FN23]. What recurs, however, is a theme that the process is not an exact science and depends on a variety of factors necessary to balance the competing interests involved. Rate setting is essentially a prospective exercise where determinations are made on the basis of estimates and information that will not necessarily remain static.

26 Most jurisdictions adopt a "multiple factor" approach. The *Bluefield Waterworks* case[FN24] in the United States emphasized early on that the determination of a fair rate of return

> ...depends upon many circumstances and must be determined by the exercise of a fair and enlightened judgment, having regard to all relevant facts.[FN25]

27 Statements such as "the company will be allowed as large a return on the capital invested in the enterprise ... as it would receive if it were investing the same amount in other securities possessing an attractiveness, stability and certainty equal to that of the company's enterprise"[FN26] often occur. For the rationale for such statements one need look no further than the provincial policy, stated in paragraph 3(a)(iii) of the *EPC Act* that the utility must be "able to achieve and maintain a sound credit rating in the financial markets of the world" so as to be able to raise the money necessary for the proper performance of its functions. To achieve such a goal of attracting capital, factors such as comparisons with other comparable enterprises, the respective costs of debt and equity, the capital breakdown between debt and equity and general economic conditions, amongst other things, are considered.

28 In *Federal Power Commission v. Hope Natural Gas Co.*[FN27], another landmark United States case, the court emphasized that it is the "end result of the process which has to be judged as to whether the rate is "just and reasonable". As a result, in the words of deGrandpré:

> In stating that the end result was the only point of consideration, whatever the means of arriving thereat, the court opened the door to a wide variety of ways and means to arrive at a proper calculation of returns. In effect, it left the valuation of rate bases to the Commission's or Court's discretion.[FN28]

DeGrandpré's conclusion, based on his survey of North American regulatory regimes, is later stated as follows:

> The constantly changing economic conditions are perhaps a good reason why there should be no stringent rules for determining a rate of return. As was often stated, the process is one which calls for common sense, good judgment and a proper appreciation of all surrounding factors.[FN29]

29 This approach is also reflected in the decision of this Court in *Newfoundland Light & Power Co. v. Newfoundland (Public Utilities Commissioners Board)* where O'Neill, J.A., speaking for the Court in rejecting an argument that the Board of Commissioners of Public Utilities had exceeded its jurisdiction in determining a just and reasonable rate of return by not adopting a particular methodology (a "comparable earnings" test), stated:

> ...it is within the discretion of the Board, having heard all the evidence and giving consideration to the

> various tests which may be used, to make its ruling on the basis of what in the Board's opinion will give to the applicant a just and reasonable return and permit it to maintain a sound financial credit rating.[FN30]

The Board therefore has a broad discretion to adopt appropriate methodologies for the calculation of allowable rates of return. So long as the methodologies chosen are not inconsistent with generally accepted sound public utility practice and the purposes and policies of the Act, and can be supported by the available opinion evidence, the determination of what constitutes a just and reasonable return in a given case will generally be within the province of the Board and will not normally be interfered with[FN31]. The jurisdiction of the Board must therefore be defined to enable that process to occur.

30 Because setting the rate of return is not an exact science no matter what methodology is chosen, because the viewpoint is essentially prospective, it has been recognized that there is a "zone of reasonableness" within which a rate of return chosen by the Board should be regarded as just and reasonable. This has been expressed by the United States Supreme Court in the following language:

> Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint. It allows a substantial spread between what is unreasonable because too low and what is unreasonable because too high [FN32].

This notion has also at times been recognized in Canada[FN33].

31 This leads to another point: because the setting of the rate of return is based on projections, one cannot be sure that the rate of return will be achieved in practice. Although the utility is "entitled" by s. 80 of the Act to have the Board determine a just and reasonable rate of return based on appropriate predictive techniques and methodologies, it is not "entitled", in the sense of being guaranteed, to that rate of return[FN34]. The utility therefore takes the risk that its chosen management techniques and the future economic climate may not yield its expected success. Although some of the activities of the utility are regulated within the framework of the statutory objectives, the utility nevertheless remains subject to business risks and the effects of management decisions. To that extent, the financial risks associated with the operation of the utility, just as in the case of any private business, are to be born by the investors in the enterprise, not the consumer of the service.

32 The corollary of this position is that the utility must be accorded a degree of managerial flexibility in decision-making in order to be able to minimize the risks to which it must respond. Thus, it is often said that the powers of the Board must be regulative and corrective, but not managerial, and they do not therefore contemplate a retroactive adjustment of the actions of management.

33 This leads to the general principle of non-retroactivity which prevents a utility from recovering expenses incurred in the past out of current rates. The utility must live with the decisions it makes and the economic vicissitudes that occur.[FN35].

34 By the same token, it is sometimes argued that the occurrence of the reverse situation, of the utility doing better than expected, should mean that the utility should be able to reap the advantage of better and more efficient management techniques and favourable economic conditions and keep any surplus. The concern for the consumer interest is often put forward as a brake on this idea, however. The requirement that the consumer receive power "at the lowest possible cost"[FN36] consistent with the utility's requirement of earning a just and reasonable return for its purposes means, it is often argued, that the regulator ought to have power to ensure that excessive returns are somehow accounted and compensated for.

35 Another factor that is referred to in the cases is the recognition that the capital structure of the utility will often have a bearing on the total cost of capital and this will therefore be important where the determination of the rate base depends on the total debt and equity capital requirements. DeGrandpré observes that "the reasonableness of the ratio of debt to equity is a question of fact left to the appreciation of the Board or Court" [FN37]. Thus, issues such as whether the Board can dictate to the utility a particular mix of debt and equity or, for the purpose of setting the rate of return, do so on the basis of a notional blend of capital requirements if the actual blend is not in accordance with what the Board feels is optimal to ensure a fair return as well as low rates, tolls and charges, often surface. Indeed, this issue is presented in this case.

36 Having conducted this brief survey, I will now attempt to state some general principles to be used in the interpretation and application of the local legislation:

1. The Act should be given a broad and liberal interpretation to achieve its purposes as well as the implementation of the power policy of the province;

2. The Board has a broad discretion, and hence a large jurisdiction, in its choice of the methodologies and approaches to be adopted to achieve the purposes of the legislation and to implement provincial power policy;

3. The failure to identify a specific statutory power in the Board to undertake a particular impugned action does not mean that the jurisdiction of the Board is thereby circumscribed; so long as the contemplated action can be said to be "appropriate or necessary" to carry out an identified statutory power and can be broadly said to advance the purposes and policies of the legislation, the Board will generally be regarded as having such an implied or incidental power;

4. In carrying out its functions under the Act, the Board is circumscribed by the requirement to balance the interests, as identified in the legislation, of the utility against those of the consuming public;

5. The setting of a "just and reasonable" rate of return is of fundamental importance to the utility and must always be an important focus of the Board's deliberations; however, the "entitlement" of the utility to a just and reasonable rate of return does not guarantee it that level of return. The "entitlement" is to have the Board address that issue and to make its best prospective estimate, based on its full consideration of all available evidence, for the purpose of setting rates, tolls and charges.

6. The Board has jurisdiction, which will not generally be interfered with on judicial review, to make a determination of what is a just and reasonable rate of return within a "zone of reasonableness" and in so doing is not constrained in its choice of applicable methodologies, so long as they can be rationally justified in accordance with sound utility practice and are not inconsistent with the achievement of the purposes and policies of the legislation.

37 It is now necessary to consider each of the specific questions that have been posed. In approaching them, it is worth remembering that the questions have been posed in the abstract and ask for answers to broadly-identified issues of jurisdiction. The case is not an appeal and there can be no findings of fact made by this Court in arriving at its conclusions. The information provided by the Board as to past hearings was given as background only so as to assist the Court in better understanding the scope and potential importance of the questions. While the answers given may provide guidance with respect to specific issues that have arisen in hearings in the past, they cannot be taken as an adjudication of those issues in the specific factual context in

which they arose.

Question No.1

(1) Does the Board have jurisdiction pursuant to the Act to set and fix the return which a public utility may earn annually upon:

(i) the rate base as fixed and determined by the Board for each type of service applied by the public utility; and/or

(ii) the investment which the Board has determined has been made in the public utility by the holders of common shares.

38 It will become apparent from the ensuing discussion that a number of the questions posed on this stated case are interrelated in the sense that the answer to some of them will provide a strong impetus for a particular response in others. This is particularly evident in Question 1.

39 The answer to Question 1 in fact involves a consideration of two sub-issues. The first relates to the legal significance of a determination by the Board on a given application of the just and reasonable return to which the utility is entitled. The second sub-issue, which is affected by the decision on the first, relates to the powers of the Board to make determinations with respect to the rate of return on a utility's common equity portion of its capital structure.

(a) The Legal Significance of a "Determination"

40 It is to be noted that Question 1 asks whether the Board has jurisdiction to "set and fix" the utility's return whereas s-s. 80(1) of the Act speaks in terms of the utility being entitled to earn a return as "determined" by the Board. The use of this differing terminology in the question, as explained by counsel for the Board at the hearing, was designed deliberately to raise the issue as to whether the Board may, by determining the level of return, be said to be prescribing that level as an upper limit to the level of earnings to which the utility may be entitled and thereby exercise certain powers with respect to disposition of any excess that may in fact be earned. This issue becomes more focused when Question 3 is considered. The answer to that question will, to some extent, be influenced by the powe which the Board can be said to have unde s. 80 with respect to the setting of a level of return.

41 It is obvious, of course, that in the process of approving rates, tolls and charges under s-s. 70(1) the Board must determine what is a just and reasonable return on the utility's rate base in order to determine the level of revenue needed by the utility[FN38]. This flows from the utility's "entitlement" in s-s. 80(1) to earn that level of return. The determination of a just and reasonable return on rate base is therefore an essential component in the series of calculations which the Board must undertake in the process of approving rates, tolls and charges.

42 If the determination of a just and reasonable return is merely a step in the process of approving rates, tolls and charges under s-s. 70(1), that is, if it is only an intermediate calculation necessary to arrive at the final result of consumer rate approval, the "determination" of a just and reasonable level of return will have no independent legal significance, in the sense of prescribing the limit of the utility's return for other purposes of the Board's functions.

is applied to the rate base "as fixed and determined" by the Board. On a strict linguistic analysis alone, the use of the word "fixed" in conjunction with "determined" in one place would imply that its absence in the other was deliberate.

49 Notwithstanding these matters, I am not satisfied that a linguistic analysis of the subsection can provide the answer in this case. Even a cursory perusal of the remaining provisions of the Act indicates that there is no uniform terminology chosen to describe the various decision-making functions in which the Board may engage. For example, the Act provides that the Board may "inquire into and determine"[FN41] the valuation of a utility's assets and may "determine"[FN42] those values in accordance with a number of stated rules. It may "ascertain and determine"[FN43] what are proper and adequate rates of depreciation of classes of utility property. Its role with respect to the utility's rates, tolls and charges is one of "approval"[FN44]. Indeed, if there is any decision of the Board which is contemplated as having operative legal effect and to amount to a "fixing" of the utility's rates, tolls and charges from which the utility may not deviate, it is the "approval" contemplated in this regard; yet the word "fix" does not appear. In another context, the Board may "fix and determine"[FN45] a separate rate base for each kind of service supplied by a utility; yet when describing what is to be included in the calculation of rate base, the reference to "determine" is dropped and it is simply described as "fixing a rate base"[FN46]. Finally, the term "approval" surfaces again in the context of the power of the Board to authorize new stock issues of the utility[FN47].

50 To resolve this conundrum, resulting from inconsistency in terminology, resort must be had to the purposes of and policies underlying the legislation as mandated in s-s. 118 of the Act as well as s. 4 of the *EPC Act*. As indicated previously,[FN48] the Board is required, in carrying out its functions under the Act, to balance the interests, as identified in the legislation, of the utility against those of the consuming public. The notion of a "just and reasonable return" in s-s. 80(1) is the benchmark against which fairness to the utility and the consumer is to be measured. It is pivotal in the balancing exercise. The interests of the consuming public in obtaining power at the lowest possible cost consistent with reliable service[FN49] must accommodate the utility's interest in being afforded the opportunity to earn a fair rate of return for its efforts. In the methodology adopted by the Board, the approval of appropriate rates, tolls and charges necessarily factors the just and reasonable return, and only that level of return, into that calculation. Otherwise, the interests of the consumer would not be protected in obtaining power at the lowest possible cost. It is therefore inherent in the process that in determining a just and reasonable return for the utility, the utility should have the opportunity of earning that return but, other things being equal, should not expect to earn any more. Accordingly, determining the just and reasonable return necessarily involving prescribing the return and in that sense can be said to amount to "setting and fixing" the rate of return.

51 It follows from this that the use of the word "determine" can, in the context of the use of that and other terminology in the Act, encompass something more than the notion of mere calculation and extends to the idea of prescribing, or fixing, a level of return in the nature of a legal decision which can bind and have effect on the utility for other purposes related to the Act.

(b) The Power to Set and Fix the Level of Return on Common Equity

52 In order to determine the just and reasonable return on rate base to which the utility is entitled by s-s. 80(1), the Board must first determine the cost to the utility of the various components of its sources of funds. The costs associated with long term debt and preference shares are generally static over the period covered by a particular rate hearing. Accordingly, they are often described as "embedded costs". The rate of return necessary

to be earned on rate base to cover the cost of debt and preference shares can therefore usually be easily determined based on the interest rates or dividend rates applicable to such instruments. In the case of common equity, however, the cost to the utility of this source of funds depends upon a number of factors, especially current market conditions which, by nature, can be volatile.

53 At a rate hearing, therefore, the Board usually faces a greater difficulty in determining the component of rate of return on common equity than on the other sources of funds because their embedded costs are usually well defined.

54 Since the rate base is financed by a combination of debt, preference shares and common equity, the rate of return on which is different for each component, the overall rate of return on rate base is calculated as a weighted average of the rates of return on the various individual components.[FN50]

55 As a generalization, it is sometimes said that the cost of common equity is often higher than that of debt [FN51]. The rate of return on common equity may therefore be expressed as a percentage which is higher than the overall rate of return on the full rate base because the higher equity cost will be weighted downwards by the rates for the other components.

56 The issue raised by Question 1(ii) is whether the Board may set and fix the rate of return on common equity, as a component of the overall rate of return on rate base in a manner such that it can be used as an independent benchmark for other purposes in the same way as the overall determination of return on rate base can be. Alternatively, is the "determination" of the rate of return on common equity to be treated in the narrower sense of a mere calculation leading to the final determination of overall return?

57 Subsection 80(1) makes no reference at all to determining, let alone setting and fixing, the rate of return on common equity. The calculation of an appropriate rate of return on common equity is truly a mere component in the overall process of determining a just and reasonable return on rate base. Furthermore, there is nothing in the purpose of the Act or the policies which the Board is to implement which would lead inexorably to the conclusion that the Board ought to have the power to prescribe a rate of return on common equity as a component of an overall return or rate base, any more than it ought to have a power to prescribe a return on any other component.

58 The Consumer Advocate submitted that inasmuch as s-s. 80(1), by its express language, contemplates that the only measure of what NLP may earn annually is to be determined by a just and reasonable return on rate base, to allow the utility to measure what it may earn annually based upon a different factor, such as a rate of return on common equity which could very well be higher than the overall rate of return on rate base and might lead to a higher overall return that could be said to be justified, would be to allow the utility to earn more than that to which it is statutorily entitled.

59 It is to be noted, however, that in its previous orders[FN52] the Board has not sought to determine the level of return on the basis of anything other than a rate of return on rate base. For example, in the 1991 Order, the Board ordered:

> A just and reasonable return for [NLP] is determined to be between 10.96% and 11.19% on its average rate base for 1992, which will provide an opportunity to earn a rate of return on common equity between the range of 13.00% to 13.50%.

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

[Emphasis added]

The reference to the range of rates of return on common equity appears to have been inserted more as information in support of a rationale for the determination of the overall return on rate base, since the Board states that the determination of the return on rate base "will provide" an "opportunity" to earn a rate of return on common equity. Similarly, the 1996-97 Order simply described the rate of return on rate base as being "derived from" a given range of return on common equity. This is the correct approach.

60 As to whether the Board may make other decisions, for example relating to the manner in which an excess revenue fund should be maintained, by reference to the contemplated rate of return on common equity, is a separate matter which should be dealt with in that context.

61 I therefore conclude that the power to "determine" a just and reasonable return on rate base, as contained in s-s. 80(1) does not include within it a power to "set and fix a rate of return on common equity" but it obviously does contemplate that the analysis of appropriate rates of return on common equity will be undertaken and factored into the conclusion as to what is a just and reasonable return on rate base.

62 Accordingly, giving the words "set and fix" in the question a meaning which implies the notion of prescribing, I would answer Question 1 as follows:

As to:

1. (i) - Yes

1. (ii) - No

Question No. 2

(2) Does the Board have jurisdiction to set the rates of return referred to in Question (1) as a range of permissible rates of return.

63 In light of my answer to the second part of Question 1, it is only necessary to address Question 2 in the context of whether the Board has jurisdiction to set the rate of return on rate base as a "range of permissible rates of return".

64 It has already been stressed that the determination of a just and reasonable return on rate base involves a consideration of the differing costs of the components of the utility's capital structure and that in arriving at the overall rate of return, it is permissible for the Board to use a weighted average of the rates associated with each individual component. It has also been pointed out that the cost of common equity is often difficult to estimate with precision. The best that experts are often able to do is estimate rates within a reasonable range. Inasmuch as the cost of common equity is weighted into the overall rate of return on rate base, that range would also have to be reflected in the ultimate rate of return on rate base, as determined by the Board.

65 In *Edmonton (City) v. Northwestern Utilities Ltd.*[FN53] Smith, J. emphasized:

The question of a fair rate of return on a risky investment is largely a matter of opinion, and is hardly capable of being reduced to certainty by evidence, and appears to be one of the things entrusted by the

statute to the judgment of the Board.

66 It is evident, as *Newfoundland Light & Power Co. v. Newfoundland (Public Utilities Commissioners Board)*[FN54] demonstrates, that the determination of a just and reasonable return is an area in which the Board is accorded a broad discretion as to the methodology to be adopted. Obviously, the striking of a balance between the interests of the utility and the consumer, whilst at the same time attempting to comply with the Board's obligation to approve rates which will produce a fair return to the utility, cannot be done with the precision of a simple mathematical calculation. Realistically, the balance can only be struck within a reasonable range. It is for that reason that the courts have, on subsequent appeal or applications for judicial review, generally deferred to the determinations of boards in this regard provided the determination is not arbitrary or capricious and can be said to fall within a reasonable range.[FN55] As indicated in the earlier discussion[FN56], in the United States the notion of a "zone of reasonableness" as an "area rather than a pinpoint" has been recognized. Whilst this notion has been enunciated as a justification for deference to Board decisions in the context of challenges on appeal or judicial review, it nevertheless indicates a recognition of what is inherent in the rate setting process.

67 I see no reason, therefore, why, instead of attempting to justify a particular decision ex post facto by an argument that a particular rate falls within a zone of reasonableness, the Board could not expressly indicate what it believes that area of reasonableness to be by expressing what it believes to be a just and reasonable return in terms of a range of rates of return. This indeed is a practice that has been adopted elsewhere[FN57]

68 It is to be noted that s-s. 80(1) does not speak in terms of a "rate" or "rates" of return; rather, it speaks of a just and reasonable "return". It is not limited by its language to the pinpointing of a particular rate of return. I conclude that a liberal construction of the word "return" in the context of s-s. 80(1) leads to the conclusion that it can include a range of rates of return.

69 Of course, in applying the rate of return to the rate base, as ascertained by the Board, a single figure will have to be used since rates, tolls and charges are expressed as finite numbers. The Board in practice has chosen the mid-point of its stated range of rates of return as the figure to be used for this purpose. This is a perfectly acceptable practice for the purpose of setting the rates. By expressing a range, however, the Board leaves open to the utility the flexibility of earning more than the mid-point up to the maximum end of the range so as, in effect, to give the benefit of the doubt to the utility that the expert evidence favouring the upper end of the range turns out to be the more accurate and to provide an incentive to the utility towards managerial efficiency.

70 The Consumer Advocate expressed concern in argument that the use of the word "permissible" in Question 2, as qualifying the phrase "rates of return", might be misleading. As I understand the argument, the concern is that the adoption of a range approach might lead to the conclusion that the "entitlement" of the utility to a just and reasonable return would be regarded as an entitlement, or guarantee, of earning up to the maximum end of the range. While the utility, if it earned as much as the maximum would be entitled to keep that amount of earnings, it is not, for reasons already given, guaranteed that level of return if it is not in fact successful in earning them. The Board is under no obligation to adjust future rates or to take other steps to make up any such shortfall. Any rate of return earned within the range would be regarded as permissible and it is only when a rate of return exceeds the upper limit of the range that it would be regarded by the Board as subject to any excess revenue regulation.

71 Accordingly, recognizing that, on my analysis, Question 2 only relates to whether the Board has jurisdiction to set rates of return as a range in relation to its determination of a just and reasonable return on rate

base, the answer I would give to Question No. 2 is: "Yes".

Question Nos. 3 and 4

(3) Should a public utility earn annually a rate of return which is in excess of the rate of return determined by the Board to be just and reasonable, either on:

(i) the base rate as fixed and determined by the Board for each type of service applied by the public utility; or

(ii) the investment, which the Board has determined, has been made in the public utility by holders of common shares,

does the Board have jurisdiction to:

(i) require the public utility to use the excess earnings to reduce revenue requirements for the succeeding year; or

(ii) require the public utility to place the excess earnings in a reserve fund for the purpose of adjusting rates, tolls and charges of the public utility at a future date, or

(iii) require the public utility to rebate the excess earnings to customers of the public utility.

(4) Does the Board have jurisdiction to order that the rates, tolls and charges of a public utility shall be approved taking into account earnings in excess of a just and reasonable return upon,

(i) the rate base as fixed and determined by the Board for each type of service applied by the public utility, or

(ii) the investment, which the Board has determined, has been made in the public utility by the holders of common shares,

in prior years.

72 The analysis leading to the answers to Questions 3 and 4 can be considered together since they both address the same general theme: the scope of the Board's powers to deal with situations where a utility in fact earns a rate of return that is greater than that determined to be a just and reasonable return.

73 It was suggested by counsel for NLP that the concept of "excess earnings" does not exist under the Act other than by reference to a definition of what is to be deposited into a reserve fund which the utility may be ordered to create and maintain pursuant to s-s. 69(3) of the Act. This submission follows from the position taken by NLP that the Board has no power under s-s. 80(1) to "set and fix", in the sense of prescribing, a maximum rate of return. NLP had submitted that the Board's power to deal with excess earnings comes solely from its statutory powers to prescribed the form of accounts to be maintained by the utility[FN58] and to create a reserve fund "for a purpose which the Board thinks appropriate"[FN59] which could include the purpose of dealing with excess returns. This argument has already been rejected in the analysis relating to Question 1. It follows, therefore, that the issue of excess earnings may present itself for consideration by the Board in circumstances even where a reserve account has not been ordered to be set up. For the purpose of regulation by the Board, the

concept of excess earnings is derived from the process of prescribing a just and reasonable return on rate base and not by the decision to require the creation of a reserve account. The question to be considered is what enforcement mechanisms the Board may use to deal with excess earnings so identified.

74 If, as determined in the answer to Question 1, the Board has jurisdiction flowing from s-s. 80(1) to prescribe the maximum rate of return which a utility may earn in a given year, it is a necessary consequence of such a determination that revenue earned in excess of the maximum of the prescribed range of return is excess revenue to which, by definition, the utility will not be entitled. The Board accordingly must have jurisdiction to regulate how that excess revenue is to be dealt with.

75 Question 3 requires the Court to consider the range of enforcement mechanisms which the Board may employ to ensure that the utility does not benefit from any windfall profits resulting from earnings in excess of the just and reasonable return to which it is entitled. Three scenarios are proposed:

(1) use excess earnings to reduce revenue requirements for the succeeding year ("Revenue Reduction Approach");

(2) place the excess earnings in a reserve fund to enable an adjustment of rates, tolls and charges at a future date ("Reserve Fund Approach");

(3) require a rebate of excess earnings to consumers ("Rebate Approach").

Question 4 is really a subset of the Revenue Reduction Approach. In one sense it really asks the same question as in Question 3(i) but does not limit the process to the application of excess earnings to only the year next succeeding the year in which the excess earnings have been achieved. It appears to ask the Court to address the question of whether, in the absence of the existence of a reserve account, the Board may, upon being made aware of excess earnings in prior years, reach back into those prior years and take account of those excess earnings by using them to reduce rates, tolls and charges in subsequent periods below what would otherwise be indicated.

76 In approaching these questions, it is important to bear in mind the nature of the rate setting process and the general principles which are recognized as being applicable to govern the manner in which that process is carried out.

77 The process of rate setting is generally prospective by nature. Although the Board must set rates for the future, it only has data from past experience, the evidence from utility officials as to planned changes in operations and the opinions of experts as to future economic trends as a guide to what the revenue requirements of the utility will likely be. It is, therefore, necessarily speculative. In developing the utility's requirements, the Board focuses on a "test year" as the basis for its estimates and adjustments. Traditionally, in North America the test year was chosen as the latest 12 month period for which complete data were available.[FN60] More recently, due largely to inflation, boards adopted a forward-looking test year which in effect amounts to a forecast of what expenses and costs, and hence revenue requirements, will be. This has been the practice of the Board[FN61] and is supported by the Act[FN62] and the *EPC Act*[FN63]. Past experience of course remains relevant, however, insofar as it gives insight into the possibility of forecasting error.[FN64]

78 Because the process is prospective, there is a good possibility that all of the assumptions will not be achieved in practice. The actual rate of return may therefore differ from the rate, or range of rates, prescribed at

a previous hearing. On paper, this difference may appear to redound to the benefit or detriment of the utility depending upon whether the actual rate is greater or less than the rate or range prescribed.

79 When, as a result of actual experience, it appears that the actual rate of return was greater than the rate prescribed for the same period, it becomes necessary to address what the Board can do, if anything, to ensure that the earnings in excess of the prescribed level, (which by definition will be regarded as greater than a just and reasonable return on the rate base), are not allowed to remain with the utility or its investors. In the *Bell Rebate* case[FN65], Gonthier, J. observed that differences between projected and actual rates "call for a high level of flexibility in the exercise of the [Board's] regulatory duties".

80 Those opposing a broad jurisdiction on the part of the Board to define and deal with excess revenue couch the objection, at least in part, in terms of a violation of the non-retroactivity principle.[FN66] In its narrow sense, it is a principle of benefit to consumers, that "today's rate payers should pay the cost of today's services and not the cost of past or future services"[FN67]. More broadly, it also yields a presumption (which is of benefit to the utility as well), flowing from the idea that the Board acts prospectively in setting rates, that the Board cannot or, even if it has jurisdiction, should not as a general rule, make orders that have the retroactive effect of disturbing existing rights already enjoyed by the utility. In practical terms, it leads to the argument that where rates, tolls and charges have been approved by the Board as being permissible for the utility to charge, the Board cannot or should not make a subsequent order that has the direct or indirect effect of reducing or otherwise changing those rates. In other words, changing past transactions or attaching new consequences to past transactions would be prohibited.

81 As Penning points out[FN68] the retroactivity rule has its genesis in general rules of statutory interpretation that guard against interpreting a statutory provision as having a retrospective operation unless it is clear that such an effect was intended. It is not an immutable rule but can give way to contrary legislative intention.

82 Doctrinally, in the context of utility rate regulation, the retroactivity principle is described by Penning in this way:

> ...the rule is concerned more with issues of fairness, both to customers and to utility shareholders. The customer-related fairness issue is often referred to as the "inter-generational equity" problem, which, broadly stated, means that today's customers ought not to be held responsible for expenses associated with services provided to yesterday's customers. The fairness concern in terms of utility shareholders arises because to attract and maintain reasonably-priced equity investment in a utility, shareholders require some certainly that matters already dealt with by the regulator have some degree of finality associated with them. [FN69]

83 It was argued that one of the questions that is theoretically presented in this case is the degree to which the Board is authorized to trespass on the no-retroactivity principle in fulfilment of its legislative powers, specifically, to enforce a prescription that a utility may earn a just and reasonable return and no more.

84 In reality, however, in light of the prospective nature of this Opinion, the non-retroactivity principle is not, in practical terms engaged by Question No. 3. The answers to previous questions have already established that the concept of excess revenue is to be determined by reference to the meaning of a "just and reasonable return" as that phrase is understood in ss. 80(1); and not by the definition used to operate an excess revenue account. All participants in the regulatory process must therefore take account of that concept and conduct their

activities accordingly. The "rules of the game" are known.

85 Section 59 of the Act requires the utility, unless otherwise ordered by the Board, to close its accounts at the end of each calendar year and to file with the Board its balance sheet, together with such other information as may be required by the Board, before April 2nd of the following year. Effectively, therefore, within 3 months after the utility's year end, both the utility and the Board will know the financial position of the company for the previous year and from that, as well as any other information which the Board may require, a determination of the actual level of return earned by the utility in the previous year can be made. Applying the known definition of excess revenue, by reference to the upper end of the range of return on rate base, as determined by the Board's prior orders under ss. 80(1), it can be determined whether there has been any excess revenue earned. There is no revisiting and revision of a prior order respecting the allowable return on rate base. The examination of actual results in the context of a comparison with the previously prescribed rate merely leads to enforcement of the original order. Any decision by the Board with respect to disposition of excess revenue will therefore not retroactively interfere with past revenues which the utility assumes belong to it and which may be disbursed to shareholders or otherwise spent. Given the concept of excess revenue, as explained in this option, the utility knows in advance that it is not entitled to excess revenue so defined and may institute whatever accounting practices are necessary to segregate and deal with such revenues pending direction from the Board.

86 The situation is conceptually no different from the concept behind an excess revenue account set up under ss. 69(3), which the utility accepts as a legitimate way of dealing with such revenue. Just as in the case of an excess revenue account, the definition of excess revenue is known in advance and the utility can account for such revenue accordingly.

87 The scenario contemplated by Questions 3 & 4 is unlike the situation which arises where an interim order setting rates, tolls and charges is subsequently superseded by a final order, resulting in excess revenue being earned in the intervening period because the rates, tolls and charges charged in that period pursuant to the interim order were higher than those which were ultimately found to be justified in the final order. In that situation, if the final order is treated as being operative as and from the date of the interim order that was superseded, the final order will, indeed, have a retroactive effect. In the context of the Newfoundland legislation, that situation is specifically contemplated and authorized by ss. 75(3) of the Act.

88 In the situation presently under consideration, however, there is no subsequent order of the Board which retroactively changes previously-approved rates, tolls or charges or revises the prescribed level of return to which the utility is entitled. All that occurs is the subsequent examination of actual results and a determination of whether excess revenue was in fact earned by applying a pre-existing standard derived from a previous Board order made under ss. 80(1).

89 I recognize that, to the extent that the utility in the past may have been operating under the impression, perhaps engendered by positions taken by the Board, that excess revenue need only be calculated by reference to the excess over the rate of return on common equity as defined for the purpose of operating the existing excess revenue account, it may consider that if the concept of excess earnings as discussed in this Opinion is applied at this stage to those previous years, there may effectively be a change in the "rules of the game". In that practical sense, there would be a "retroactive" readjustment.

90 The Court is not being asked, however, to determine the position of the utility specifically in relation to the years 1991 through 1996 and to determine the entitlement of the utility to excess revenues as calculated by

reference to the current definition. The degree of NLP's misapprehension, if any, the actions of the Board in dealing with the excess revenue issue in the past, the degree to which NLP may have acted to its prejudice, and the degree to which the utility may nevertheless be required to disgorge excess revenues in previous years in accordance with presently understood concepts raise complex issues of mistake of law in the law of restitution and the defence of change of position which require for their resolution a detailed factual base. It would be inappropriate to attempt to answer such questions in this Opinion.

91 The issue, therefore, is not whether the Board may revise the definition of excess revenue and then apply the revised definition to the results of previous years. That might well engage the principle of non-retroactivity. Here, assuming (without deciding) there was a misapprehension in the past as to how excess revenue should be calculated, the "change" in calculation method comes about, not because of a retroactive change in the rule by the Board but by a (perhaps) unanticipated declaration and clarification by the Court of what the law is and how it is or should be applied.

92 I turn now to the determination of the powers of the Board to deal with excess revenue once it has been determined to exist.

93 The only express provisions of the Act dealing with excess revenue are s-s. 69(4) which provides a power to require a utility to refrain from distributing extra revenue as dividends until further order, and s-s. 75(3) which enables the Board to order that excess revenue earned as a result of an "interim order" made under s-s. 75(1) and not confirmed by final order be either refunded to customers or placed in a reserve account for an approved purpose. Does the fact that similar powers are not expressed in respect of "final" orders mean that they were not intended to be available?

94 I do not believe so. The power to deal with excess revenue is inherent in the nature of the regulatory scheme the Board is required to administer. The starting point is the power, found to exist in the answer to Question 1, that the Board may prescribe a rate of return under s-s. 80(1) which carries with it the necessary corollary that the utility is only entitled to earn that level of return, as determined by the Board to be just and reasonable. It follows that unless the Board is to be a "toothless tiger" it must be accorded the means by which revenues earned in excess of the prescribed level of return are used in furtherance of the objectives and policies of the legislation and not simply for the benefit of the utility's investors. Such policies as the maintenance of a sound credit rating by the utility[FN70], the efficient production, transmission and distribution of power[FN71], the delivery of power at the lowest possible cost[FN72] and the provision of reliable service[FN73] are all candidates for the use of the excess. It does not follow, as the Consumer Advocate argued, that any dealing with the excess should involve only a return or rebate to consumers so as to ensure that the goal of delivery of low cost power is vindicated. While the maintenance of low rates is an important objective of the legislation, it is not the only one. As emphasized earlier,[FN74] the Board is always engaged in a balancing exercise between the interests of the consumer and the interests of the utility. It is not correct to say that any revenues earned in excess of a just and reasonable return belong to the consumer. Just as the utility is not "entitled" to earn and retain revenues in excess of such a level of return, so also the consumer is not absolutely "entitled" to the excess. The Board, having identified that an excess exists, must deal with it in furtherance of the objectives of the legislation.

95 The means whereby the excess is dealt with should not be, unless expressly limited by the legislation, rigidly prescribed provided the means chosen comport with the objectives and policies of the legislation. It is worth repeating Gonthier, J.'s observation in the *Bell Rebate* case that the fact that the differences between

projected and actual rates of return are common calls for "a high level of flexibility in the exercise of the [Board's] regulatory duties".[FN75]

96 Counsel for NLP argued that the only power of the Board to deal with excess revenue, aside from interim order situations, flows from its power in s. 58 to prescribe the form of books and accounts to be kept by the utility and that, if it ordered, pursuant to s-s. 69(3), the creation of a reserve fund "for a purpose which the Board thinks appropriate", it could stipulate that the accounts should be kept in such a way as to require excess revenues to be accounted for in such a reserve account. I do not find the jurisdiction to deal with excess revenue in the power to prescribe the utility's accounts. That is only a procedural means of exercising powers, the jurisdiction for which must be found elsewhere. Whilst the creation, pursuant to s-s. 69(3), of a reserve fund to deal with excess revenues could be said to be "a purpose which the Board thinks appropriate" (provided that purpose is consistent with the powers otherwise conferred on the Board), there is nothing in the language of s-s. 69(3) which expressly makes it applicable to an excess revenue situation and there is certainly nothing there which would purport to make the use of a reserve fund for the purpose of dealing with excess revenue as the only mechanism which would be at the Board's disposal to deal with this issue.

97 I conclude that, bearing in mind the approach to interpretation mandated by s-s. 118(2) of the *Act*, the Board must of necessity have broad powers to deal with revenue earned by a utility in excess of the prescribed rate of return. Inasmuch as the ascertainment of the existence of excess revenue can only be made following a subsequent review, any order dealing with excess revenue will of necessity have certain retrospective elements about it. But that is not the same as saying that an order dealing with excess revenue ascertained by application of a pre-existing concept of what constitutes excess revenue is a retroactive order. It was argued by NLP that the setting up of a reserve account would be the only method that would not involve any trespass on the principle of non-retroactivity because the utility would know in advance that it had to set up its reserve account and could therefore provide for it without running the risk of spending or distributing excess revenues in ignorance of the fact that they would have to be held accountable for them.

98 For reasons already given, this argument is unconvincing. By virtue of the answers given to Question 1, the utility knows that it is only entitled to earn a just and reasonable rate of return pursuant to any order made by the Board to that effect under s-s. 80(1). It can monitor its financial progress and can organize its accounts in such a way as to account for excess revenue so as to prevent the possibility of it being disposed of before any subsequent order dealing with the excess may be made. The utility does not need an express order of the Board requiring it, as a general rule, to set up a reserve account for this purpose. Nevertheless, the use of a reserve account is a convenient way of doing this. It may well be, however, that the Board may, through other directions with respect to the manner of keeping accounts, develop other accounting procedures that will enable the utility to identify excess returns and to segregate them for other use.

99 A reserve fund could be ordered by the Board to be used in the future to improve service, or to keep rates low or for some other purpose that is consistent with the objectives and policies of the legislation. Whether the advancement of these policies is done formally through the use of a reserve fund or through some other mechanism such as an order setting further rates, tolls and charges taking the prior excess revenue into account, the utility should not be prejudiced, in light of the fact that it knows that it is not entitled to earn a return in excess of a just and reasonable return.

100 A rebate to consumers would also be permissible since it would have the indirect effect of ex post facto keeping the rates low. While it is true that any rebate would not, because of the fluid nature of the customer

base, result in a return to exactly the same body of consumers who had paid the original rates, this is not an insuperable objection to using this type of mechanism. Penning[FN76] observes:

> As a practical matter, however, at least some of this concern appears misplaced. By far the majority of today's rate payers for the majority of regulated public service utilities were also yesterday's rate payers - especially since the time frames at issue are typically not more than a year or two. So the unfairness argument about cost allocation loses some of its force. Furthermore, to the extent it is still present, it can be dealt with through the choice of mechanism design - so instead of adjusting all rates, through either surcharges or refunds, the individual customers who met the timing criteria would receive an adjustment to their bill.

101 This recognition was echoed by Gonthier, J. in the *Bell Rebate* case[FN77] as follows:

> ...it is true that the one time credit ordered by the appellant will not necessarily benefit the customers who are actually billed excessive rates. However, once it is found that the appellant does have the power to make a remedial order, the nature and extent of this order remain within its jurisdiction in the absence of any specific statutory provision on this issue. The appellant admits that the use of a one time credit is not the perfect way of reimbursing excess revenues. However, in view of the cost and the complexity of finding who actually paid excessive rates, where these persons reside and of quantifying the amount of excessive payments made by each, and having regard to the appellant's broad jurisdiction in weighing the many factors involved in apportioning respondent's revenue requirement among its several classes of customers to determine just and reasonable rates, the appellant's decision was imminently reasonable...

102 Accordingly, I conclude that each of the Revenue Reduction, Reserve Fund and Rebate approaches to dealing with excess returns are within the jurisdiction of the Board and could, in particular circumstances, all constitute reasonable responses to a finding that the utility has earned in excess of a just and reasonable return.

103 I would also add that the setting up of a reserve fund in a given case does not exhaust the ways in which the Board may deal with excess revenue. The methodologies proposed are not mutually exclusive. The Board has jurisdiction to deal with all revenue in excess of a just and reasonable return on rate base using one, or a judiciously blended combination, of the methodologies identified.

104 Having said that, it must be emphasized that just because the Board has the jurisdiction to use these approaches, the particular circumstances may well dictate that one or more of them may be inappropriate in a given case. For example, the ordering of a rebate to consumers of the total amount of an excess return might not, in the light of the general financial condition of the utility, be appropriate when measured against such legislative objectives as the maintenance of the utility's sound credit rating. It might be appropriate, when all of the interests are properly balanced, for the Board, for example, to order that only the excess over a stipulated rate of return on equity, or some other measure, be refunded or otherwise dealt with. These are all matters to be considered by the Board in a given case.

105 The answers to Questions 3 and 4 can be given as follows:

As to: 3(i) - Yes

3(ii) - Yes

3(iii) - Yes

106 The answer to Question 4 is also "yes" on the assumption that what is being asked is not whether the Board may retroactively revise a previous order but merely whether, applying a defined and understood concept of excess revenue, (ie. an excess of a just and reasonable return on rate base) the excess so determined to have existed in prior years may then be taken account of and applied in setting future rates, tolls and charges.

Question 5

Does the fact that the Board has advised the public utility that it is permitted to retain earnings in excess of the rate of return determined by the Board to be a just and reasonable return, upon the rate base as fixed and determined by the Board for each type of service supplied by the public utility, but not in excess of the return determined by the Board to be a just and reasonable return upon the investment which the Board has determined has been made in the public utility by the holders of common shares, affect the jurisdiction of the Board to approve rates, tolls and charges on the basis queried in Question (4).

107 In order to understand the import of this question, it is necessary to review the approach taken by the Board to the definition of excess earnings in past years.

108 In correspondence passing between NLP, Newfoundland Telephone Company Limited (which at that time was regulated by the Board) and the Board during the late 1980's, there was considerable discussion as to the manner of defining "excess revenue" for the purpose of the operation of the reserve account which the Board had required the utilities to maintain for that purpose. As a result of these discussions, the Board approved a change in the utilities' systems of accounts to recognize a new definition of excess earnings. As indicated, this was accomplished by defining the excess revenue account in the utilities' system of accounts as follows:

This account shall be credited with any revenue in excess of the maximum return on common equity determined by the Board at the previous rate hearing to be refunded to customers or used for such purposes as the Board may order.

109 By the operation of this definition, the situation could occur whereby the utility might earn a rate of return on rate base in excess of the maximum range of returns determined by the Board pursuant to s-s. 80(1) but could nevertheless be within the range of return on common equity used by the Board for the purpose of determining a just and reasonable return on rate base under s-s. 80(1). If that eventuality occurred, there would be no requirement on the utility to pay anything into the excess revenue account; yet, the result would be that the utility would have earned more than a just and reasonable return on rate base. In light of the answer given to Question 1, the benchmark for determining excess revenue is the range of return on rate base determined by the Board to be just and reasonable. Does the Board have jurisdiction to deal with this money as excess earnings in light of the fact that it has defined excess earnings for the purposes of the utility's accounting by reference to the maximum return on common equity?

110 Question 5, we were told, attempts to address this issue. As phrased, however, the question merely asks whether the fact that the Board has "advised" (presumably, in the form of its order changing the definition of excess revenue for the purposes of the establishment of the excess revenue account) the utility of this new definition of excess revenue "affect" the jurisdiction of the Board to approve rates, tolls and charges. The short answer to this question, strictly construed, is "no". The Board cannot limit its jurisdiction, in the sense of its legal power, by determinations made in exercise of its powers. It either has the jurisdiction or it does not.

Whether it chooses to exercise the jurisdiction is another matter.

111 As a result of the discussions at the hearing, however, it is apparent that there is a more fundamental issue at stake. The assumption appears to be that if the Board chooses to define excess revenue for the purpose of establishment of the excess revenue account in terms of revenue earned in excess of the maximum return on common equity, it is in effect saying that revenue earned below that maximum but which happens to be in excess of the just and reasonable return on rate base as determined by the Board under s-s. 80(1) is necessarily money which the utility can keep. This position is obvious from the arguments made by counsel for NLP since his position has been throughout that excess revenue has no meaning other than by reference to the definition used for the purposes of the excess revenue account. As indicated previously,[FN78] this is not a correct interpretation of the situation. The same assumption is also apparent from the position taken by the Consumer Advocate who argues that the decision of the Board to define excess revenue for the purpose of the excess revenue account in terms of exceeding the return on common equity, as opposed to rate base is ultra vires the Board because the Board must determine excess revenue by reference to revenues which are earned in excess of a just and reasonable return on rate base.

112 The assumption that the definition of excess revenue for the purpose of the operation of the reserve account is equivalent to the concept of excess revenue flowing from earnings in excess of a just and reasonable return on rate base as prescribed under s-s. 80(1), is false. I agree with the Consumer Advocate, for reasons already given[FN79], that any revenues earned in excess of the maximum range of a just and reasonable return on rate base are revenues to which the utility is not automatically entitled. It does not follow, however, that for the purposes of regulating the accounts of the utility, the Board is prevented from requiring payment into an excess revenue account on a different basis (provided it does not deprive the utility of the level of return on rate base to which it has been determined to be entitled). The Board can and should deal with all revenue earned in excess of a just and reasonable return on rate base; however, it does not have to require that all of it be paid into an excess revenue account.

113 As indicated in the answer to Question 3 and 4, the Board has a broad jurisdiction as to how to deal with the excess and it may well be that, in the circumstances obtaining, it will determine that only a portion (i.e. that portion above the maximum return on common equity) should be paid into a reserve account. It might determine that the rest should be rebated to consumers or used by the utility in furtherance of the objective of ensuring that it maintains a sound credit rating in the financial markets of the world. In short, there is nothing wrong in principle with the Board defining excess revenue for the purposes of a reserve account differently from the notion of excess revenue as determined by a comparison with a just and reasonable return on rate base as determined by s-s. 80(1). In so doing, however, the Board ought not to assume that any additional excess revenue ought necessarily to be returned to the utility to be used as it sees fit. The Board has jurisdiction, and in exercise of its legislative mandate it ought to exercise that jurisdiction, to make a determination as to how that remaining excess revenue, if any, should be dealt with consistent with the objectives and policies of the legislation.

114 Accordingly, the technical answer to Question 5 is "no" but so as to limit any confusion over the implications of the wording of the question, I would add that the Board has jurisdiction to define excess revenue for the purposes of maintenance of a reserve account by reference to the maximum level of return on common equity (or any other appropriate measure for that matter) but that does not mean that the Board may for all purposes define the level of excess revenue to which the utility is not entitled by reference to that measure; rather, the Board must determine, on the specific circumstances of the case, what is to be done with respect to

any excess revenue measured against a just and reasonable return on rate base. If all or a portion of the excess revenue, measured against the return on rate base, is not ordered to be paid into a reserve account, it must nevertheless be dealt with in some other manner consistent with the objects and policies of the legislation. It should not be simply assumed that such excess revenue if not required to be paid into a reserve account belongs to the utility to be dealt with as it sees fit.

Question 6

> Does the Board have jurisdiction to order the rates, tolls and charges of the public utility shall be approved taking into account the amount of expenses previously incurred by the public utility which the Board may now consider inappropriate to be allowed as reasonable and prudent and properly chargeable to operating account notwithstanding that such classes of expenses were allowed as reasonable and prudent and properly chargeable to operating account.

115 The just and reasonable return on rate base which the Board determines that the utility is entitled to earn annually is "in addition to those expenses which the Board may allow as reasonable and prudent and properly chargeable to the operating account..."[FN80]. Thus, in the process leading up to the prospective setting of rates, the Board may look at the type and level of projected expenses of the utility in the test year and determine whether they are reasonable and, if not, only allow, for the purposes of calculation of a just and reasonable return on rate base, such types and levels of expenses as are, in the opinion of the Board, reasonable.

116 In the 1991 rate hearing, certain types and levels of projected advertising expenses were approved by the Board. At the 1996 rate hearing, it was suggested that in the light of what actually happened in the years subsequent to 1991, the utility had in fact incurred advertising expenses well in excess of the amounts approved as reasonable and also of a type different from those which were approved, i.e. for corporate image building rather than related to the supply of service. The issue posed by Question No.6 is whether expenses of a class which were previously approved as reasonable but which are in excess of the projected amounts can be disallowed by the Board for the purposes of rate regulation.

117 The level of operating costs is obviously an important factor in fixing rates. It is generally accepted that Board supervision as to reasonableness of such costs is therefore essential to effective regulation.[FN81] Phillips describes the matter thus:

> Commissions seldom challenge expenditures controlled by competitive forces, such as those for plant maintenance, raw materials and labor. Conflicts do arise over whether certain expenditures should be charged to operating expenses or paid for by owners out of earnings.
>
> Management might vote itself high salaries and pensions. Payments to affiliated companies for fuel and services might be excessive. Expenses for advertising, rate investigations, litigation and public relations should be closely scrutinized by the commissions to determine if they are extravagant or if they represent an abuse of discretion. In all cases, moreover, the commissions should require proof as to the reasonableness of a utility's charges to operating expenses.[FN82].

Accordingly, the power to determine reasonable rates necessarily requires supervision of operating expenses.

118 In defining the parameters of such supervisory power, however, the Board must account for a competing principle, namely, that the Board is not the manager of the utility and should not as a general rule

substitute its judgment on managerial and business issues for that of the officers of the enterprise[FN83].

119 Nevertheless, it is recognized that regulatory boards have a wide discretion to disallow or adjust the components of both rate base and expense[FN84]. In an American case[FN85] the matter was put as follows:

> The contention is that the amount to be expended for these purposes is purely a question of managerial judgment. But this overlooks the consideration that the charge is for a public service, and regulation cannot be frustrated by a requirement that the rate be made to compensate extravagant or unnecessary costs for these or any other purposes.

120 Having said that, however, there will normally be a presumption of managerial good faith and a certain latitude given to management in their decisions with respect to expenditures. In the United States, the test for disallowance is usually "abuse of discretion" showing "inefficiency or improvidence" or "extravagant or unnecessary costs".[FN86].

121 When the issue becomes a retrospective examination of actual expenses as compared with what was projected and determined to be reasonable and prudent, there ought, similarly, to be caution exercised before determining that an expense was improperly incurred. The circumstances facing a utility are not static and a considerable latitude has to be given to the decisions of management in making expenditures to respond to the new situations as they present themselves.

122 Nevertheless, it is still within the jurisdiction of the Board to supervise and review both the type and level of expenses incurred by the utility in respect of its operations. If it did not have that jurisdiction, the actual rate of return earned on rate base in a given year would be subject to manipulation by the utility as, for example, in a year where near the close of the fiscal period it appears that the rate of return will be more than anticipated, the utility, if totally unsupervised, could make large expenditures, unrelated to the delivery of service, simply to bring the rate of return in line with what had been projected.

123 The jurisdiction of the Board to take account of deviations from estimates of expenses when setting future rates does not differ from that pertaining to its jurisdiction with respect to taking account of excess revenue. The disallowance of an expense may lead, in effect, to a greater rate of return, and potentially to excess revenue if the resulting actual adjusted rate of return is in excess of the previously determined acceptable range of return. The excess revenue over a just and reasonable range of return on rate base can be dealt with by the Board as discussed in the answers to Questions 3 and 4. It does not remain the property of the company.

124 Accordingly, the answer to Question 6 is "yes". In giving this answer, however, I would emphasize that the question that was asked is a jurisdictional one. It does not give, in the circumstances of a particular case, a wide unfettered power to "second guess" managerial decisions with respect to expenses. In this regard, I agree with the comments of Phillips:

> Public utilities ... cannot spend freely and expect all expenditures to be included as allowable operating expenses. In effect, this means the commissions are permitted to question both the judgment and integrity of management. And if rates must be high enough to yield sufficient revenue to cover all operating expenses, the consumer has the right to expect that such expenditure will be necessary and reasonable.
>
> At the same time, managerial good faith is presumed. Public utilities must be given the opportunity to prove the necessity and reasonableness of any expenditure challenged by a commission (or intervenor). To justify

an expenditure, a company must show that the expenses was actually incurred (or will be incurred in the near future), that the expense was necessary in the proper conduct of its business or was of direct benefit to the utility's rate payers, and that the amount of the expenditure was reasonable. Moreover, it must be emphasized again that a public utility may still spend its money in any way it chooses. Management's function is to set the level of expenses; the commission's duty is to determine what expense burden the rate payer must bear.

Question Nos. 7 and 8

(7) Does the Board have jurisdiction to require a public utility to maintain:

(i) a ratio; or

(ii) a ratio within a stated range of ratios

of equity and debt, as the means of obtaining the capital requirements of the public utility.

(8) Does the Board, upon an application pursuant to Section 91 or otherwise, have the jurisdiction to require a public utility to obtain its capital requirements by the issue of specific financial instruments, whether common shares, preferred shares, stocks, bonds, debentures or evidence of indebtedness payable in more than one year.

125 These two questions will be considered together because the issues they raise are interrelated.

126 In theory, both the overall level of capitalization and the individual components of a utility's structure are of interest to regulatory boards. Clearly, if a utility is allowed to engage in financing practices which result in overcapitalization, the whole viability of the enterprise may be threatened with consequent impact on the delivery of service to the public.

127 Furthermore, unlike in competitive conditions where the enterprise would not be able effectively to raise its prices over those of its competitors even if its costs of capital were excessive, overcapitalization of a regulated utility may well affect rates. That is because, in principle, rates must be set at such a level as to allow for recovery of the utility's costs, including its costs of capital, as well as a just and reasonable return. Overcapitalization, if uncontrolled, would increase the utility's costs and hence its rates. If the utility is not permitted to recover its costs in this regard it will, like any unregulated business, face bankruptcy with the consequence of disruption of service to customers. Overcapitalization may therefore indirectly put an upward pressure on rates to ensure the continued viability of the utility to enable service to be maintained. Alternatively, service may suffer.

128 Arguably, the purpose of s. 91 of the *Act* is to enable the Board to control the risk of overcapitalization and its impact on the viability of the utility, or at least on its credit standing. By examining each proposed new security issue in advance, the Board has a chance of minimizing the adverse effects of overcapitalization before the occur.

129 The composition of a utility's capital structure, that is, the mix of debt and equity, is also a matter that is necessarily of interest to regulatory boards.

130 Because the costs of the individual components of a utility's capital structure, i.e. the embedded costs of

debt and preference shares and the reasonable rate of return on common equity, are given a weighted cost, proportional to their share of the total capital structure, for the purpose of deriving a reasonable rate of return on rate base, the level of the actual proportional share of each component will necessarily have an effect on the result of the overall determination of a just and reasonable return on rate base. The makeup of the utility's capital structure can therefore influence that determination.[FN87]

131 Phillips[FN88] expresses it this way:

> ...the traditional theory of business finance holds that the average cost of capital to a firm varies with the capital structure upon which it is based. The interest rate on debt is normally lower than the cost of equity capital. Consequently, within limits determined by such factors as the risk of a business, the overall cost may be somewhat lower when the debt-equity ratio is high than when the debt-equity ratio is low.

It is too simplistic, however, to say that in all cases, the higher the debt equity ratio, the lower will be the overall costs of capital. As deGrandpré[FN89] points out:

> It is often argued that if utilities increased their debt ratio, their cost of capital would be reduced since the cost of debt is less than the cost of equity. This may be true, but then the rate of return would have to be increased under the risk factor since the interest has to be paid before dividends and the investor might find himself deprived of dividends because of insufficient earnings.

The debt equity ratio can, therefore, have a complicated effect. What is undeniable, however, is that the debt-equity mix does have an effect on the rate of return. Hence, it is something which, in principle, should come within the regulatory umbrella in fulfilment of the policies of keeping the costs to consumers low and of ensuring a sound credit rating for the utility. The higher the cost of capital, the higher will be the return necessary to be awarded to the utility to enable it to maintain a sound credit rating in world financial markets. This would inevitably lead to higher rates, tolls and charges which would work against the policy of providing power to consumers at the lowest possible cost consistent with reliable service.

132 From this, the Consumer Advocate and the Board itself argued that it is a necessary and appropriate power on the part of the Board to regulate the ratio of debt to equity in a utility's capital structure. Without such a power, the Board is limited, it was suggested, in its ability to ensure that sources and facilities for the production, transfer and distribution of power are managed and operated in a manner that would result in power being delivered to consumers at the lowest possible cost consistent with reliable service.

133 In like manner, it was argued that the Board has the power, as a necessary incident of the legislative scheme, to stipulate, from time to time, that a public utility must obtain its capital requirements by the issue of financial instruments of a specified nature.

134 Granting that the level of overall capitalization and the composition of the capital structure of a utility are both matters of regulatory concern, at least insofar as they affect the utility's rate of return on rate base and hence the cost to consumers of the delivery of reliable service, the question to be determined is the degree of intrusion which the Board may undertake into the financial affairs of the utility. Can it be proactive and, as Question 7 suggests, "require" the utility to maintain a particular debt-equity ratio or, as Question 8 implies, "require" the utility to finance its activities in a particular way, or is it limited to passive disallowance of particular financing in a particular financing proposals either in the process of setting rates or in the course of other applications?

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

135 In approaching these questions, it has to be remembered that there is no such thing as one ideal capital structure. It is a function of economic conditions, business risks and "largely a matter of business judgment". [FN90] Furthermore, a given capital structure cannot be changed easily or quickly. As well, the long-term effects of changes on capital structure on the enterprise and on the future cost of capital may not be easily predictable. Capitalization decisions also have other business dimensions that transcend the considerations relevant to this issues directly presented in the regulatory process.

136 All of these considerations favour an approach that, in principle, should limit the degree of intrusion by the Board into the managerial control by the utility over financial decision-making. As emphasized earlier [FN91] the powers of the Board should be generally regulatory and corrective, not managerial. A debate has nevertheless occurred over whether regulatory agencies can and should "fix" debt-equity ratios and restrict new financing techniques to specified types of instruments.[FN92] Phillips notes that:

> These methods, however, have limitations. For example, since the financial conditions of individual utilities vary, no one ratio of debt to equity is correct. The refusal to approve a bond issue may lead to no issue at all, since, if a utility's earnings are insufficient to maintain its stock at par, it is in no position to issue more stock; bonds are the only way new capital can be raised. As a result of these problems, few commissions are willing to substitute their judgments for those of management...[FN93]

137 An alternative to actual intrusion into the utility's financial affairs in the form of a direction as to how the enterprise should be structured is for the regulator, *for the purpose of setting rates*, to base its estimates of the cost of capital on a hypothetical appropriate capital structure, thereby disregarding the utility's actual capitalization[FN94]. The justification for this approach is given by Phillips who, citing other authors, states:

> Locklin has argued that most commissions 'disregard actual capital structures and set up an ideal or normal structure for the purpose. To do otherwise would burden the public with the higher costs of obtaining capital that result from a capital structure that is something less than ideal, and may, in fact be quite unsound'. And Rose argues: 'When a commission in determining cost of capital disregards the actual capital structure or a capital structure proposed by management it is no more invading the domain of management than when it disregards unreasonable expenses for labor, fuel, or other productive factors in prescribing rates'.[FN95].

It appears, however, that actual capitalization has also been used as a basis[FN96]. Nevertheless, the arguments in favour of the ability of the Board to disregard the actual capital structure in an appropriate case and base its determination upon a hypothetical structure are convincing. Indeed, this has occurred in Canada.[FN97] Without such a power, the Board would not be able effectively to fulfill its mandate of promoting the delivery of reliable service to consumers at the lowest possible cost and at the same time maintaining a sound credit rating for the utility in the financial markets of the world. Having said that, in exercising that power, it goes without saying that the Board ought to have a healthy respect for managerial judgment[FN98] in such matters since if a hypothetical capital structure is used that is too far off the mark of the actual structure, it may in practical terms make the utility unable to meet its actual commitments, thereby threatening its credit standing and possibly affecting service to customers.

138 It is not necessary to go further, for the purpose of promotion of the objectives and policies of the legislation, and accord to the Board a power of actual intrusion into the capital structure of the utility. The distinction between actual intrusion and disallowance for rate making purposes is justified in the context of the existing legislation and enables the Board o respect the principle of general deference to managerial decisions.

139 The question that remains is whether s. 91 of the Act, which is the only provision expressly dealing with the powers of the Board respecting capital structure, can be said, either expressly, or by necessary implication, to accord greater powers to the Board.

140 On its face, s. 91 appears to be limited to a situation where the Board may approve or disapprove of a particular proposal from the utility for the issuance of a proposed form of securities. It is expressed in terms of a power of negative disallowance rather than positive direction.

141 As noted previously[FN99], s. 91 enables the Board to control the level of overall capitalization. Is that the only purpose for which a disallowance under s. 91 can be made? Obviously, an indirect effect of an approval or refusal of a particular security issue could be to affect the utility's future proposed debt-equity ratio and hence the composition of its capital structure. In practical terms, the power to disallow a specific proposal will enable the Board to exercise at the very last, by means of moral suasion in discussion, a degree of positive influence over total capitalization as well as capital structure. The power of disallowance under s.91 may, in my view, be used, in appropriate cases, to further such objectives. Subsection 91(3) requires the Board, before approving a security issue, to be satisfied that it is in accordance with law and "for a purpose approved by the Board". Accordingly, so long as the power of approval or disallowance under s. 91 is exercised in a manner that is consistent with and in furtherance of any of the policies which the legislation was designed to serve, it will be within the jurisdiction of the Board to so act. In what way, the Board may influence the total level of capitalization as well as the particular debt-equity ratio. It does not, however, permit the Board to direct the utility to raise money in a particular way or to maintain a particular debt-equity ratio. In other words, it cannot be used as a springboard for an aggressive intrusion into the day to day financial and managerial decision making of the utility with respect to the capital structure of the enterprise. Nor can the general policies underlying the legislation justify such a power. As indicated, financing is undertaken for considerations that are not necessarily directly related to utility regulation. Furthermore, it has also been noted that, within the regulatory context, the utility is still subject to business risks and the effects of management decisions and the utility, other things being equal, ought to have the power to respond to that zone of risk. To that extent, the utility must be able to make financial decisions related to the overall health of the enterprise for reasons other than strictly regulatory ones, provided that in so doing it does not trespass on the objectives and policies of the legislation.

142 Accordingly, while recognizing that a degree of influence over the utility's capital structure and over the choice of financial instruments to be used in financing the enterprise can be exercised by means of the powers conferred by s. 91 and the powers inherent in the regulatory scheme itself, the answers to Questions 7 and 8, insofar as the questions imply an ability to directly stipulate particular financing results, is, in each case, "no".

General Observations

143 In answering the foregoing questions, it is worth emphasizing that the answers are given in terms of the jurisdiction of the Board. The fact that the Board may have jurisdiction, in the sense of legal power, to do something does not mean that, in a particular case, the power ought to be exercised. In the arguments which were presented on the hearing of the stated case, it was apparent that some of the positions taken by a party were being advanced out of a concern that if the jurisdiction was conceded, it would necessarily follow that the Board would exercise its power in a manner adverse to that party.

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

144 The question of whether the Board should in fact exercise powers within its sphere of jurisdiction and the question of the manner in which those powers should be exercised raise very different considerations. It must always be remembered that, as has been emphasized throughout this opinion, the Board is charged with balancing the competing interests of the utility and the consumers of the service it provides. Neither set of interests can be emphasized in complete disregard of the interests of the other. Thus, in choosing to exercise a particular power within the Board's jurisdiction, the Board must always be mindful of whether, in so acting, it will be furthering the objectives and policies of the legislation and doing so in a manner that amounts to a reasonable balance between the competing interests involved.

Opinion

145 Pursuant to s. 101 of the *Act*, I would summarize my opinion on the questions posed as follows:

Question 1(i) Yes

Question 1(ii) No

Question 2 Yes

Question 3(i) Yes

Question 3(ii) Yes

Question 3(iii) Yes

Question 4 Yes

Question 5 No

Question 6 Yes

Question 7 No

Question 8 No

I emphasize that inasmuch as the import of the answers given depends on my interpretation of the questions posed, it is necessary to read the answers in the context of the rest of this Opinion.

146 Pursuant to s. 102, the Deputy Registrar of the Court is directed to remit this Opinion to the Board.

O'Neill, J.A.: (dissenting)

147 The Board of Commissioners of Public Utilities (the Board) is a statutory body existing under the provision of the Public Utilities Act, R.S.N. 1990, c. P-47, as amended (the Act).

148 The general powers of the Board are set out in s. 16 of the Act:

> 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 public utilities with the law and

shall have the right to obtain from a public utility all information necessary to enable the board to fulfil its duties.

149 In addition to the powers and obligations given to and imposed on the Board by the Act, the Board has certain duties and powers under the Electrical Power Control Act, 1994, Chapter E-5.1, as amended and, by s. 4 of that Act, is specifically directed to "implement the power policy" of the Province, as set out in s. 3 of that Act, and in doing so to apply tests "which are consistent with generally accepted sound public utility practice".

150 By s. 101 of the Act, the Board may, of its own motion, state a case in writing for the opinion of the Court upon a question which in the opinion of the Board is a question of law.

151 On August 14, 1996, the Board stated a case requesting the opinion of the Court with respect to certain specific questions as set out therein. Following an application for directions, the court ordered that, inter alia, certain parties be notified of the proposed hearing. Subsequently Newfoundland Light & Power Co. Ltd., a utility, and "the Consumer Advocate" were granted status to appear and be heard at the hearing before the court.

152 In its application to the Court, the Board stated that in the course of a hearing before it, the submissions of various parties raised questions as to the jurisdiction of the Board under the Act and the Board thereupon stated a case for the Court upon the following questions:

> (1) Does the Board have jurisdiction pursuant to the Act to set and fix the return which a public utility may earn annually upon:
>
> > (i) the rate base as fixed and determined by the Board for each type of service supplied by the public utility; and/or
> >
> > (ii) the investment which the Board has determined has been made in the public utility by the holders of common shares.
>
> (2) Does the Board have jurisdiction to set the rates of return referred to in Question (1) as a range of permissible rates of return.
>
> (3) Should a public utility earn annually a rate of return which is in excess of the rate of return determined by the Board to be just and reasonable, either on:
>
> > (i) the rate base as fixed and determined by the Board for each type of service supplied by the public utility; or
> >
> > (ii) the investment, which the Board has determined, has been made in the public utility by holders of common shares,
>
> does the Board have jurisdiction to:
>
> > (i) require the public utility to use the excess earnings to reduce revenue requirements for the succeeding year; or
> >
> > (ii) require the public utility to place the excess earnings in a reserve fund for the purpose of adjusting rates, tools and charges of the public utility at a future date; or

(iii) require the public utility to rebate the excess earnings to customers of the public utility?

(4) Does the Board have jurisdiction to order that the rates, tolls and charges of a public utility shall be approved taking into account earnings in excess of a just and reasonable return upon:

(i) the rate base as fixed and determined by the Board for each type of service supplied by the public utility, or

(ii) the investment, which the Board has determined, has been made in the public utility by the holders of common shares,

in prior years.

(5) Does the fact that the Board has advised the public utility that it is permitted to retain earnings in excess of the rate of return determined by the Board to be a just and reasonable return, upon the rate base as fixed and determined by the Board for each type of service supplied by the public utility, but not in excess of the return determined by the Board to be a just and reasonable return upon the investment which the Board has determined has been made in the public utility by the holders of common shares, affect the jurisdiction of the Board to approve rates, tools and charges on the basis queried in Question(4).

(6) Does the Board have jurisdiction to order the rates, tolls and charges of the public utility shall be approved taking into account the amount of expenses previously incurred by the public utility which the Board may now consider inappropriate to be allowed as reasonable and prudent and properly chargeable to operating account notwithstanding that such classes of expenses were allowed as reasonable and prudent and properly chargeable to operating account.

(7) Does nhe Board have jurisdiction to require a public utility to maintain:

(i) A ratio; or

(ii) A ratio within a stated range of ratios

of equity and debt, as the means of obtaining the capital requirements of the public utility.

(8) Does the Board, upon an application pursuant to Section 91 of the Act or otherwise, have the jurisdiction to require a public utility to obtain its capital requirements by the issue of specific financial instruments, whether common shares, preferred shares, stocks, bonds, debentures or evidence of indebtedness payable in more than one year.

Question #1

(1) Does the Board have jurisdiction pursuant to the Act to set and fix the return which a public utility may earn annually upon:

(i) the rate base as fixed and determined by the Board for each type of service supplied by the public utility; and/or

(ii) the investment which the Board has determined has been made in the public utility by the

holders of common shares.

153 It may be useful to set out here the relevant parts of ss. 37, 70 and 80 of the Act:

> 37 (1) A public utility shall provide service and facilities which are reasonably safe and adequate and just and reasonable.
>
> 70.(1) A public utility shall not charge, demand, collect or receive compensation for a service performed by it whether for the public or under contract until the public utility has first submitted for the approval of the board a schedule of rates, tolls and charges and has obtained the approval of the board and the shall be the only lawful rates, tolls and charges of the public utility, until altered, reduced or modified as provided in this Act.
>
> 80.(1) A public utility is entitled to earn annually a just and reasonable return as determined by the board on the rate base as fixed and determined by the board for each type or kind of service supplied by the public utility but where the board by order requires a public utility to set aside annually a sum for or towards an amortization fund or other special reserve in respect of a service supplied, and does not in the order or in a subsequent order authorize the sum or a part of it to be charged as an operating expense in connection with the service, the sum or part of it shall be deducted from the amount which otherwise under this section the public utility would be entitled to earn in respect of the service, and the net earnings from the service shall be reduced accordingly.
>
> (2) The return shall be in addition to those expenses that the board may allow as reasonable and prudent and properly chargeable to operating account, and to all just allowances made by the board according to this Act and the rules and regulations of the board.
>
> (4) The board may use estimates of the rate base and the revenues and expenses of a public utility.

154 In the past, the Board has ordered that a just and reasonable return for a utility is "determined" to be between two stated percentages of its annual rate base for a test year, and ordered the utility to file, for examination by the Board, a schedule of rates, tolls and charges which will comply with the Board's determination, and, if so found to comply, approval is granted for those rates, tolls and charges.

155 The rate base is arrived at by calculating the utility's net investment in plant and equipment required for the rendering of the regulated service.

156 While not having fixed the return which the utility may earn, the Board has, in its orders, directed that a utility establish an "excess revenue reserve" into which revenue exceeding a certain rate of return on equity is to be deposited.

157 The Board, in its order dated December 4, 1991, having fixed the average rate base for Newfoundland Power for the year 1992, and having determined a just and reasonable return for Newfoundland Power on its average rate base for that year, noted that that return would provide an opportunity for it to earn a somewhat higher rate of return on common equity:

> A just and reasonable return for [Newfoundland Power is determined to be between 10.96% and 11.19% on its average rate base for 1992, which will provide an opportunity to earn a rate of return on common equity between the range of 13.00% to 13.50%.

158 The Board's position before the court was that since what is a just and reasonable return on rate base is influenced by the proportion of the various financing components, including long term and short term debt and preferred shares, it is imperative that the Board be able to set and fix the return which the holders of the common shares in the utility may earn since the market conditions for debt could alter the return to the holders of the common shares significantly.

159 Although s. 80 does not specifically provide for a rate of return for common shares, the determination of a rate of return on the common shares of a utility is very much a part of the rate making process. Further, it must be noted that by s. 3 of the Electrical Power Control Act, the policy of the Province is declared to be that the rates to be charged, either generally or under specific contracts, for the supply of power within the Province "should provide sufficient revenue to the producer or retailer of the power to enable it to earn a just and reasonable return as construed under the *Public Utilities Act* so that it is able to achieve and maintain a sound credit rating in the financial markets of the world...".

160 For Newfoundland Power it was argued that the Board has the jurisdiction to determine the just and reasonable return on the rate base and, as part of that process, the jurisdiction to determine the return on common equity, it being one of its sources of funds. I see no distinction between "determine" and "set and fix" insofar as the jurisdiction of the Board here is concerned. The calculations and projections made by the Board in arriving at the rate of return, whether specifically on rate base or the return on common equity, involve by their very nature, looking into the future, estimating as best can be done the revenues and expenditures contemplated for the utility's operations, the costs of money which may vary substantially, up and down, and then to fix a rate base, and a just and reasonable return on that base upon which the rates, tolls and charges will be based and approved.

161 Although the Board is supplied on a regular basis and has the authority to demand all the financial information it requires of a utility, the rates are, in effect, established for relatively long periods, (in excess of one year) and the likelihood of the accuracy of the forecasts which are necessarily made in setting the rate base and the rates of return is somewhat diminished.

162 For the Consumer Advocate it was argued that s. 80(1) only gives the Board the jurisdiction to calculate the rate of return on rate base and does not allow a calculation of what return the common equity shares will have.

163 As noted earlier, common shares constitute one of the components of the financial make-up of a utility and, as argued by counsel for the Board, while, theoretically, the Board only determines a just and reasonable return on the rate base as fixed and determined by it, in a practical sense, the return on common equity must be considered as part of the mix in setting the return on rate base, just as are the rates of interest paid on preferred shares, bonds and other financial obligations.

164 In the result, in my opinion, questions 1(i) and 1(ii) should be answered in the affirmative.

Question #2

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

Does the Board have jurisdiction to set the rates of return referred to in question (1) as a range of permissible rates of return?

165 There is no question but that the rate setting process of the Public Utilities Board is prospective and is performed by the Board's making estimates of the myriad of factors which have to be considered. The problem is exacerbated by the fact that the process is not one which is contemplated to be reviewed regularly or on a short term basis. The meaningful interpretation of the word "return" as it appears in s. 80(1) allows for and, in the circumstances, contemplates a range of rates of return. It follows then that a just and reasonable return, though it may be stated as a fixed percentage, may be a range of rates which is determined to be just and reasonable. In making such a determination, the Board is clearly acting within its jurisdiction. As noted earlier, a consideration of a just and reasonable return on common equity as one of the components of the financial investment in the company is a necessary part of the process of arriving at a just and reasonable return on rate base, and this return may also be stated as a range.

166 I would answer question 2 in the affirmative.

Question #3

Should a public utility earn annually a rate of return which is in excess of the rate of return determined by the Board to be just and reasonable, either on;

(i) the rate base as fixed and determined by the Board for each type of service supplied by the public utility; or

(ii) the investment, which the Board has determined has been made in the public utility by holders of common shares,

does the Board have jurisdiction to:

(i) require the public utility to use the excess earnings to reduce revenue requirements for the succeeding year; or

(ii) require the public utility to place the excess earnings in a reserve fund for the purpose of adjusting rates, the tolls and charges of the public utility at a future date, or

(iii) require the public utility to rebate the excess earnings to customers of the public utility?

167 Under s. 69 of the Act, the Board has very broad powers including requiring a public utility to set aside from earnings monies in a depreciation account and creating and maintaining a reserve fund. Section 69 of the Act is as follows:

69.(1) A public utility, if so ordered by the board, shall, out of earnings, set aside all money required and carry it in a depreciation account.

(2) The depreciation account shall not, without the consent of the board, be spent otherwise than for replacements, new constructions, extensions or additions to the property of the company.

(3) The board may by order require a public utility to create and maintain a reserve fund for a purpose

> which the board thinks appropriate, including the improvement of the public utility's status as a borrower or seeker of funds for necessary maintenance or expansion of its operations.
>
> (4) The board, in a case where it has made an order which has the effect of increasing a public utility's revenues, may require the public utility to refrain from distributing as dividends until further order the whole or a part of the extra revenue which is in the board's opinion attributable to the order.

168 The answer to the question also requires a consideration of the powers of the Board as set out in ss. 58 and 59 of the Act.

169 By ss. 58 and 59, the Board may prescribe the form of all books of account and records to be kept by the public utility and to make its returns to the Board on such forms as may be prescribed by it. By s. 59, unless otherwise ordered by the Board, the utility shall close its accounts at the end of each calendar year and shall file with the Board its balance sheet, together with such other information as may be required by the Board, before April 2nd of the year following. In effect, approximately three months after the close of the utility's financial year, the Board is made aware of the exact financial position of the company at the end of the previous year and of any other information which it may require.

170 It will be seen from s. 69(3) that the Board has the power to direct a utility to set up reserves out of revenue to be used for replacement of equipment, new construction, extensions or additions to the property of the company. As well, reserves may be ordered to be created which would have the effect of "improving the status of the utility as a borrower or seeker or funds for necessary maintenance or expansion". There is a further power which comes to the Board from s. 69(4) and that is to require the utility to set up a reserve of monies which may have been in excess of those anticipated by the Board at the time of setting the rate of return and to prevent the distribution of that money or any part of it as dividends until the further order of the Board.

171 In the setting of rates, the Board is looking into the future and addressing the anticipated revenues and expenses of the utility with the many variables which may occur. It follows then that it must have the authority to anticipate that there will be variations from what was forecast. While the rates, tolls and charges are set following a hearing and only by an order following a hearing, the constant reporting which a utility must make to the Board allows the Board to be kept informed as to the financial operations of the utility and, in the result, to be aware of how these revenues and expenditures affect the rate of return anticipated by the Board and set out in its order. At the same time, as stated earlier, the rate of return on rate base and on common equity are set not as specific percentages but as a range.

172 In order P.U. 6-1991, the following appears at p. 56:

> The applicant has applied for a rate of return on common equity in the range of 13.5% to 14.0%, with rates set at 13.75%. The midpoint of the range was chosen since it is consistent with past practice and gives the Company the motivation to strive for a higher range (up to 14.0%) while giving them an opportunity to remain within the range if they are unable to come in on forecast (i.e. earn 13.5%)

And later at p. 72:

> The Board orders a range of 13.00% to 13.50% be adopted as the Company's rate of return on common equity with rates being set at the mid-point of the range, 13.25%. In the Opinion of the Board this will give

> [Newfoundland Power] the opportunity to earn a fair and reasonable return and will increase [Newfoundland Power's] interest coverage in 1992 to 2.87 times.
>
> The Board believes that [Newfoundland Power's] interest coverage in 1991 of 2.81 times at existing rates, which is an increase from 2.7 times in 1990, together with the increase to 2.87 in 1992 is satisfactory.

173 In my view, when rates, tolls and charges are set, the revenues generated belong to the company. If the net revenues are less than forecast and result in a return on rate base or on common equity less than as set out in the Board's order, then that loss is the company's loss. Revenues which are greater than anticipated belong to the company and any revenues in excess of those forecast by the Board as reflected in its order belong to the company and cannot be used, except as discussed in the following paragraph, to reduce the revenues of the utility in the future.

174 I see nothing to preclude the Board's directing that those revenues of a utility in excess of the top of the range allowed by the Board in its order as a return on common equity, be set aside and maintained in a reserve fund by an order of the Board, as contemplated by s. 69 "for a purpose which the [B]oard thinks appropriate, including the improvement of the public utility's status as a borrower or seeker of funds for necessary maintenance or expansion of its operations." I do not view any revenues of a utility in excess of those required to achieve the higher point of the range of return either on rate base or on common equity as becoming excess funds unless and until they are set aside by an order of the Board as authorized by s. 69. Until such order, these funds remain the property of the utility and may be treated as such. The creation of a reserve fund is a power given to the Board to be exercised as it sees fit. Indeed, s. 69(4) gives the Board the authority to "require the utility to refrain from distributing as dividends until further order the whole or a part of the extra revenue which is in the [B]oard's opinion, attributable to the order". Indeed, it may happen from time to time that circumstances may so change following the making of an order that a utility may need to and may actually earn revenues in excess of those contemplated by the Board when the last order was issued.

175 It follows from what I have said that the Board does not have the power to order rebates to the customers of the utility other than out of such a reserve fund. To order a rebate from revenues other than those which have been placed in a reserve fund and, in that sense, not available to the company directly, would be to make a retroactive order. A sufficiently good reason for this is that just as additional billings are not permitted to be made to customers because of revenues which have fallen below the range set when the order was made, so any additional revenues may not be paid out. The role of rate making is prospective and this is itself in my view would preclude any reaching back.

176 Reference should also be made to s. 80(1) which in may view contemplates, by the use of the words "earn annually", that each year becomes a separate unit and the revenues from one year may not be applied to another year so as to effect any change in the financial makeup of the utility, except through the use of the reserve fund, which, on its creation by order of the Board, has the effect of removing funds from the particular financial year affected by the order of the Board creating or ordering the placing of funds in the reserve fund and, in effect, makes those monies unavailable for the general use of the utility, including the payment of dividends to the holders of common equity.

177 I would answer question 3(i) in the negative, 3(ii) in the affirmative and 3(iii) in the negative.

Question #4

Does the Board have jurisdiction to order that the rates, tolls and charges of a public utility shall be approved taking into account earnings in excess of a just and reasonable return upon,

(i) the rate base as fixed and determined by the Board for each type of service supplied by the public utility; or

(ii) the investment which the Board has determined has been made in the public utility by the holders of common shares,

in prior years?

178 Although the Board's jurisdiction is to fix and determine a rate base which will enable the utility to earn annually a just and reasonable return on that rate base, it follows that, depending on the range settled upon by the Board in its order and considering that the rates, tolls and charges are set using the mid-point of that range as a basis, the utility may, from time to time, record net revenues which are less than or more than that contemplated by the range as set. Although the wording of s. 80 of the Act states that the utility is entitled to earn a just and reasonable return, it does not follow that it may not nor should not have revenues in excess of those contemplated. At the same time, for reasons which may be beyond the complete control of the utility, the revenues received might be substantially below those anticipated when the rates, tolls and charges were set and approved.

179 In my view, the Board cannot set rates, as argued by counsel for the Board, in a manner that would compensate for prior "excess" earnings. At the same time, in setting rates, as it must do prospectively, the Board must be alive to the various factors which may have caused the utility in any previous year to earn more or less than that anticipated by the Board in its order, and it must factor those causes into the percentages and ranges for return on rate base and for return on common equity in future orders.

180 I would answer question 4 in the negative.

Question #5

Does the fact that the Board has advised the public utility that it is permitted to retain earnings in excess of the rate of return determined by the Board to be adjust and reasonable return, upon the rate base as fixed and determined by the Board for each type of service supplied by the public utility, but not in excess of the return determined by the Board to be a just and reasonable return upon the investment which the Board has determined has been made in the public utility by the holders of common shares, affect the jurisdiction of the Board to approve rates, tolls and charges on the basis queried in Question 4.

181 Counsel for the Board argued that the authority of the Board to amend, alter or rescind any order made by it is plenary and the Board has full power to reconsider any order made previously by it, notwithstanding that there is a right of appeal in respect of its decisions on questions of law. Further, he argued that the fact that the Board has previously ruled or ordered a particular basis for the calculation of excess revenue does not preclude the Board from considering the effect of such earlier decisions in determining what revenues will be required by the utility in setting new rates based on a just and reasonable return in accordance with a new method of calculation.

182 Counsel further argued that since there is no fixed term for the continuing application of any approved

rates, tolls or charges, the Board is not precluded from altering its previous order and assessing what is a just and reasonable return based upon its current assessment of the utility. Counsel argued that s. 87(1) of the Act clearly sets out that power:

> 87.(1) Where upon an investigation the rates, tolls, charges or schedules are found to be unjust, unreasonable, insufficient or unjustly discriminatory, or to be preferential or in violation of this Act, the board has power to cancel those rates, tolls, charges or schedules and declare void all contracts or agreements, either oral or written, dealing with them upon and after a day named by the board, and to determine and by order substitute those rates, tolls or schedules that are reasonable.

183 The investigation undertaken under s. 87(1) follows upon a complaint made to the Board as set out in s. 84(1) and following upon the procedures set out in ss. 85 and 86 of the Act.

184 The legislation empowers and indeed directs the Board to conduct a constant monitoring of the financial position of the utility and gives the Board the authority to institute a correction process at any time. It does not, in my opinion follow, as argued by counsel for the Board, that the Board in setting new rates, tolls and charges may take into account earnings of the utility in previous years in excess of a just and reasonable return upon the rate base or upon the investment which the Board has determined has been made in the public utility by the holders of common shares. This is so notwithstanding that the Board has previously ordered or advised a utility that it is permitted to retain earnings in excess of the rate of return determined by the Board to be a just and reasonable return upon the rate base as fixed and determined by the Board where not in excess of the return determined by the Boards to be a just and reasonable return upon the investment made by the holders of common shares.

185 Counsel for the utility argued that the Board does not have jurisdiction to order that the rates, tolls and charges shall be approved taking into account earnings in excess of a just and reasonable return, either on rate base or on common equity, in prior years. Counsel further argued that such a power would "constitute retroactive appropriation of past revenues for future purposes". He further argued that the only mechanism available to the Board, where a utility earns in excess of the rate of return on rate base or on common equity, is to require the utility to deposit excess revenue, as defined by the Board, into a reserve account in the year earned. It is then, he argued, that the Board may approve the application of these funds as revenue in determining the rates, tolls and charges for a future period but any funds not ordered to be deposited in the reserve account are funds of the utility, belong to the utility, and cannot be considered in setting future rates. To do so, he argued, would be to change the system of accounts so that funds which were not excess in a previous year will then become excess and be brought forward - a retroactive order which is beyond the jurisdiction of the Board.

186 For the Consumer Advocate it was argued that although the Board had advised the utility that it was permitted to retain earnings in excess of the rate of return as determined by the Board, it is not precluded from later making an order under s. 80(1) and s. 76 of the Act rescinding, altering or amending any existing order and in declaring these earnings as excess revenue. The Consumer Advocate also argued that in light of its position taken in response to question 4, the Board does not have jurisdiction to order that the "excess revenue" earned in previous years by the utility should be taken into account in setting rates, tolls and charges in subsequent years but that the Board must order that it be rebated to customers of the utility.

187 I agree with the position taken by the utility. I would answer question 5 in the negative.

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

Question #6

Does the Board have jurisdiction to order the rates, tolls and charges of the public utility shall be approved taking into account the amount of expenses previously incurred by the public utility which the Board may now consider inappropriate to be allowed as reasonable and prudent and properly chargeable to operating account notwithstanding that such classes of expenses were allowed as reasonable and prudent and properly chargeable to operating account.

188 The example given by the Board in its factum illustrative of the situation giving rise to question 6 is as follows:

In determining in 1991 what was a just and reasonable return on the basis of projection for test year, 1992, the Board was presented with projections for the future cost of operating expenses including advertising. The actual cost of advertising for 1995 exceeded the projection for 1992 by some $314,000.00. As such, the amounts for advertising contemplated by the Board as being reasonable, prudent and properly chargeable to operating account vary significantly for the year 1995 from the estimate upon which the Board determined a just and reasonable rate of return.

189 Counsel for the Board argued that "the circumstances of a significant increase in expenses over the estimates used for the test year is indistinguishable from the circumstances of an increase in net earnings. For the same reasons as advanced by it in question 5, it argued that the Board had jurisdiction to order that the rates, tolls and charges could be approved taking into account these expenses, previously incurred, but now considered inappropriate to be allowed as reasonable and prudent.

190 For the utility, it was argued that once rates, tolls and charges are set, the resulting revenue belongs to the utility except for any amounts which the Board may order to be deposited into an excess revenue account. Further, although the Board has the authority to determine whether the expenses comply with s. 80(2), which jurisdiction is necessary to ensure the integrity of the excess revenue account, the Board does not have jurisdiction to disallow the amount of any operating expenses which is reasonable or which had previously been allowed as a just allowance. Further, it argued that the Board may not disallow an expenses because it is of the opinion that had it been the manager, it would not have made that expenditure. The question is whether the expenditure is one that could have been made by a reasonable and prudent manager.

191 The utility further argued that there should be no "microscopic review" especially with the benefit of hindsight. Counsel argued that the Board makes its annual review of the returns made by the utility and, in the specific example here, the Board had obviously made the decision that that expense, although it exceeded predictions, was reasonable (or at least the fact that it didn't say anything about it would indicate that it was reasonable). That expense should not, except in very rare circumstances, be later held to be unreasonable. The utility's position was stated in its factum as follows:

The Board does <u>not</u> have jurisdiction to order that rates, tolls and charges shall be approved taking into account the amount of such "disallowed" expenses. The Board's jurisdiction is limited to disallowing expenses which it determines not to be "reasonable and prudent and properly chargeable to operating account" or otherwise not a "just allowance" under s. 80(2). The disallowance of an expense would lead to the company earning a somewhat greater return on common equity for the purpose of the excess revenue

account for the year in which the expense was incurred. However, this revenue remains the property of the company and its shareholders unless the amount disallowed would mean that the company's return on common equity would exceed the maximum return on common equity previously allowed by the Board. If that were to occur, the amount which would be beyond the maximum return on common equity would be deposited into the "excess revenue account".

192 For the Consumer Advocate, it was argued that the Board may take into account past expenses in order to forecast more accurately future revenues and expenditures. However, its counsel argued that the Board does not have jurisdiction to set future rates, tolls and charges designed to compensate for past expenses that the Board may now consider inappropriate to be allowed as reasonable and prudent and properly chargeable to operating account.

193 I agree with the arguments proferred by the utility and the Consumer Advocate.

194 I would answer question 6 in the negative.

Questions #7 & 8

Question #7

Does the Board have jurisdiction to require a public utility to maintain:

(i) A ratio; or

(ii) A ratio within a stated range of ratios

of equity and debt, as the means of obtaining the capital requirements of the public utility.

Question #8

Does the Board, upon an application pursuant to Section 91 or otherwise, have the jurisdiction to require a public utility to obtain its capital requirements by the issue of specific financial instruments, whether common shares, preferred shares, stocks, bonds, debentures or evidence of indebtedness payable in more than one year.

195 In his decision which I have read in draft, Green, J.A. considered questions 7 and 8 together because, as he stated, the issues they raise are interrelated. I agree with the reasoning of Green, J.A. in dealing with these questions and I would answer both questions, as he did, in the negative.

196 I would also agree with the comments made by Green, J.A. in that part of his decision, entitled "General Observations".

Conclusion

197 In the result then I would answer the questions posed as follows: 1(i) yes, 1(ii) yes, question 2 - yes, question 3(i) - no, question 3(ii) - yes, question 3(iii) - no, question 4 - no, question 5 - no, question 6 - no, question 7 - no, and question 8 - no.

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

Order accordingly.

FN1 R.S.N. 1990, c. P-47 as amended (hereinafter the "Act")

FN2 *Act*, s. 16

FN3 *Act*, s. 70

FN4 *Act*, s. 80

FN5 Board Orders P.U.6 (1991) and P.U.7 (1991)

FN6 Hereinafter, "NLP"

FN7 Pursuant to s. 117 of the Act. See OC 96-226; OC 96-236

FN8 S.N. 1994, c. E-5.1, as amended (hereinafter, the "EPC Act")

FN9 I acknowledge a large indebtedness to the following sources for much of the information referred to herein about general regulatory principles and practice in North America: Charles F. Phillips, Jr. *The Regulation of Public Utilities* (Arlington: Public Utilities Reports Inc., 1993); A.J. deGrandpré, "Fair Returns for Utilities-Concept or Reality?" (1970), 16 McGill L.J. 19; A.B. Jackson, "The Determination of the Fair Return for Public Utilities" (1964), 7 Canadian Public Administration 343.

FN10 s. 4

FN11 See *Bell Canada v. Canada (Canadian Radio-Television & Telecommunications Commission)*, [1989] 1 S.C.R. 1722 (S.C.C.) (hereinafter referred to as the "Bell Rebate case") where Gonthier, J. in response to an argument that a regulatory board did not have a particular power because it was not expressly provided for in the legislation stated at p. 1758: "This approach to the interpretation of statutes conferring regulatory authority over rates and tariffs is only the expansion of the wider rule that the Court must not stifle the legislator's intention by reason only that a power has not been explicitly provided for."

FN12 "Nearly all the boards and commissions in the United States and Canada that regulate public utility rates do so on the basis of allowing a public utility a 'return' on the 'value' of the public utility property. The return that must be allowed is usually referred to as the 'fair return' ..." per Jackson, op.cit. fn.9, p. 343. See also *Union Gas Ltd. v. Ontario (Energy Board)* (1983), 1 D.L.R. (4th) 698 (Ont. Div. Ct.) per Anderson, J. at page 710: "By way of general observation ... there are substantial similarities between the situation here and in the United States, and authorities of courts in the United States are frequently referred to and considered..."

FN13 *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (U.S. 1944), per Douglas J. at page 603: "The rate-making process under the Act, i.e., the fixing of "just and reasonable" rates, involves a balancing of the investor and the consumer interests"; *Edmonton (City) v. Northwestern Utilities Ltd.*, [1929] S.C.R. 186 (S.C.C.), per Lamont, J. at pages 192-193: "The duty of the Board was to fix fair and reasonable rates; rates which, under the circumstances, would be fair to the consumer on the one hand, and which, on the other hand, would secure to the company a fair return for the capital invested".

FN14 deGrandpré, op.cit. fn. 9, p. 20. See also *Union Gas Ltd. v. Ontario (Energy Board)* (1983), 1 D.L.R. (4th)

698 (Ont. Div. Ct.) per Anderson, J. at page 710: "...it is the function of the [Board] to balance the interest of the [utility] in earning the highest possible return on the operation of its enterprise (a monopoly) with the conflicting interests of its customers to be served as cheaply as possible". See also *Bell Canada v. Canada (Canadian Radio-Television & Telecommunications Commission)*, [1989] 1 S.C.R. 1722 (S.C.C.) per Gonthier, J. at p. 1748.

FN15 *EPC Act*, s. 3(a)(iii)

FN16 *EPC Act*, s. 3(a)(i)

FN17 *EPC Act*, s. 3(b)(iii)

FN18 *Act*, s. 37(1)

FN19 *Act*, s. 70(1). Although, unlike the legislation of some other jurisdictions, s. 70 does not expressly state that the rates approved by the Board must be "reasonable" or "just and reasonable", that standard is nevertheless imported into the approval process by virtue of the *EPC Act*, s. 3(a)(i) which declares the policy of the province to be that rates must be "reasonable".

FN20 *Act*, s. 80(1)

FN21 *British Columbia Electric Railway v. British Columbia (Public Utilities Commission)*, [1960] S.C.R. 837 (S.C.C.), per Locke, J. at page 848: "The obligation to approve rates which will produce the fair return to which the utility has been found entitled is, in my opinion, absolute..."

FN22 Ibid., per Locke, J. at pages 845, 847.

FN23 Ibid., per Locke, J. at page 848: "I do not think it is possible to define what constitutes a fair return upon the property of utilities in a manner applicable to all cases ...". This observation was adopted and followed by this Court in *Newfoundland Light & Power Co. v. Newfoundland (Public Utilities Commissioners Board)* (1987), 25 Admin. L.R. 180 (Nfld. C.A.) at page 193.

FN24 *Bluefield Waterworks & Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679 (U.S. W. Va. 1923). (This case has often been referred and relied upon in subsequent decisions in the United States and Canada, including in this Court. See *Newfoundland Light & Power Co. v. Newfoundland (Public Utilities Commissioners Board)* supra, fn. 23 at page 193.)

FN25 Ibid., page 692.

FN26 *Edmonton (City) v. Northwestern Utilities Ltd.*, [1929] S.C.R. 186 (S.C.C.), per Lamont, J. at page 193.

FN27 320 U.S. 591 (U.S. 1944)

FN28 deGrandpré op.cit. fn. 9, page 28

FN29 Ibid., page 37

FN30 supra, fn. 23 at page 194

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

FN31 Ibid. page 194

FN32 *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246 (U.S. S.D. 1951), per Jackson, J. at page 251

FN33 *Bell Telephone Co. of Canada, Re* (1966), 56 B.T.C. 535 at page 731: "We are ... not persuaded that reasonableness can, in practical terms, be expressed as a fixed point from which there can be no deviation. We therefore propose to use a range of percentage earnings on total average capitalization."

FN34 *Federal Power Commission v. Hope Natural Gas Co.* Supra fn. 13 per Douglas, J. at page 603

FN35 In *Northwestern Utilities, Re* (1978), 89 D.L.R. (3d) 161 (S.C.C.), Estey, J. stated at p. 164: "The statutory pattern is founded on the concept of the establishment of rates *in futuro*... [T]he Board must act prospectively and may not award rates which will recover expenses incurred in the past and not recovered under the rates established for past periods." [Of course, such an approach assumes that without such rates, the utility will continue to be economically viable. If poor management leads to losses that threaten the very continued existence of the utility, the Board may well have to set future rates at a level that will enable the utility to remain operative so as to ensure continued service to customers. This is an unlikely scenario in view of the close monitoring that the Board should exercise between rate hearings.]

FN36 *EPC Act*, s. 3(1)(b)(iii)

FN37 deGrandpré op.cit. fn. 9, page 26

FN38 "The fixing of tolls and tariffs that are just and reasonable necessarily involves the regulation of the revenues of the regulated entity": per Gonthier, J. in *Bell Canada v. Canada (Canadian Radio-Television & Telecommunications Commission)* supra, fn. 11 at page 1747

FN39 4th ed. rev., 1968

FN40 J.B. Sykes (ed), 7th ed.

FN41 s. 64(1)

FN42 s. 64(2)

FN43 s. 68(4)

FN44 s. 70(1). This provision makes the scheme administered by the Board a "positive approval scheme" (requiring advance approval of rates as being reasonable) rather than a "negative disallowance scheme" (permitting the utility to set its own rates subject to user objection, which would only then trigger a review into reasonableness), as those terms were explained by Gonthier, J. in the *Bell Rebate* case, supra, fn. 11 at p. 1758.

FN45 s. 78(1)

FN46 s. 78(2)

FN47 s. 91(1), (3)

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

FN48 supra, paragraphs [21]-[23]

FN49 *EPC Act*, s. 3(b)(iii)

FN50 See, e.g., Board Order P.U.6 (1991), page 72

FN51 Phillips, op.cit., fn. 9, p. 389

FN52 See, e.g. P.U. 6 (1991) and P.U. 7 (1996-97)

FN53 Supra fn. 13 at p.199

FN54 supra fn. 23

FN55 *Union Gas Ltd. v. Ontario (Energy Board)*, supra fn. 12

FN56 para.[30]

FN57 See *Bell Canada v. Canada (Canadian Radio-Television & Telecommunications Commission)*, supra, fn. 11 at page 1733. Yvonne Penning, "The 1986 Bell Rate Case: Can Economic Policy and Legal Formalism be Reconciled" (1989), 47 U of T Fac. L.R. 607 observes at p. 617: "The CRTC has developed the practice of setting the allowed ROE on the basis of a one percentile range. While only one actual ROE - usually the middle of the range - is used in the calculation of rates to be charged customers, all rates encompassed by the range, in theory, represent a reasonable return. One reason for setting such a range is that it explicitly provides some incentive for the company to be efficient; financial rewards due to efficiency or productivity gains would accrue to the company's shareholders, rather than being passed on to consumers through lower prices." Another rationale for a range approach is given by Penning later in her article at p. 621 where, after noting that the U.S. Federal Communications Commission also employs ranges, states: "...it also serves a very useful administrative function in that it limits the circumstances under which it would be necessary to alter rates on a prospective basis, within the time period for which the range of rates of return was deemed to be reasonable, in response to changing economic circumstances."

FN58 s. 58

FN59 s. 69(3)

FN60 Phillips, op cit. fn. 9, page 196

FN61 See, eg. Board Order P.U.6(1991), page 81

FN62 S. 80(4)

FN63 S. 3(a)(ii)

FN64 *Northwestern Utilities, Re*, supra fn. 35, per Estey, J. at p. 170: "...the Act does not prevent the Board from taking into account past experiences in order to forecast more accurately future revenues and expenses of a utility".

FN65 supra, fn. 11 at p. 1734.

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

FN66 See supra, para. [33]

FN67 *Wabush (Town) v. Power Distribution District of Newfoundland & Labrador* (1988), 71 Nfld. & P.E.I.R. 29 (Nfld. C.A.), per Goodridge, C.J.N. at p. 33.

FN68 op cit. fn. 57, pp. 608-610

FN69 Ibid, p. 610

FN70 *E.P.C. Act*, s. 3(b)(iii)

FN71 s. 3(b)(i)

FN72 s. 3(b)(iii)

FN73 s. 3(b)(iii)

FN74 Paras. [21]-[23]

FN75 Supra fn 11, at p. 1734

FN76 Op.cit. fn. 57 at page 619

FN77 supra, fn. 11 at page 1762 - 3

FN78 para.[73]

FN79 paras.[31], [50]

FN80 *Act*,s.80(2)

FN81 Phillips, op.cit. fn. 9, pages 256-257

FN82 Ibid. page 256

FN83 supra, para. 32

FN84 *Union Gas Ltd. v. Ontario (Energy Board)* supra fn. 12 per Anderson, J. at page 712.

FN85 *Acker v. United States*, 298 U.S. 426 (U.S. Ill. 1936), per Roberts, J. at pages 430-431

FN86 Phillips, op. cit. fn. 9, at page 258

FN87 deGrandpré op cit. fn. 9, page 26; Phillips op. cit. fn. 9, page 233

FN88 Phillips, op. cit. fn. 9, pages 388-389

FN89 op. cit. fn. 9, page 26. See also to the same effect Phillips, op. cit. fn. 9, page 233

FN90 Phillips, op. cit. fn. 9, p. 234

1998 CarswellNfld 150, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 164 Nfld. & P.E.I.R. 60, (sub nom. Reference re s. 101 of the Public Utilities Act (Nfld.)) 507 A.P.R. 60, 164 Nfld. & P.E.I.R. 60

FN91 paragraphs [31] - [32]

FN92 Phillips, op. cit. fn. 9, p. 236

FN93 Ibid.

FN94 Phillips, op. cit. fn. 9, pages 388-392

FN95 Ibid., page 389

FN96 Ibid., page 391

FN97 *Bell Telephone Co. of Canada, Re*, supra. fn. 33 at page 723: "...the Board has, when the circumstances so warrant it, seen fit to adjust the company's debt-ratio *for rate making purposes.*"

FN98 No doubt as a practical matter, the Board would also be hesitant to make assumptions respecting a utility's capital structure for rate-making purposes, that are different from the actual structure which will have been created as a result of previous approvals given by the Board (though perhaps in not as focused a context as a rate hearing and without the benefit of argument from rate hearing participants, such as the Consumer Advocate) to the issuing of individual share or other financial instruments in the past pursuant to s. 91.

FN99 paragraph [128]

END OF DOCUMENT

TORT LAW

Fifth Edition

Lewis N. Klar, Q.C.
B.A., B.C.L., LL.M.
Professor of Law
University of Alberta

CARSWELL®

is to say, because of factors peculiar to the activity, the balance ought to be tilted in the defendant's favour, making it more difficult for a victim to show that the defendant's conduct ought to result in legal liability. This has been done by imposing liability only when conduct can be characterized as grossly negligent. Thus, for example, the Alberta Emergency Medical Aid Act[163] directs that doctors and others who render emergency first aid assistance under certain circumstances are not to be held liable for damages for injuries to, or the death of, a person unless it can be established that these injuries or the death were caused by the gross negligence of those rendering the assistance. As well, until recently the highway traffic legislation of several provinces directed that those who gratuitously gave other people rides in their cars were not to be held liable to them for injuries caused in a traffic accident unless the accident was caused by the gross negligence or wilful and wanton misconduct of the host drivers.[164] Other examples can be found in Municipal Government Acts[165] which relieve municipalities of liability for injuries caused to persons or property as a result of slippery sidewalks, unless the gross negligence of these defendants can be proved.[166]

Legislation requiring that gross negligence be proved in order for a defendant to be held liable for injuries caused has been criticized. It is clear that the phrase 'gross negligence' itself is not susceptible of a clear definition to assist courts in deciding whether it has been shown.[167] It has frequently been defined in terms which merely replace the words "gross negligence" with other equally ambiguous words, without actually clarifying the concept.[168] It has, for example, been de-

---

163 R.S.A. 2000, c. E-7, s. 1.

164 The legislation varied slightly. Most stated that there was no liability unless there was "gross negligence or wilful and wanton misconduct." The guest passenger discrimination provisions have now been repealed.

165 For example, Alberta's Municipal Government Act, S.A. 2000, c. M-26, s. 531. There are numerous other legislative provisions establishing "gross negligence" as the standard of care, for example, in relation to the activities of police, civil servants, and so on. See, for example, the Police Act, R.S.B.C. 1996, c. 367, s. 21 applied in *Doern v. Phillips Estate* (1994), 23 C.C.L.T. (2d) 283, affirmed (1997), 43 B.C.L.R. (3d) 53 (C.A.), *Noel (Committee of) v. Royal Canadian Mounted Police* (1995), [1995] B.C.J. No. 1184, 1995 CarswellBC 342 (S.C.), and *Insurance Corp. of British Columbia v. Vancouver (City)* (1997), 38 C.C.L.T. (2d) 271 (B.C. S.C.), affirmed (2000), 182 D.L.R. (4th) 366 (B.C. C.A.).

166 See, e.g., *Ancvirs v. London (City)* (1987), 48 D.L.R. (4th) 252 (Ont. H.C.). In *Bannon v. Thunder Bay (City)* (2000), 48 O.R. (3d) 1 (C.A.), leave to appeal allowed (2001), 149 O.A.C. 198 (note) (S.C.C.), reversed (2002), 210 D.L.R. (4th) 62 (S.C.C.), the Court of Appeal upheld the finding of the trial judge that the City's failure to plough or sand the sidewalk for one month constituted "gross negligence" as required by the statute. The trial judge allowed the claim, but the Court of Appeal reversed based on the plaintiff's failure to give the required notice. The Supreme Court of Canada restored the trial judgment. More recent cases involving falls on icy sidewalks are *Crinson v. Toronto (City)*, 2010 CarswellOnt 299, 316 D.L.R. (4th) 145 (C.A.) — liability found; *Billings v. Mississauga (City)*, 2011 CarswellOnt 2166, 81 M.P.L.R. (4th) 175 (C.A.) — no liability; *Ryan v. Sault Ste. Marie (City)*, 2009 CarswellOnt 2208, 55 M.P.L.R. (4th) 206 (C.A.) — municipality liable.

167 This was recognized by Anglin C.J.C. in *Holland v. Toronto* (1926), 59 O.L.R. 628 at 634 (S.C.C.), where the Chief Justice stated: "The term 'gross negligence' . . . is not susceptible of definition." See MacArthur, "Gross Negligence and the Guest Passenger" (1960), 38 Can. Bar Rev. 47 at 50.

168 Locke J. in *Cowper v. Studer*, [1951] S.C.R. 450, regretted that the term was used instead of a "more definite term."

scribed as "very great negligence",[169] as being the same thing as negligence with the addition of a "vituperative epithet",[170] or as "conduct in which, if there is not conscious wrong doing, there is a very marked departure from the standards by which responsible and competent people . . . habitually govern themselves."[171] One writer has described the doctrine of different degrees of care as "an untested invention of fancy" which does not spring from the common law.[172] Others have argued that it is meaningless to suggest that there can even be degrees of negligence, for "a man is either guilty of negligence or he is not."[173] The Chief Justice of Manitoba conceded that "the term is not susceptible of definition and, consequently, judges have found gross negligence where none existed and where at most plain, ordinary negligence existed but nothing else."[174] It has been agreed, however, that despite these objections, whether there has been gross negligence or not is a question of fact depending entirely upon the circumstances of the case.[175] It also has been argued that as with the concept of ordinary negligence

---

169 For example, Wilson J. in *Dahl v. Saydack* (1970), 73 W.W.R. 133 (Man. Q.B.).

170 Dean Wright, in his S.J.D. Thesis on Gross Negligence, written in 1927 and published in (1983), 33 U.T.L.J. 184, notes that Baron Rolfe used this expression to describe gross negligence in *Wilson v. Brett* (1843), 152 E.R. 737.

171 Duff C.J.C. in *McCulloch v. Murray*, [1942] S.C.R. 141 at 145. This phrase has been very popular in many of the cases. See, e.g., *Dahl v. Saydack* (1970), 73 W.W.R. 133 (Man. Q.B.), and cases discussed in the literature, especially Singleton, "Gross Negligence and the Guest Passenger" (1973), 11 Alta. L. Rev. 165. There are dozens of cases which have applied the term under the various legislative enactments which have used it. In *Marino v. Marino* (1981), 13 Man. R. (2d) 169 (Q.B.), it was noted that the Supreme Court of Canada has been called upon to decide the gross negligence issue in *McCulloch v. Murray*, [1942] S.C.R. 141; *Studer v. Cowper*, [1951] S.C.R. 450; *Burke v. Perry*, [1963] S.C.R. 329; and *Walker v. Coates*, [1968] S.C.R. 599.

172 Green, "High Care and Gross Negligence" (1928), 23 Ill. L. Rev. 4, cited by Pierce in a paper delivered to the 1965 meeting of the Canadian Bar Association. For a thorough historical account see Wright, "Gross Negligence". 1927 S.J.D. Thesis, published in (1983), 33 U. T.L.J. 184. Note that the common law did apply a rule of gross negligence in certain situations. See, e.g., *Nightingale v. Union Colliery of B.C.* (1905), 35 S.C.R. 65; cf. *Armand v. Carr*, [1926] S.C.R. 575. The phrase gross negligence is said to have first been introduced in the bailment case of *Coggs v. Bernard* (1703), 92 E.R. 107 (K.B.).

173 Lynskey J. in *Pentecost v. London Dist. Auditor*, [1951] 2 K.B. 759, cited by MacArthur, above, note 167. MacArthur also cites others who share this view that there are no degrees of negligence, although the author himself did not agree that the term is meaningless.

174 Monnin C.J.M. in *Occhino v. Winnipeg (City)* (1988), 51 D.L.R. (4th) 546 at 548 (Man. C.A.). A similar sentiment was expressed by Chief Justice Hickman in *Andrews v. Leger* (1981), 30 Nfld. & P.E.I.R. 258 at 263 (Nfld. T.D.), quoted by Green J. in *Mayo v. Harding* (1993), 111 Nfld. & P.E.I.R. 271 (Nfld. T.D.):

> The courts, over many years, have wrestled with the problem of defining that invisible juridical line which separates ordinary negligence from gross negligence. It is not a fixed line or one that is forever straight but one which has been bent and positioned as the exigencies and justice of the cause persuaded the trial judge or jury was necessary to ensure that justice be done.

175 See, e.g., *Gordon v. Nutbean*, [1969] 2 O.R. 420 (H.C.); *McCulloch v. Murray*, above, note 171; *Studer v. Cowper*, above, note 171; *Remmers v. Lipinski* (2000), 262 A.R. 295 (Q.B.), affirmed (2001), 203 D.L.R. (4th) 367 (Alta. C.A.), leave to appeal refused (2002), 2002 CarswellAlta 784, 2002 CarswellAlta 785 (S.C.C.); *Crinson v. Toronto (City)*, above, note 166. Nevertheless, certain conduct, such as falling asleep at the wheel, has been held to amount to gross negligence, almost as a matter of law. See Dickson J. in *Power v. Roussel* (1978), 23

itself, there is no rigid definition of gross negligence, the standard varying according to the type of activity in issue.[176] It has been generally held that the requirements for gross negligence are less than for criminal negligence,[177] and that gross negligence can be proved by cumulating the effect of several acts, each of which taken alone might only be considered as being ordinary negligence.[178]

Despite the difficulty involved in defining the term gross negligence, that the intention of its use has been to lighten the legal liability of defendants engaged in certain activities. The legislators have decided that for a variety of reasons, it ought to be more difficult for victims of accidents caused by some defendants to succeed in a negligence claim. It is this aspect of the legislators' use of the phrase gross negligence, especially in relation to the now repealed guest passenger discrimination, which has been the subject of most of the criticism.[179] The argument that some victims of accidents caused by the negligence of others should be denied compensation except in cases of extreme misconduct by defendants, has not been popular to a compensation-oriented tort law. It has become evident that a sufficiently flexible negligence law is able to accommodate legitimate policy considerations in determining the liability of defendants, and thus has little need for the notion of gross negligence.

8. GOOD FAITH AND REASONABLE CARE

An issue which has been raised in the case law, particularly where the nature of the defendant's task involves an element of discretion, is whether the standard of "reasonable care" should be replaced by a lower standard of "good faith", and if so, what this latter standard implies. As discussed above in relation to public authority liability,[180] proof of "bad faith" is in fact *required* where a public authority's alleged negligence related to a "policy" as opposed to an "operational" activity. Moreover, many statutory provisions specifically provide that the defendants cannot be held personally liable for acts done in "good faith" in the exercise of their statutory powers, duties or functions.[181]

The treatment by the courts of these "good faith" statutory provisions has been somewhat uneven. For example, in the two leading Supreme Court of Canada "duty of care" cases, i.e., *Cooper v. Hobart* and *Edwards v. L.S.U.C.*, there were statutory good faith provisions. Nevertheless, the Supreme Court viewed these

---

N.B.R. (2d) 298 (Q.B.). This view was contradicted in *Steeves v. Lutes* (1982), 43 N.B.R. (2d) 338 (Q.B.), affirmed (1983), 51 N.B.R. (2d) 105 (C.A.).

176 See *Doern v. Phillips*, above. note 165.

177 See, e.g., *Marino v. Marino* (1981), 13 Man. R. (2d) 169 (Q.B.).

178 See, e.g., *Ogwa v. Alli* (1972), 4 N.B.R. (2d) 423 (C.A.); *Jones v. Green*, [1995] 4 W.W.R. 118 (Alta. C.A.). It has also been held that *res ipsa loquitur* can be used to assist in establishing gross negligence. See *Genik v. Ewanylo* (1980), 12 C.C.L.T. 121 (Man. C.A.).

179 See, e.g., Gibson, "Guest Passenger Discrimination" (1968), 6 Alta. L. Rev. 211. The Alberta legislation was subject to an unsuccessful Charter challenge: see *Mohr v. Scoffield* (1991), 83 Alta. L.R. (2d) 1 (C.A.), reversing (1990), 77 Alta. L.R. (2d) 68 (Q.B.), leave to appeal to S.C.C. refused (1992), 12 A.R. 398 (note) (S.C.C.).

180 See Chapter 8.

181 See, for example, the Child, Family and Community Service Act, R.S.B.C. 1996, c. 46, s. 101. "Good faith" statutory provisions in fact were included both in the Mortgage Brokers Act, R.S.B.C. 1996, c. 313 (*Cooper v. Hobart*) and Law Society Act, R.S.O. 1990, c. L.8 (*Edwards v. L.S.U.C.*).

Updated to 1 December 2013
This document has official status.

Québec

CIVIL CODE OF QUÉBEC

PRELIMINARY PROVISION

The Civil Code of Québec, in harmony with the Charter of human rights and freedoms (chapter C-12) and the general principles of law, governs persons, relations between persons, and property.

The Civil Code comprises a body of rules which, in all matters within the letter, spirit or object of its provisions, lays down the *jus commune*, expressly or by implication. In these matters, the Code is the foundation of all other laws, although other laws may complement the Code or make exceptions to it.

1607. The creditor is entitled to damages for bodily, moral or material injury which is an immediate and direct consequence of the debtor's default.

1613. In contractual matters, the debtor is liable only for damages that were foreseen or foreseeable at the time the obligation was contracted, where the failure to perform the obligation does not proceed from intentional or gross fault on his part; even then, the damages include only what is an immediate and direct consequence of the nonperformance.

Kazimierz Janiak *Appellant*;

and

Samuel Ippolito *Respondent.*

File No.: 16792.

1983: December 12; 1985: March 14.

Present: Ritchie*, Dickson, Estey, Chouinard and Wilson JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Torts — Damages — Refusal to undergo recommended surgery — Procedure having 70 per cent success rate and 100 per cent chance of recovery if successful — Whether or not uncertainty a factor to include in calculating award.

Respondent was disabled as a result of a traffic accident and could not return to work. The recommended surgical treatment entailed a 70 per cent chance of success, and if successful, a 100 per cent chance of recovery and the possibility of respondent's returning to work. Respondent, however, feared surgery of any kind and refused to undergo the operation without his doctors' assuring him of a 100 per cent chance of success; he remains disabled and out of work. The action was limited, given appellant's admission of liability, to the issue of damages. The trial judge found respondent was not entitled to damages in respect of pain or suffering or loss of earnings consequent upon an unreasonable refusal to undergo the proper medical treatment. The Court of Appeal adopted a similar line of reasoning but adjusted the award for loss of income upwards to take into account the fact that recovery was not completely guaranteed.

Held: The appeal and cross-appeal should be dismissed.

The question of whether or not a person has been reasonable in refusing to accept the recommended medical treatment is for the trier of fact to decide. In making that finding, the trier of fact must take into consideration the degree of risk from the surgery, the gravity of the consequences of refusing it, and the potential benefits to be derived from it. If any one of several recommended courses of treatment is followed, a plaintiff cannot be said to have acted unreasonably. The trial

* Ritchie J. took no part in the judgment.

Kazimierz Janiak *Appelant*;

et

Samuel Ippolito *Intimé.*

N° du greffe: 16792.

1983: 12 décembre; 1985: 14 mars.

Présents: Les juges Ritchie*, Dickson, Estey, Chouinard et Wilson.

EN APPEL DE LA COUR D'APPEL DE L'ONTARIO

Responsabilité délictuelle — Dommages-intérêts — Refus de subir une intervention chirurgicale recommandée — Opération qui comporte 70 pour 100 de probabilités de réussite et qui entraîne une guérison totale si elle réussit — L'incertitude est-elle un facteur à considérer dans le calcul de l'indemnité?

L'intimé a été rendu invalide par suite d'un accident de la circulation et n'a pu reprendre son travail. Le traitement chirurgical recommendé comportait 70 pour cent de probabilités de réussite et, en cas de réussite, cent pour cent de probabilités de guérison et de retour au travail pour l'intimé. Cependant, l'intimé craignait toute espèce d'intervention chirurgicale et a refusé de subir l'opération à moins que ses médecins ne lui assurent à cent pour cent les chances de réussite; il est demeuré invalide et sans travail. L'action a été restreinte à la question du montant des dommages-intérêts étant donné que l'appelant a reconnu sa responsabilité. Le juge de première instance a conclu que l'intimé n'avait pas le droit d'être indemnisé pour la douleur, les souffrances et la perte de revenu subies par suite d'un refus déraisonnable de subir le traitement médical indiqué. La Cour d'appel a adopté à peu près la même façon de raisonner, mais elle a augmenté l'indemnité pour perte de revenu de manière à tenir compte du fait que la guérison n'était pas totalement assurée.

Arrêt: Le pourvoi et le pourvoi incident sont rejetés.

Il appartient au juge des faits de décider si une personne a été raisonnable ou non en refusant de subir le traitement médical recommandé. Pour arriver à cette décision, le juge des faits doit tenir compte du risque que présente l'intervention chirurgicale, de la gravité des conséquences du refus de la subir et des avantages qu'il était possible d'en tirer. Si un demandeur a suivi l'une ou l'autre des différentes formes de traitement recommandées, on ne peut dire qu'il a agi déraisonnablement.

* Le juge Ritchie n'a pas pris part au jugement.

judge committed no error of law here and there was no basis on which an appellate court could interfere with his finding.

Damages for aggravated injuries consequent on some pre-existing infirmity are recoverable even if the infirmity is of a psychological nature. A psychological "thin skull" that developed subsequent to the tortious act is not, however, a factor to be considered in relation to reasonableness. The analytical focus in each case is on the capacity to make a reasonable choice. A line must be drawn between those capable of making a rational choice and those who cannot due to some pre-existing psychological condition. A person capable of choice must bear the cost of an unreasonable decision but a person incapable of making such a choice due to a pre-existing psychological condition should not bear the cost when wrongfully injured. The burden of proof of damages lies with the plaintiff but shifts once it is alleged that the loss should have been mitigated.

The principle that a plaintiff cannot recover damages which could have been avoided by the taking of reasonable steps underlies the duty to mitigate. Avoidable damages are to be determined by assuming that the plaintiff has agreed to an operation not yet performed rather than looking at what on the balance of probabilities would have happened had the operation taken place. The courts must therefore take into account any "substantial possibility" of failure and the amount by which full compensation would be discounted would represent the avoidable loss.

Cases Cited

Marcroft v. Scruttons, Ltd., [1954] 1 Lloyd's Rep. 395; *Elloway v. Boomars* (1968), 69 D.L.R. (2d) 605; *Morgan v. T. Wallis Ltd.*, [1974] 1 Lloyd's Rep. 165; *Buczynski v. McDonald* (1971), 1 S.A.S.R. 569; *Plenty v. Argus*, [1975] W.A.R. 155; *Selvanayagam v. University of West Indies*, [1983] 1 All E.R. 824, considered; *Steele v. Robert George and Co.*, [1942] A.C. 497; *Hay or Bourhill v. Young*, [1943] A.C. 92; *Bishop v. Arts & Letters Club of Toronto* (1978), 83 D.L.R. (3d) 107; *Love v. Port of London Authority*, [1959] 2 Lloyd's Rep. 541; *Gray v. Cotic*, [1983] 2 S.C.R. 2; *Malcolm v. Broadhurst*, [1970] 3 All E.R. 508; *Dulieu v. White & Sons*, [1901] 2 K.B. 669; *Blackstock v. Foster*, [1938] S.R. (N.S.W.) 341; *Smith v. Leech Brain & Co.*, [1962] 2 Q.B. 405; *McGrath v. Excelsior Life Insurance Co.* (1974), 6 Nfld. & P.E.I.R. 203; *Asamera Oil Corp. v. Sea Oil & General Corp.*, [1979] 1 S.C.R. 633; *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London,*

Le juge de première instance n'a commis aucune erreur de droit en l'espèce et il n'y a rien qui justifie qu'une cour d'appel modifie sa conclusion.

Des dommages-intérêts relatifs à des blessures aggravées résultant d'une infirmité préexistante peuvent être obtenus même si l'infirmité est de nature psychologique. La vulnérabilité psychologique consécutive à l'acte fautif n'est toutefois pas un facteur à prendre en considération pour déterminer le caractère raisonnable de la décision. L'examen dans chaque cas porte sur la capacité de faire un choix raisonnable. Il faut distinguer entre les personnes capables de faire un choix rationnel et celles qui ne peuvent le faire à cause d'un état psychologique préexistant. Une personne capable de choisir doit assumer le coût d'une décision déraisonnable, mais une personne incapable de faire un tel choix en raison d'un état psychologique préexistant ne doit pas en assumer le coût si elle a été blessée par suite d'un acte fautif. Le demandeur a l'obligation de prouver l'étendue du préjudice, mais le fardeau se déplace si l'on allègue que les pertes auraient pu être minimisées.

L'obligation de minimiser les dommages découle du principe selon lequel le demandeur ne peut être indemnisé pour les dommages qui auraient pu être évités par des mesures raisonnables. Les pertes évitables doivent être déterminées en supposant que le demandeur a consenti à une opération qui n'a pas encore eu lieu plutôt qu'en considérant ce qui, selon la prépondérance des probabilités, se serait produit si l'opération avait eu lieu. Les cours doivent donc tenir compte de toute «possibilité réelle» d'échec et la somme dont le plein dédommagement serait diminué représenterait la perte évitable.

Jurisprudence

Arrêts examinés: *Marcroft v. Scruttons, Ltd.*, [1954] 1 Lloyd's Rep. 395; *Elloway v. Boomars* (1968), 69 D.L.R. (2d) 605; *Morgan v. T. Wallis Ltd.*, [1974] 1 Lloyd's Rep. 165; *Buczynski v. McDonald* (1971), 1 S.A.S.R. 569; *Plenty v. Argus*, [1975] W.A.R. 155; *Selvanayagam v. University of West Indies*, [1983] 1 All E.R. 824; arrêts mentionnés: *Steele v. Robert George and Co.*, [1942] A.C. 497; *Hay or Bourhill v. Young*, [1943] A.C. 92; *Bishop v. Arts & Letters Club of Toronto* (1978), 83 D.L.R. (3d) 107; *Love v. Port of London Authority*, [1959] 2 Lloyd's Rep. 541; *Gray c. Cotic*, [1983] 2 R.C.S. 2; *Malcolm v. Broadhurst*, [1970] 3 All E.R. 508; *Dulieu v. White & Sons*, [1901] 2 K.B. 669; *Blackstock v. Foster*, [1938] S.R. (N.S.W.) 341; *Smith v. Leech Brain & Co.*, [1962] 2 Q.B. 405; *McGrath v. Excelsior Life Insurance Co.* (1974), 6 Nfld. & P.E.I.R. 203; *Asamera Oil Corp. c. Sea Oil & General Corp.*, [1979] 1 R.C.S. 633; *British Westinghouse Electric and Manufacturing Co. v. Underground*

[1912] A.C. 673; *Banco de Portugal v. Waterlow and Sons, Ltd.*, [1932] A.C. 452; *Savage v. T. Wallis, Ltd.*, [1966] 1 Lloyd's Rep. 357; *McAuley v. London Transport Executive*, [1957] 2 Lloyd's Rep. 500; *Darbishire v. Warran*, [1963] 1 W.L.R. 1067; *Harlow & Jones, Ltd. v. Panex (International), Ltd.*, [1967] 2 Lloyd's Rep. 509; *Taylor v. Addems and Addems*, [1932] 1 W.W.R. 505; *Masny v. Carter-Hall-Aldinger Co.*, [1929] 3 W.W.R. 741; *Matters v. Baker and Fawcett*, [1951] S.A.S.R. 91; *Red Deer College v. Michaels*, [1976] 2 S.C.R. 324; *Newell v. Lucas*, [1964-65] N.S.W.R. 1597; *Mallett v. McMonagle*, [1970] A.C. 166; *Davies v. Taylor*, [1972] 3 All E.R. 836; *Schrump v. Koot* (1978), 18 O.R. (2d) 337; *McCarthy v. MacPherson's Estate* (1977), 14 Nfld. & P.E.I.R. 294, referred to.

Authors Cited

American Jurisprudence, 2nd ed., vol. 22, Rochester, N.Y., The Lawyers Co-operative Publishing Company; San Francisco, Calif., Bancroft-Whitney Company, 1965.

Cooper-Stephenson, Kenneth D. and Iwan B. Saunders. *Personal Injury Damages in Canada*, Toronto, The Carswell Company Limited, 1981.

Dobbs, Dan B. *Law of Remedies*, St. Paul, Minn., West Publishing Co., 1973.

Fleming, John G. *The Law of Torts*, 6th ed., Sydney, The Law Book Company Limited, 1983.

APPEAL AND CROSS-APPEAL from a judgment of the Ontario Court of Appeal (1981), 34 O.R. (2d) 151, varying an award of damages made by Callaghan J. Appeal and cross-appeal dismissed.

Brendan O'Brien, Q.C., for the appellant.

William Morris, Q.C., Rhona Waxman and *Kim Carpenter-Gunn*, for the respondent.

The judgment of the Court was delivered by

WILSON J.—The central issue in this case is how damages for personal injury are to be assessed where the victim of the accident unreasonably refuses to undergo the recommended surgery.

Electric Railways Company of London, [1912] A.C. 673; *Banco de Portugal v. Waterlow and Sons, Ltd.*, [1932] A.C. 452; *Savage v. T. Wallis, Ltd.*, [1966] 1 Lloyd's Rep. 357; *McAuley v. London Transport Executive*, [1957] 2 Lloyd's Rep. 500; *Darbishire v. Warran*, [1963] 1 W.L.R. 1067; *Harlow & Jones, Ltd. v. Panex (International), Ltd.*, [1967] 2 Lloyd's Rep. 509; *Taylor v. Addems and Addems*, [1932] 1 W.W.R. 505; *Masny v. Carter-Hall-Aldinger Co.*, [1929] 3 W.W.R. 741; *Matters v. Baker and Fawcett*, [1951] S.A.S.R. 91; *Red Deer College c. Michaels*, [1976] 2 R.C.S. 324; *Newell v. Lucas*, [1964-65] N.S.W.R. 1597; *Mallett v. McMonagle*, [1970] A.C. 166; *Davies v. Taylor*, [1972] 3 All E.R. 836; *Schrump v. Koot* (1978), 18 O.R. (2d) 337; *McCarthy v. MacPherson's Estate* (1977), 14 Nfld. & P.E.I.R. 294.

Doctrine citée

American Jurisprudence, 2nd ed., vol. 22, Rochester, N.Y., The Lawyers Co-operative Publishing Company; San Francisco, Calif., Bancroft-Whitney Company, 1965.

Cooper-Stephenson, Kenneth D. and Iwan B. Saunders. *Personal Injury Damages in Canada*, Toronto, The Carswell Company Limited, 1981.

Dobbs, Dan B. *Law of Remedies*, St. Paul, Minn., West Publishing Co., 1973.

Fleming, John G. *The Law of Torts*, 6th ed., Sydney, The Law Book Company Limited, 1983.

POURVOI ET POURVOI INCIDENT contre un arrêt de la Cour d'appel de l'Ontario (1981), 34 O.R. (2d) 151, qui a modifié les dommages-intérêts accordés par le juge Callaghan. Pourvoi et pourvoi incident rejetés.

Brendan O'Brien, c.r., pour l'appelant

William Morris, c.r., Rhona Waxman et *Kim Carpenter-Gunn*, pour l'intimé.

Version française du jugement de la Cour rendu par

LE JUGE WILSON—La question centrale du présent pourvoi est de savoir comment évaluer les dommages-intérêts pour blessures corporelles lorsque la victime d'un accident refuse déraisonnablement de subir l'intervention chirurgicale qui lui est recommandée.

1. The Facts

On March 31, 1976 the respondent sustained serious back injuries when his automobile was struck from behind by a vehicle driven by the appellant. Prior to that date the respondent had been employed for eleven years as a crane operator. Since the accident he has been disabled to such an extent that it has been impossible for him to return to work. Liability for negligent driving was admitted by the appellant and the trial was confined to the issue of damages.

The respondent's main injury, according to the medical evidence presented at trial, consisted of a disc protrusion of the cervical spine. Several medical experts testified to the effect that the recommended course of treatment for such an injury would be the surgical excision of the disc together with a spinal fusion. The trial judge accepted the evidence that this type of operation entails an approximately 70 per cent chance of success and that, if successful, could result in an almost 100 per cent recovery for the respondent who could thereafter return to work as a crane operator. The respondent, however, appears to have suffered from a great fear of surgery of any kind and insisted on assurance of a 100 per cent chance of success before consenting to undergo the recommended procedure. As neither his family physician nor his orthopaedic surgeon was able to provide such an absolute guarantee for this or any other type of surgery, the respondent refused to heed the medical advice. Accordingly, his back injuries have not improved and he continues to be disabled and out of work.

2. The Courts Below

At trial, Callaghan J. found that the respondent (plaintiff in the original action) had acted unreasonably in refusing to undergo the recommended surgery. Having made this finding he went on to state that any individual claiming damages for personal injuries has "a duty to mitigate his loss by obtaining proper medical treatment" and that he is not entitled to damages in respect of "any pain, suffering, loss of amenities, or loss of earnings consequent upon an unreasonable refusal to under-

1. Les faits

Le 31 mars 1976, l'intimé a subi des blessures graves au dos lorsque sa voiture a été heurtée à l'arrière par celle de l'appelant. Avant cette date, l'intimé travaillait depuis onze ans comme grutier. Depuis l'accident, il est invalide au point de ne pouvoir reprendre son travail. L'appelant a reconnu sa responsabilité pour négligence dans la conduite d'un véhicule à moteur et le procès n'a porté que sur la question des dommages-intérêts.

Selon la preuve médicale soumise en première instance, la blessure principale de l'intimé est une protrusion discale de la colonne vertébrale. Plusieurs experts en médecine ont témoigné que le traitement recommandé pour ce genre de blessure serait l'ablation chirurgicale du disque et une fusion vertébrale. Le juge de première instance a ajouté foi aux témoignages selon lesquels ce genre d'opération comporte environ 70 pour 100 de chances de succès et pourrait, à condition de réussir, entraîner une guérison presque totale de l'intimé qui pourrait, par la suite, reprendre son travail de grutier. Cependant, l'intimé semble avoir craint énormément toute espèce d'intervention chirurgicale et insisté pour qu'on lui assure à cent pour cent les chances de réussite avant de consentir à subir le traitement recommandé. Puisque ni son médecin de famille ni son chirurgien orthopédiste ne pouvaient fournir cette garantie absolue pour ce genre ou tout autre genre d'intervention chirurgicale, l'intimé a refusé de suivre l'avis des médecins. En conséquence, ses blessures au dos n'ont pas guéri et il continue d'être invalide et sans travail.

2. Les cours d'instance inférieure

En première instance, le juge Callaghan a conclu que l'intimé (le demandeur dans les procédures initiales) avait agi de façon déraisonnable en refusant de subir l'intervention chirurgicale recommandée. Après avoir tiré cette conclusion, il a ajouté que toute personne qui réclame des dommages-intérêts pour blessures corporelles a [TRADUCTION] «l'obligation de réduire ses pertes en se faisant soigner convenablement» et n'a pas droit à des dommages-intérêts pour [TRADUCTION] «toute

go medical treatment or surgical operation". Taking into account the estimated period of convalescence from a spinal fusion operation, Mr. Justice Callaghan found that, had the respondent acted reasonably, he would have been able to return to work by the end of March 1978. Accordingly, he found the appellant responsible for the respondent's loss of income for the two years between the date of the accident and March 31, 1978, which loss amounted to a total of $33,000. In addition, he assessed general damages for pain and suffering in sustaining the injuries at $25,000. When these awards were reduced to reflect the insurance benefits the respondent had received, the total amount for which the respondent received judgment at trial was $47,900 plus interest from November 25, 1977.

douleur, souffrance, perte de jouissance de la vie ou perte de revenu résultant du refus déraisonnable de subir un traitement médical ou une intervention chirurgicale». Tenant compte de la période estimative de convalescence nécessaire par suite d'une opération de fusion vertébrale, le juge Callaghan a conclu que si l'intimé avait agi de façon raisonnable, il aurait pu reprendre son travail dès la fin de mars 1978. En conséquence, il a tenu l'appelant responsable de la perte de revenu subie par l'intimé pendant les deux années comprises entre la date de l'accident et le 31 mars 1978, perte qui s'élève au total à 33 000 $. De plus, il a évalué à 25 000 $ les dommages-intérêts généraux pour douleur et souffrances résultant des blessures subies. Après réduction de ces montants de manière a refléter les prestations d'assurance touchées par l'intimé, ce dernier s'est vu accorder en première instance la somme totale de 47 900 $ plus les intérêts à compter du 25 novembre 1977.

In the Ontario Court of Appeal [(1981), 34 O.R. (2d) 151] Blair J.A. (with whom Goodman J.A. concurred) agreed generally with the line of reasoning pursued by the trial judge, but differed in his calculation of damages to the extent that he did not cut off the appellant's responsibility for lost earnings at the date when the respondent might have been expected to recuperate from the operation and return to work. Rather, he took into account the fact that the recommended surgery entailed only a 70 per cent chance of success and adjusted the award for loss of income upward in order to take into account the fact that, even if the respondent had acted reasonably in the circumstances, his recovery would not have been assured. After making a series of adjustments to reflect the contingencies entailed in the surgery and the respondent's future job prospects had he undergone the operation, Blair J.A. awarded damages for loss of earnings in the amount of $81,661. He then deducted the insurance benefits which the respondent had received and added the $25,000 representing general damages for pain and suffering. This produced a total award of $103,651.

En Cour d'appel de l'Ontario [(1981), 34 O.R. (2d) 151], le juge Blair (aux motifs duquel le juge Goodman a souscrit) s'est dit d'accord, dans l'ensemble, avec le genre de raisonnement adopté par le juge de première instance, mais a divergé d'opinion avec lui quant au calcul des dommages-intérêts, dans la mesure où il n'a pas mis fin à la responsabilité de l'appelant pour la perte de revenu à la date à laquelle on aurait pu s'attendre à ce que l'intimé soit rétabli de l'opération et retourne à son travail. Il a plutôt pris en considération le fait que l'intervention chirurgicale recommandée comportait seulement 70 pour 100 de chances de succès et a augmenté le montant accordé pour la perte de revenu de manière à tenir compte du fait que, même si l'intimé avait agi de façon raisonnable dans les circonstances, son rétablissement n'aurait pas été garanti. Après avoir procédé à une série d'ajustements de manière à refléter les aléas de l'intervention chirurgicale et les possibilités d'emploi futur de l'intimé si ce dernier avait subi l'opération, le juge Blair a accordé des dommages-intérêts de 81 661 $ pour la perte de revenu. Il a ensuite déduit les prestations d'assurance touchées par l'intimé et a ajouté 25 000 $ de dommages-intérêts généraux pour douleur et souffrances. Le montant total accordé a été ainsi de 103 651 $.

A strong dissent in the Court of Appeal was voiced by MacKinnon A.C.J.O. based on his analysis of the English case law on the issue of the refusal of a tort victim to seek medical care. The principle he elicited from the English authorities is that a tort victim's unreasonable refusal to undergo medical treatment constitutes an intervening cause which effectively cuts off the liability of the initial tortfeasor. Accordingly, as applied by MacKinnon A.C.J.O., this principle has the effect of barring the respondent from any claim for loss of income beyond the date on which he might reasonably be expected to have returned to work had he undergone the surgery and the surgery had been a success. While MacKinnon A.C.J.O. was prepared to take account of the approximately 30 per cent chance of the operation's failure in assessing the reasonableness of the respondent's refusal of the surgery, he was not prepared to factor this percentage into the *quantum* of loss awarded once the respondent was held to have acted unreasonably. Although he would have varied the damages calculation in some minor respects, the overall thrust of his dissent was to approve the approach taken by Callaghan J. at trial.

Le juge en chef adjoint MacKinnon a exprimé énergiquement sa dissidence en s'appuyant sur son analyse de la jurisprudence anglaise portant sur la question du refus de la victime d'une faute de recourir à des soins médicaux. Selon le principe qu'il a dégagé de la jurisprudence anglaise, le refus déraisonnable de la victime d'une faute de subir un traitement médical constitue une cause nouvelle qui a pour effet de mettre fin à la responsabilité de l'auteur initial de la faute. En conséquence, selon l'application qu'en a fait le juge en chef adjoint MacKinnon, ce principe a pour effet d'empêcher l'intimé de réclamer quoi que ce soit pour la perte de revenu subie après la date à laquelle on aurait pu raisonnablement s'attendre à ce qu'il retourne au travail s'il avait subi avec succès l'intervention chirurgicale. Même si le juge en chef adjoint MacKinnon était disposé à tenir compte de la probabilité d'environ 30 pour 100 que l'opération ne réussisse pas en évaluant le caractère raisonnable du refus de l'intimé de subir l'intervention chirurgicale, il n'était pas prêt à tenir compte de ce pourcentage dans le montant accordé pour la perte après avoir conclu que l'intimé a agi de façon déraisonnable. Quoiqu'il aurait modifié le calcul des dommages-intérêts sous certains aspects de moindre importance, la portée globale de sa dissidence a été d'approuver le point de vue adopté par le juge Callaghan en première instance.

3. Unreasonable Refusal of Treatment

The single most noteworthy fact with which this appeal is concerned is that the trial judge found the respondent to have been unreasonable in his refusal to accept the recommended medical treatment. As noted by each of the member of the House of Lords in *Steele v. Robert George and Co.*, [1942] A.C. 497, this question is most appropriately left to the trier of fact to decide. There is no reason to conclude that Callaghan J. committed any error of law in determining this issue in the case at bar. Both the majority and the dissent in the Ontario Court of Appeal were of the view that there was sufficient evidence to support the trial judge's finding and, in the absence of any suggestion that he misdirected himself or applied the wrong test to the facts presented to him, there is no basis on which this Court can interfere with his

3. Le refus déraisonnable de subir un traitement

Le fait le plus important auquel touche le présent pourvoi a trait à la conclusion du juge de première instance portant que l'intimé a été déraisonnable en refusant de subir le traitement médical recommandé. Comme le souligne chacun des membres de la Chambre des lords dans l'arrêt *Steele v. Robert George and Co.*, [1942] A.C. 497, c'est au juge des faits qu'il appartient vraiment de trancher cette question. Il n'y a pas de raison de conclure que le juge Callaghan a commis une erreur de droit quelconque en tranchant cette question en l'espèce. En Cour d'appel de l'Ontario, les juges formant la majorité et le juge dissident ont tous été d'avis qu'il y avait suffisamment d'éléments de preuve pour étayer la conclusion du juge de première instance et, en l'absence de toute prétention qu'il s'est trompé ou qu'il a appliqué le

finding. He alone had the opportunity to assess the evidence and determine the issue of the respondent's reasonableness at first hand.

It may, however, be opportune, since this Court now has the concept of reasonableness in relation to a refusal of medical or surgical treatment before it, to make reference to some of the difficult elements involved in a finding of unreasonableness before considering precisely how such a finding affects the legal principles otherwise applicable on an assessment of damages.

(1) Unreasonableness and the "Thin Skull" Doctrine

The first difficult issue which arises in assessing the reasonableness or otherwise of a plaintiff's refusal of medical treatment is the extent, if any, to which subjective attributes of the plaintiff may be taken into account by the court. In the case at bar it was submitted by the respondent that, whether or not his refusal of treatment was perceived as objectively unreasonable, its source lay in an innate fear of surgery which he could not be expected to overcome. Accordingly, he invoked a variation of the long accepted principle that "if the wrong is established the wrongdoer must take the victim as he finds him": *per* Lord Wright in *Hay or Bourhill v. Young*, [1943] A.C. 92, at pp. 109-10. It followed from this, he argued, that the injuries resulting from his inordinate fear, which might otherwise have been avoided if a reasonable decision regarding medical treatment had been made, were analagous to the type of aggravated injuries which might be suffered by a haemophiliac inflicted with a bleeding wound or any other victim with a predisposed physiological oversensitivity: *Bishop v. Arts & Letters Club of Toronto* (1978), 83 D.L.R. (3d) 107 (Ont. H.C.)

It is, of course, well established that damages for aggravated injuries consequent on some preexisting infirmity of the plaintiff are recoverable

mauvais critère aux faits qui lui ont été soumis, il n'y a rien qui puisse justifier cette Cour de modifier sa conclusion. Lui seul avait la possibilité d'évaluer directement la preuve et de trancher la question du caractère raisonnable de l'intimé.

Cependant, puisque cette Cour doit étudier le concept du caractère raisonnable du refus de subir un traitement médical ou chirurgical, il peut être opportun de mentionner certaines difficultés que comporte le fait de conclure au caractère déraisonnable avant d'analyser précisément comment une telle conclusion modifie les principes juridiques applicables par ailleurs à l'évaluation des dommages-intérêts.

(1) Caractère déraisonnable et doctrine de la «vulnérabilité de la victime»

La première difficulté qui se présente lors de l'évaluation du caractère raisonnable ou déraisonnable du refus par un demandeur de subir un traitement médical est la mesure, s'il y a lieu, dans laquelle la cour peut tenir compte des caractéristiques subjectives du demandeur. En l'espèce, l'intimé a soutenu que, peu importe que son refus de subir le traitement soit perçu ou non comme objectivement déraisonnable, il s'explique par une crainte innée de subir une intervention chirurgicale, qu'il ne pouvait être censé surmonter. En conséquence, il a invoqué une variante du principe accepté depuis longtemps selon lequel [TRADUCTION] «si la faute est prouvée, son auteur doit subir les conséquences de l'état antérieur de la victime»: lord Wright dans l'arrêt *Hay or Bourhill v. Young*, [1943] A.C. 92, aux pp. 109 et 110. Il s'ensuit, a-t-il soutenu, que le préjudice qui découle de sa peur insurmontable, qui aurait pu être par ailleurs évité si une décision raisonnable avait été prise à propos du traitement médical, est semblable au préjudice aggravé que pourrait subir un hémophile victime d'une hémorragie due à une blessure ou une autre victime prédisposée à une hypersensibilité physiologique: *Bishop v. Arts & Letters Club of Toronto* (1978), 83 D.L.R. (3d) 107 (H.C. Ont.)

Il est évidemment bien établi que des dommages-intérêts relatifs à des blessures aggravées résultant d'une infirmité préexistante du demandeur

even if the infirmity is of a psyehological nature: see, *e.g. Love v. Port of London Authority*, [1959] 2 Lloyd's Rep. 541 (Q.B.); *Gray v. Cotic*, [1983] 2 S.C.R. 2. As Geoffrey Lane J. said in *Malcolm v. Broadhurst*, [1970] 3 All E.R. 508, at p. 511, "there is no difference in principle between an egg-shell skull and an egg-shell personality". Indeed, it would seem that the *locus classicus* of the "thin skull rule", the decision of Kennedy J. in *Dulieu v. White & Sons*, [1901] 2 K.B. 669, was in fact a case of aggravated injuries which were triggered by the impact of the defendant's tortious act on the plaintiff's inchoate psychological hypersensitivity.

peuvent être obtenus même si l'infirmité est de nature psychologique: voir, par exemple, *Love v. Port of London Authority*, [1959] 2 Lloyd's Rep. 541 (B.R.); *Gray c. Cotic*, [1983] 2 R.C.S. 2. Comme l'affirme le juge Geoffrey Lane dans *Malcolm v. Broadhurst*, [1970] 3 All E.R. 508, à la p. 511, [TRADUCTION] «en principe, il n'y a pas de différence entre la vulnérabilité physique et la vulnérabilité psychologique». En réalité, il semblerait que la source classique de la «règle de la vulnérabilité de la victime», c.-à-d. l'arrêt du juge Kennedy *Dulieu v. White & Sons*, [1901] 2 K.B. 669, ait été une affaire de préjudice aggravé déclenché par l'effet de la faute du défendeur sur l'hypersensibilité psychologique innée du demandeur.

The key word, however, is pre-existing. Once it is acknowledged that there is such a thing as a "psychological thin skull", the inquiry shifts to (a) the timing and (b) the nature of the alleged psychological infirmity.

Le mot clé est cependant le mot préexistante. Dès que l'on reconnaît qu'il y a «vulnérabilité psychologique de la victime», l'examen doit alors porter sur a) l'élément de temps et b) la nature de la prétendue infirmité psychologique.

(a) Timing

a) L'élément de temps

With regard to timing, it would seem that the very concept of a thin skulled plaintiff embodies within it the notion that the oversensitive condition was pre-existing at the time of the injury. That is to say, where the ultimate consequence of which the plaintiff complains is not due to the impact of the defendant's wrongful act on some existing sensitivity of the plaintiff, but rather arises only subsequent to the injury and independent of any intrinsic physiological or psychological problem for which the tortious act has served as a catalyst, the ordinary rules of recoverability apply. By way of illustration, where a blow to the plaintiff's chest inflicted by the defendant ultimately results in the development of a malignancy, but there is no evidence of any pre-existing susceptibility to such a disease in the plaintiff, then the ordinary rules of causation apply: *Blackstock v. Foster*, [1938] S.R. (N.S.W.) 341. On the other hand, where the defendant's negligent act results in the plaintiff's lip being burned and, due to a rare pre-malignant condition of the plaintiff, this burn turns into a fatal malignant growth, then the pre-existing "thin skull" serves to displace the otherwise applicable

Quant à l'élément de temps, il semblerait que le concept même de la vulnérabilité du demandeur comporte l'idée que l'état d'hypersensibilité existait déjà au moment où la victime a été blessée. Autrement dit, les règles ordinaires en matière de dédommagement s'appliquent lorsque la conséquence ultime dont le demandeur se plaint n'est pas due à l'effet de la faute du défendeur sur une certaine sensibilité préexistante du demandeur, mais survient plutôt seulement après avoir subi la blessure, indépendamment de tout problème physiologique ou psychologique auquel la faute a servi de catalyseur. Par exemple, si un coup porté par le défendeur à la poitrine du demandeur entraîne finalement l'apparition d'une tumeur maligne, sans qu'il y ait de preuve que le demandeur était prédisposé à souffrir d'une telle maladie, alors les règles ordinaires en matière de causalité s'appliquent: *Blackstock v. Foster*, [1938] S.R. (N.S.W.) 341. D'autre part, lorsque le demandeur subit une brûlure de la lèvre par suite de la faute du défendeur et qu'en raison d'une prédisposition rare du demandeur, cette brûlure se transforme en tumeur maligne mortelle, alors la «vulnérabilité préexis-

rules of causation: *Smith v. Leech Brain & Co.*, [1962] 2 Q.B. 405.

The same dichotomy must presumably apply to cases of a psychological thin skulled plaintiff. A significant distinction has to be made between persons who subsequent to an accident develop an emotional or psychological infirmity and those who bring a pre-existing emotional or psychological infirmity to the accident. The question posed by the kind of case we have here is: do persons in the latter group have to meet the objective test of reasonableness when their refusal of medical help is being assessed by the trier of fact or are their subjective attributes to be given due consideration?

In *Marcroft v. Scruttons, Ltd.*, [1954] 1 Lloyd's Rep. 395 (C.A.), the plaintiff, a dock labourer, was unloading cargo from a steamship at the Liverpool docks when the wire of a derrick which was unloading cargo from part of the lower hold fouled the hatch beam. The hatch cover on which the plaintiff was standing was dislodged and he fell about ten feet into the hold. He suffered no physical injuries apart from bruises but anxiety neurosis and depression following the shock incapacitated him from work. Liability was not contested by the plaintiff; the only issue was damages.

The plaintiff saw his panel doctor who referred him to a psychologist. She saw him on several occasions and observed that he had tremors of the hand, mouth, eyelids, general shaking of the body, severe depression and lack of confidence. She recommended that he go to the Rainhill Mental Hospital for electric shock treatment. He refused to go because it was a mental hospital. The trial judge found that this was unreasonable. When the case went to appeal Lord Justice Singleton said it was one of the most difficult cases on the assessment of damages that he had encountered in a long time. He adverted to the fact that some of the

tante de la victime» a pour effet d'écarter les règles de causalité par ailleurs applicables: *Smith v. Leech Brain & Co.*, [1962] 2 Q.B. 405.

La même dichotomie doit probablement s'appliquer au cas de vulnérabilité psychologique d'un demandeur. Il faut faire une distinction importante entre les personnes qui, à la suite d'un accident, deviennent infirmes sur le plan émotif ou psychologique et celles qui souffraient déjà d'une infirmité émotive ou psychologique avant l'accident. La question que pose le genre d'affaire dont nous sommes saisis en l'espèce est la suivante: les personnes de la dernière catégorie doivent-elles satisfaire au critère objectif du caractère raisonnable lorsque le juge des faits évalue leur refus de recevoir des soins médicaux ou doit-on prendre dûment en considération leurs caractéristiques subjectives?

Dans l'affaire *Marcroft v. Scruttons, Ltd.*, [1954] 1 Lloyd's Rep. 395 (C.A.), le demandeur, qui était débardeur, déchargeait des marchandises d'un navire sur les quais de Liverpool lorsque le câble d'une grue qui déchargeait des marchandises d'une partie de la cale inférieure a heurté la poutre d'écoutille. Le panneau d'écoutille sur lequel se tenait le demandeur s'est détaché et celui-ci est tombé d'une hauteur d'environ dix pieds dans la cale. Il ne s'est infligé aucune autre blessure que des ecchymoses, mais une névrose d'angoisse et une dépression consécutives au choc l'ont rendu incapable de travailler. Il n'y a pas eu de contestation de responsabilité de la part du demandeur; le litige portait uniquement sur les dommages-intérêts.

Le demandeur a consulté son médecin conventionné qui lui a dit de s'adresser à une psychologue. Celle-ci l'a rencontré à maintes reprises et a constaté des tremblements de la main, de la bouche, des paupières, des tremblements de tout le corps, une dépression grave et un manque de confiance en soi. Elle lui a recommandé de se rendre au Rainhill Mental Hospital pour y subir des électrochocs. Il a refusé d'y aller parce qu'il s'agissait d'un hôpital psychiatrique. Le juge de première instance a conclu que cela était déraisonnable. En appel, le lord juge Singleton a affirmé qu'il s'agissait d'un cas d'évaluation de dommages-inté-

doctors who gave evidence testified "that this man was of a type who might be more readily affected by an accident of this kind than other men would be". He also referred to the medical evidence that many people have a natural antipathy to entering mental hospitals. He had to deal with the contention made by counsel for the plaintiff that the plaintiff's condition really was such that he could not make up his mind. Dr. Evans, one of the defendant's witnesses, said, at p. 398:

> I felt he was incapable of really coherent thought when I saw him. I did not think he was really capable of reasoning the thing out. I think it was just a matter of taking fright at the mere mention of mental hospital.

Lord Justice Singleton dealt with that in the following way, at p. 399:

> A man who is in an anxiety state may have difficulty in making up his mind, but on a question as to the treatment which he should have his mind is, or ought to be, made up for him by his own medical advisers. That is one of the purposes of having medical advisers. The patient would not know what he ought to do; the patient takes medical advice, and the patient ought to be guided by his medical advisers.

His Lordship concluded at the same page and at p. 400:

> I do not wish to say anything that would hurt the feelings of a plaintiff in a case of this kind, but I believe it to be the duty of this Court to say that if a man is recommended by his own medical advisers and by others to undergo a course of treatment, he ought to undergo it; if he is advised that it gives him a reasonable chance of recovery, and if the treatment is reasonable, he ought to undergo it; if he will not, and does not, he must see that it is a little hard upon the defendants if they are to be asked to pay damages in respect of a period extending afterwards. If the general opinion is that treatment would cure him, or, at least, render him in a much better state in every way, then he ought to undergo the treatment.

It is interesting to note that Lord Justice Denning in his concurring reasons indicates, at p. 401,

rêts parmi les plus difficiles qu'il lui ait été donné de rencontrer depuis longtemps. Il a parlé du fait que certains des médecins qui ont témoigné ont déclaré [TRADUCTION] «que cet homme était du genre de ceux qui pourraient être affectés plus facilement que d'autres par un accident de ce type». Il a aussi fait état des éléments de preuve médicale selon lesquels de nombreuses personnes répugnent naturellement à se faire traiter dans des hôpitaux psychiatriques. Il avait dû examiner la prétention de l'avocat du demandeur que l'état de ce dernier était tel qu'il n'était pas vraiment en mesure de prendre une décision. Le Dr Evans, qui a déposé pour la défenderesse, affirme, à la p. 398:

> [TRADUCTION] J'ai senti qu'il était incapable de penser de façon vraiment cohérente lorsque je l'ai rencontré. Je ne crois pas qu'il était vraiment capable d'entendre raison. Je crois qu'il prenait tout bonnement peur à la seule mention de l'hôpital psychiatrique.

Le lord juge Singleton traite cette question de la façon suivante, à la p. 399:

> [TRADUCTION] Une personne qui souffre d'angoisse peut avoir de la difficulté à prendre une décision, mais à propos du traitement à lui prodiguer, la décision est ou se doit d'être prise par son médecin. C'est là le rôle du médecin, le patient n'est pas censé savoir quoi faire; le patient consulte le médecin et doit être guidé par ce dernier.

Sa Seigneurie conclut, à la même page et à la p. 400:

> [TRADUCTION] Je ne veux rien dire qui puisse froisser le demandeur dans une affaire de ce genre, mais je crois qu'il est du devoir de cette Cour d'affirmer que si une personne se voit recommander par ses propres médecins et d'autres médecins de subir un traitement, celle-ci se doit de le subir; si on lui dit qu'elle a des chances raisonnables de guérir et si le traitement est raisonnable, elle se doit de le subir; si elle ne veut pas le subir et ne le subit pas, elle doit se rendre compte que c'est un peu trop exiger des défendeurs que de leur demander de payer des dommages-intérêts pour la période de temps qui suit ce refus. Si on estime de manière générale que le traitement permettrait de la guérir ou, au moins, d'améliorer sensiblement son état à tous égards, alors elle se doit de subir le traitement.

Il est intéressant de noter que, dans ses motifs concordants, le lord juge Denning indique, à la

that the plaintiff had "unbeknown to him, a constitutional weakness which made it very serious for him, because the accident operating on that weakness produced in him a very severe nervous shock, trembling from head to foot". He nevertheless found that this factor had to be disregarded. He said at p. 401:

> Viewing the matter objectively, he was quite unreasonable in refusing to follow their advice; but viewing the matter subjectively, the man's attitude was quite understandable. He was an uneducated, ignorant man who did not realize that a mental hospital nowadays is very different from what it was 30 or 40 years ago; and, moreover, owing to his anxiety neurosis, he was not in a fit state to make reasonable decisions. The difficult question in the case is whether we are to admit this subjective condition of his as a reason for refusing medical treatment. I think not. We should do great harm if we allowed him to go on receiving compensation for the rest of his life because of his refusal to accept medical treatment. Persons who suffer from an anxiety state have more chance of recovery if they are treated as responsible human beings and are expected to behave reasonably, rather than as weaklings who can give way to their weakness and expect to get paid for it. [Emphasis added.]

The Court in *Marcroft* clearly refused to permit subjective attributes to enter into the question of the reasonableness of the plaintiff's refusal of medical treatment. Their Lordships' conclusion that the plaintiff was more vulnerable than most prior to the accident to the effects of shock does not appear to have affected the outcome either in terms of the reasonableness of his refusal of medical treatment or in relation to aggravated damages.

By way of contrast, in *Elloway v. Boomars* (1968), 69 D.L.R. (2d) 605 (B.C.S.C.), the plaintiff who suffered minor injuries in an automobile accident developed a psychosis of a schizophrenic nature which by the time of trial was largely disabling. McIntyre J. found on the medical evidence that the plaintiff suffered from a pre-existing condition which predisposed him to schizophrenic illness and that the accident, operating on that predisposition, brought about the full schi-

p. 401, que le demandeur avait [TRADUCTION] «sans le savoir, une faiblesse diathésique qui a aggravé les choses pour lui parce qu'en agissant sur cette faiblesse, l'accident lui a causé un choc nerveux très grave et des tremblements de la tête aux pieds». Il a néanmoins conclu qu'il ne fallait pas tenir compte de ce facteur. Il affirme, à la p. 401:

> [TRADUCTION] Du point de vue objectif, il a été tout à fait déraisonnable de sa part de refuser de suivre leur avis; cependant, du point de vue subjectif, l'attitude de cet homme est très compréhensible. Il s'agit d'un homme sans instruction et mal informé qui ne s'est pas rendu compte qu'aujourd'hui l'hôpital psychiatrique est très différent de ce qu'il était il y a 30 ou 40 ans; de plus à cause de sa névrose d'angoisse, il n'était pas en état de prendre une décision raisonnable. Le problème qui se pose en l'espèce est de savoir si nous devons accepter son état subjectif comme une justification de son refus de subir le traitement médical. Je ne le crois pas. Nous agirions très mal en lui permettant de toucher une indemnité pour le reste de ses jours par suite de son refus de subir un traitement médical. Les personnes qui souffrent d'angoisse ont plus de chances de guérir si elles sont traitées comme des personnes responsables et si on s'attend à ce qu'elles se conduisent de façon raisonnable plutôt que comme des faibles qui peuvent donner libre cours à leur faiblesse et s'attendre à être payées en retour. [C'est moi qui souligne.]

Dans l'arrêt *Marcroft*, la cour a clairement refusé de permettre que les caractéristiques subjectives comptent dans la détermination du caractère raisonnable du refus par le demandeur de subir le traitement médical. La conclusion de leurs Seigneuries que le demandeur était, avant l'accident, plus vulnérable que la plupart des gens aux effets de choc ne semble pas avoir modifié l'issue ni en ce qui concerne le caractère raisonnable de son refus d'être traité ni en ce qui a trait à l'aggravation du préjudice.

Par contre, dans l'arrêt *Elloway v. Boomars* (1968), 69 D.L.R. (2d) 605 (C.S.C.-B.), le demandeur qui avait subi des blessures mineures dans un accident d'automobile a commencé à souffrir d'une psychose de nature schizophrénique qui l'affectait énormément à l'époque du procès. Le juge McIntyre a conclu, en se fondant sur la preuve médicale, que le demandeur était, avant l'accident, dans un état qui le prédisposait à la schizophrénie et que l'accident, en agissant sur cette prédisposition,

zophrenic illness. The plaintiff had been advised to take treatment for his condition but he refused. McIntyre J. concluded, however, that his psychosis was itself a factor in his refusal and he could not therefore be held responsible for the worsening of his condition. Damages must be assessed on the basis that he had not wilfully failed in his duty to mitigate.

In *McGrath v. Excelsior Life Insurance Co.* (1974), 6 Nfld. & P.E.I.R. 203 (Nfld. T.D.), the plaintiff, an unskilled labourer, injured his back while working as a painter's helper. He was in continuous pain. One specialist recommended a spinal fusion to alleviate the pain. Another said it wouldn't help. The plaintiff decided not to have it and the insurance company discontinued his disability benefits. Higgins J. said, at p. 208:

> The position therefore is that Dr. Shapter and Dr. Russell, both specialists in their respective fields, are in complete disagreement as to the benefits which might result from surgery. Faced with this conflict of expert opinion, it is not to be wondered at that the patient, an unlettered man, would be reluctant to agree to an operation. I do not regard his refusal, in these circumstances, as unreasonable. [Emphasis added.]

In *Morgan v. T. Wallis Ltd.*, [1974] 1 Lloyd's Rep. 165, the plaintiff, aged 33, was employed by the defendants as a lighterman on the River Thames. In January 1970, a stevedore employed by the defendants on the ship *Cymric* threw some wire rope on to an adjoining barge on which the plaintiff was working. While trying to avoid this the plaintiff fell into the hold and injured his back. There was no dispute as to liability. Special damages were agreed. General damages were disputed on the ground that the plaintiff unreasonably refused to undergo tests and an operation out of a genuine, though misplaced, fear. The evidence indicated that the fear was beyond his control. Mr. Justice Browne found that the plaintiff's refusal to undergo the tests and the operation was unreasonavait provoqué une schizophrénie caractérisée. On avait conseillé au demandeur de se faire traiter pour sa maladie, mais il a refusé. Le juge McIntyre a toutefois conclu que sa psychose était elle-même un facteur de son refus et qu'on ne pouvait en conséquence le tenir responsable de l'aggravation de son état. Les dommages-intérêts doivent être évalués en considérant qu'il n'a pas délibérément manqué à son obligation de limiter le préjudice subi.

Dans la décision *McGrath v. Excelsior Life Insurance Co.* (1974), 6 Nfld. & P.E.I.R. 203 (D.P.I. T.-N.), le demandeur, qui était manoeuvre, s'est blessé au dos en travaillant comme aide-peintre. Il éprouvait des douleurs persistantes. Un spécialiste a recommandé de pratiquer une fusion vertébrale pour calmer la douleur. Un autre a affirmé que ce serait inutile. Le demandeur a décidé de ne pas se faire opérer et la compagnie d'assurance a cessé de lui verser des prestations d'invalidité. Le juge Higgins affirme ceci, à la p. 208:

> [TRADUCTION] La situation est donc la suivante: le Dr Shapter et le Dr Russell, des spécialistes dans leurs domaines respectifs, ne s'entendent absolument pas sur les avantages qui pourraient résulter d'une intervention chirurgicale. Face à cette divergence d'opinions des experts, il n'est pas étonnant que le patient, qui est illettré, se soit montré réticent à consentir à l'opération. Je ne considère pas son refus comme déraisonnable dans ces circonstances. [C'est moi qui souligne.]

Dans l'arrêt *Morgan v. T. Wallis Ltd.*, [1974] 1 Lloyd's Rep. 165, le demandeur, âgé de 33 ans, était employé par la défenderesse comme batelier sur la Tamise. En janvier 1970, un arrimeur au service de la défenderesse sur le navire *Cymric* a lancé un câble sur une barge adjacente sur laquelle travaillait le demandeur. En essayant de l'éviter, le demandeur est tombé dans la cale et s'est blessé le dos. La responsabilité n'a pas été contestée. Le montant des dommages-intérêts spéciaux a fait l'objet d'un accord. Les dommages-intérêts généraux ont été contestés pour le motif que le demandeur avait refusé déraisonnablement de subir des examens et une opération à cause d'une crainte réelle mais déplacée. Il est ressorti de la preuve que cette crainte était incontrôlable chez lui. Le juge Browne a conclu que le refus du demandeur

able. Quoting from his reasons at p. 170:

Everybody agrees, and I emphasize strongly, that the plaintiff in the present case is not in the slightest degree a malingerer, and is a completely honest man who genuinely holds the beliefs and fears about which he has told us in evidence. But in deciding whether the defendants have proved that he has unreasonably refused to have the investigation and operation in question here, it seems to me clear from the authorities to which I have referred, that I must apply an objective test, in this sense, would a reasonable man in all the circumstances, receiving the advice which the plaintiff did receive, have refused the operation? I think this question must be considered as at the times when his decision was made and on the basis of the advice he then received. If the plaintiff preferred and prefers to go on as he is rather than to have the operation no-one can blame him. But the question I have to consider is not, "Is the plaintiff to blame for refusing the operation?" but, "Is it fair and reasonable to make the defendants pay for his refusal?" [Emphasis added.]

It is, however, of interest to note that at p. 173 Browne J. states:

As I have said several times, I entirely accept that the plaintiff's fear and his inability to bring himself to agree to the operation are absolutely genuine. But in my view there is no evidence that this is due to any physical or mental or psychological disability which existed before the accident and which would entitle the plaintiff to say that the defendants must take the plaintiff as they find him. [Emphasis added.]

He concluded at the same page:

As I have said, I think one must decide the question whether the plaintiff's refusal was unreasonable by the objective standard of the reasonable man, and the fact that this particular plaintiff has got himself into an emotional state where he finds it impossible to agree to the operation is, in my view, no ground for saying that his refusal was not unreasonable.

It would appear then on the English authorities that a psychological "thin skull" developed subsequent to the tortious act is not a factor that can be considered in relation to reasonableness: the objective test prevails in the absence of any pre-existing condition.

de subir les examens et l'opération était déraisonnable. Voici un extrait de ses motifs tiré de la p. 170:

[TRADUCTION] Tous reconnaissent, et je le souligne avec vigueur, que le demandeur en l'espèce ne simule absolument pas une maladie, qu'il est tout à fait honnête et qu'il croit et craint véritablement les choses qu'il nous a dites dans sa déposition. Mais pour ce qui est de décider si la défenderesse a prouvé qu'il a refusé déraisonnablement de subir les examens et l'opération en cause en l'espèce, il me semble clair, d'après la jurisprudence que j'ai consultée, que je me dois d'appliquer un critère objectif, c'est-à-dire une personne raisonnable dans les mêmes circonstances, ayant reçu les conseils que le demandeur a reçus, aurait-elle refusé l'opération? Je crois qu'il faut examiner cette question par rapport à l'époque où il a pris sa décision et en fonction des conseils qu'il a alors reçus. Si le demandeur a préféré et préfère toujours rester comme il est plutôt que de subir l'opération, personne ne peut le lui reprocher. Mais la question qu'il me faut examiner n'est pas «Le demandeur est-il à blâmer pour avoir refusé l'opération?» mais «Est-il juste et raisonnable d'obliger la défenderesse à payer pour son refus?» [C'est moi qui souligne.]

Il est cependant utile de souligner qu'à la p. 173, le juge Browne affirme:

[TRADUCTION] Comme je l'ai déjà dit à plusieurs reprises, je conviens entièrement que la crainte du demandeur et son incapacité de se décider à consentir à l'opération sont absolument réelles. Mais à mon avis, il n'y a aucune preuve que cela est dû à une incapacité physique, mentale ou psychologique qui existait avant l'accident et qui permettrait au demandeur d'affirmer que la défenderesse doit subir les conséquences de l'état antérieur du demandeur. [C'est moi qui souligne.]

Il conclut, à la même page:

[TRADUCTION] Comme je l'ai déjà dit, je crois qu'il faut décider si le refus du demandeur a été déraisonnable en fonction du critère objectif de la personne raisonnable et le fait que le demandeur aux présentes se soit trouvé dans un état émotif qui l'a empêché de consentir à l'opération ne permet pas, à mon avis, d'affirmer que son refus n'était pas déraisonnable.

Il semblerait donc, d'après la jurisprudence anglaise, que la vulnérabilité psychologique qui découle de l'acte fautif n'est pas un facteur que l'on peut prendre en considération pour déterminer le caractère raisonnable: le critère objectif s'applique en l'absence de toute condition préexistante.

(b) Nature

The other element that has to be considered in determining whether the objective test of reasonableness applies to the decision made by the alleged thin skulled plaintiff is the nature of the pre-existing psychological infirmity. It is evident that not every pre-existing state of mind can be said to amount to a psychological thin skull. It seems to me that the line must be drawn between those plaintiffs who are capable of making a rational decision regarding their own care and those who, due to some pre-existing psychological condition, are not capable of making such a decision. As pointed out by Professor Fleming, a plaintiff cannot by making an unreasonable decision in regard to his own medical treatment "unload upon the defendant the consequences of his own stupidity or irrational scruples": Fleming, *The Law of Torts* (6th ed. 1983), p. 226. Accordingly, non-pathological but distinctive subjective attributes of the plaintiff's personality and mental composition are ignored in favour of an objective assessment of the reasonableness of his choice. So long as he is capable of choice the assumption of tort damages theory must be that he himself assumes the cost of any unreasonable decision. On the other hand, if due to some pre-existing psychological condition he is incapable of making a choice at all, then he should be treated as falling within the thin skull category and should not be made to bear the cost once it is established that he has been wrongfully injured.

I believe that Lord Justice Singleton's concern in *Marcroft v. Scruttons*, *supra*, stemmed from his doubt as to whether the plaintiff in that case was capable of making a rational decision. Not only that, there was some indication in the medical evidence that his incapacity may have been itself a consequence of the trauma induced by the accident. If this is so, it would appear manifestly unjust to cut off his recovery for failure to mitigate his damages through a rational decision as to treatment. The reasons of Lord Justice Denning are even more baffling. He attributes the plain-

b) La nature

L'autre élément dont il faut tenir compte pour déterminer si le critère objectif du caractère raisonnable s'applique à la décision prise par le demandeur prétendument vulnérable est la nature de l'infirmité psychologique préexistante. Il est évident qu'on ne peut pas dire que tous les états d'esprit préexistants équivalent à une vulnérabilité psychologique. Il me semble qu'il faut faire la distinction entre les demandeurs capables de prendre une décision rationnelle à propos de leur propre santé et ceux qui, à cause d'un état psychologique préexistant, sont incapables de prendre une telle décision. Comme le souligne le professeur Fleming, le demandeur ne peut, en prenant une décision déraisonnable quant à ses propres soins médicaux [TRADUCTION] «faire assumer au défendeur les conséquences de sa propre bêtise ou de ses hésitations irrationnelles»: Fleming, *The Law of Torts* (6th ed. 1983), à la p. 226. En conséquence, les caractéristiques subjectives, non pathologiques mais distinctives, de la personnalité du demandeur et de sa constitution psychologique sont écartées en faveur d'une évaluation objective du caractère raisonnable de son choix. Dans la mesure où il est capable de faire un choix, il faut présumer, selon la théorie des dommages-intérêts en matière délictuelle, qu'il assume lui-même le coût de toute décision déraisonnable. D'autre part, si en raison d'un état psychologique préexistant il est absolument incapable de faire un choix, alors il faut le considérer comme appartenant à la catégorie des victimes vulnérables et ne pas lui en faire supporter les conséquences dès qu'il est prouvé qu'il a été blessé par suite d'un acte fautif.

Je crois que ce qui préoccupait le lord juge Singleton dans l'arrêt *Marcroft v. Scruttons*, précité, tenait au doute qu'il avait quant à savoir si le demandeur, dans cette affaire, était capable de prendre une décision rationnelle. De plus, la preuve médicale portait à croire jusqu'à un certain point que son incapacité pouvait elle-même découler du traumatisme causé par l'accident. Si tel était le cas, il semblerait manifestement injuste de mettre fin au dédommagement à cause de son omission de limiter le préjudice qu'il a subi par une décision rationnelle quant au traitement. Les

tiff's traumatic state after the accident to a pre-existing constitutional weakness and says it rendered the plaintiff incapable of making reasonable decisions. Yet he concluded that this was a subjective factor that could not be considered. This would appear to be carrying the objective test too far in that it overrides the "thin skull" principle altogether.

The position in the United States would appear to be that a great number of personal attributes falling short of a constitutional incapacity to act reasonably can be taken into account in evaluating the plaintiff's post-injury behaviour. This position is best summed up in Dobbs, *Law of Remedies* (1973), p. 580 as follows:

> In such cases the courts have spoken of "the reasonable and prudent man," or "reasonable care" by the plaintiff as a test, but this term is probably too narrow. Personal preferences of the plaintiff, personal finances of the plaintiff and even irrational fears of the plaintiff are given due weight in deciding what he is expected to do to minimize damages. The standard, then, is not so much the objective standard of the hypothetical reasonable man as it is the subjective standard based on what can be reasonably expected of the particular plaintiff.

In their text on *Personal Injury Damages in Canada* (1981) Professors Cooper-Stephenson and Saunders point out that no clear position has emerged from the Canadian jurisprudence in this area although cases such as *Elloway*, *supra*, and *McGrath*, *supra*, suggest that a plaintiff in Canada may not be held to an objective standard of reasonableness which it is beyond his capacity to attain. This position would appear to most appropriately complement Fleming's assertion that where a plaintiff does not suffer from a constitutional incapacity to act reasonably he cannot make the defendant bear the burden of his unreasonable behaviour. Thus, the analytic focus in each case is on the capacity of the plaintiff to make a reasonable choice.

motifs du lord juge Denning sont encore plus déconcertants. Il attribue l'état traumatique dans lequel était le demandeur après l'accident à une faiblesse diathésique préexistante et affirme qu'il a rendu le demandeur incapable de prendre des décisions rationnelles. Il conclut néanmoins qu'il s'agit là d'un facteur subjectif dont on ne peut pas tenir compte. Cela semblerait pousser le critère objectif trop loin en ce que, tout compte fait, il l'emporte sur le principe de la «vulnérabilité de la victime».

La situation aux États-Unis semblerait être qu'un grand nombre de facteurs personnels, sauf l'incapacité diathésique d'agir raisonnablement, peuvent être pris en considération en évaluant la conduite adoptée par le demandeur après avoir subi le préjudice. On trouve le meilleur résumé de cette situation dans Dobbs, *Law of Remedies* (1973), à la p. 580:

> [TRADUCTION] Dans ces cas, les tribunaux ont cité comme critère «l'homme raisonnable et prudent» ou la «prudence raisonnable» de la part du demandeur, mais cette expression est probablement trop restreinte. Les préférences personnelles du demandeur, ses finances personnelles et même ses craintes irrationnelles sont dûment considérées pour décider ce qu'il est censé faire pour minimiser le préjudice subi. Le critère est alors moins le critère objectif de l'homme raisonnable hypothétique que le critère subjectif fondé sur ce à quoi on peut raisonnablement s'attendre du demandeur en question.

Dans leur texte intitulé *Personal Injury Damages in Canada* (1981), les professeurs Cooper-Stephenson et Saunders soulignent qu'il ne se dégage de la jurisprudence canadienne aucune position claire dans ce domaine, bien que des décisions comme *Elloway* et *McGrath*, précitées, laissent entendre qu'au Canada un demandeur ne peut pas être astreint à une norme objective de caractère raisonnable qu'il lui est impossible d'atteindre. Cette position semblerait être celle qui complète le mieux l'affirmation de Fleming selon laquelle, lorsqu'un demandeur ne souffre pas d'une incapacité diathésique d'agir raisonnablement, il ne peut faire supporter au défendeur le fardeau de sa conduite déraisonnable. Ainsi, l'examen porte dans chaque cas sur la capacité du demandeur de faire un choix raisonnable.

(2) Unreasonableness and Conflicting Medical Opinions

Another problem trial judges face in assessing the reasonableness of a plaintiff's decision whether or not to have medical or surgical treatment is the way in which he is expected to handle conflicting medical opinions.

In *Asamera Oil Corp. v. Sea Oil & General Corp.*, [1979] 1 S.C.R. 633, Estey J. stated at p. 649 that "A plaintiff need not take all possible steps to reduce his loss". He is only bound to act like "a reasonable and prudent man": *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London*, [1912] A.C. 673 (H.L.) The steps he takes, Lord Macmillan said in *Banco de Portugal v. Waterlow and Sons, Ltd.*, [1932] A.C. 452, at p. 506, "ought not to be weighed in nice scales".

What guidance, if any, do these very general observations afford an injured plaintiff confronted with conflicting medical advice and varying prognoses for the outcome of treatment? In *Savage v. T. Wallis, Ltd.*, [1966] 1 Lloyd's Rep. 357 (C.A.), the doctors disagreed as to whether a slight operation would get rid of the plaintiff's headaches. It was held that the plaintiff in refusing the surgery had not failed in his duty to mitigate. In *McGrath v. Excelsior Life Insurance Co.*, *supra*, medical opinion was divided as to whether a spinal fusion would reduce the plaintiff's pain. It was held that the plaintiff did not fail in his duty to mitigate by refusing to have the surgery. In *Steele v. Robert George & Co.*, *supra*, Viscount Simon said, at p. 500:

> It may in some cases be quite reasonable for a man to decide not to undergo an operation if his own doctor advises against it, for it is the conclusion reached by his doctor which governs his decision much more than the logic by which his doctor has reached the conclusion.

2) Le caractère déraisonnable et les opinions médicales contradictoires

Un autre problème que les juges rencontrent en évaluant le caractère raisonnable de la décision d'un demandeur de subir ou de ne pas subir un traitement médical ou chirurgical est la manière dont il est censé traiter les opinions médicales contradictoires.

Dans l'arrêt *Asamera Oil Corp. c. Sea Oil & General Corp.*, [1979] 1 R.C.S. 633, le juge Estey affirme, à la p. 649, qu'«Un demandeur n'[est] pas tenu de prendre toutes les mesures possibles pour réduire ses pertes». Il est seulement tenu d'agir comme «un homme prudent et raisonnable»: *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London*, [1912] A.C. 673 (H.L.) Les mesures qu'il prend, d'affirmer lord Macmillan dans *Banco de Portugal v. Waterlow and Sons, Ltd.*, [1932] A.C. 452, à la p. 506, «ne doivent pas être analysées au microscope».

Quel guide ces observations très générales offrent-elles à un demandeur blessé qui fait face à des avis médicaux contradictoires et à des pronostics divergents quant au résultat du traitement? Dans l'arrêt *Savage v. T. Wallis, Ltd.*, [1966] 1 Lloyd's Rep. 357 (C.A.), les médecins ne s'entendaient pas sur la question de savoir si une opération mineure permettrait de guérir le demandeur de ses maux de tête. On a conclu qu'en refusant l'intervention chirurgicale le demandeur n'avait pas manqué à son obligation de limiter le préjudice. Dans l'arrêt *McGrath v. Excelsior Life Insurance Co.*, précité, les médecins divergeaient d'opinion quant à savoir si une fusion vertébrale permettrait de diminuer les douleurs du demandeur. On a conclu que le demandeur n'avait pas manqué à son obligation de limiter le préjudice en refusant de subir l'intervention chirurgicale. Dans l'arrêt *Steele v. Robert George & Co.*, précité, le vicomte Simon affirme, à la p. 500:

> [TRADUCTION] Dans certains cas, il peut être tout à fait raisonnable pour une personne de décider de ne pas subir une opération si son propre médecin ne la recommande pas, parce que c'est la conclusion tirée par son médecin qui influe sur sa décision beaucoup plus que la logique dont a fait preuve son médecin en tirant cette conclusion.

As to the possibility of medical opinions conflicting with that of his own doctor Viscount Simon said, at p. 501:

> that where the workman has been advised against the operation by a skilled medical man in whom he has confidence, it would be necessary to bring home to the workman an extremely strong body of expert advice to the contrary before the onus which rests on the employer of proving that the refusal was unreasonable should be regarded as discharged.

These cases are, however, to be contrasted with cases such as *Marcroft v. Scruttons*, *supra*, and *McAuley v. London Transport Executive*, [1957] 2 Lloyd's Rep. 500 (C.A.), where the refusal of surgery was held to be unjustified. It would appear from the authorities that as long as a plaintiff follows any one of several courses of treatment recommended by the medical advisers he consults he should not be said to have acted unreasonably.

As a qualification to the general principle that a plaintiff's actions must not be subjected to an overly critical standard of review, the English courts have suggested that in determining what steps he ought to take the plaintiff should consider the defendant's interests as well as his own. In *Darbishire v. Warran*, [1963] 1 W.L.R. 1067 (C.A.), the court pointed out that, while the plaintiff may have acted reasonably as far as he was concerned, the true question was whether the plaintiff acted reasonably as between himself and the defendant and in view of his duty to mitigate the damages: *per* Harman L.J., at p. 1072; Pearson L.J., at p. 1076. It should be noted that this rule has never been adopted in Canada, and the English courts in the context of the law of contracts have held that a plaintiff "is not bound to nurse the interests of the contract breaker": *Harlow & Jones, Ltd. v. Panex (International), Ltd.*, [1967] 2 Lloyd's Rep. 509, *per* Roskill J., at p. 530.

In making his finding as to the reasonableness or otherwise of a refusal of medical treatment, the trier of fact will also, of course, take into consideration the degree of risk to the plaintiff from the surgery (*Taylor v. Addems and Addems*, [1932] 1

Quant à la possibilité qu'il y ait des opinions médicales contraires à celle du médecin traitant du demandeur, le vicomte Simon affirme, à la p. 501:

> [TRADUCTION] que lorsque l'ouvrier s'est vu conseiller de ne pas subir l'opération par un médecin qualifié en qui il a confiance, il faudrait soumettre à cet ouvrier un ensemble d'opinions d'expert contraires extrêmement convaincantes pour que l'on puisse considérer que l'employeur a satisfait à l'obligation qui lui incombe de prouver que le refus était déraisonnable.

Toutefois, il faut distinguer ces affaires des arrêts *Marcroft v. Scruttons*, précité, et *McAuley v. London Transport Executive*, [1957] 2 Lloyd's Rep. 500 (C.A.), où on a conclu que le refus de subir l'intervention chirurgicale était injustifié. Il semblerait, d'après la jurisprudence, que dans la mesure où un demandeur suit l'une ou l'autre des différentes formes de traitement recommandées par les médecins qu'il a consultés, on ne puisse pas dire qu'il a agi déraisonnablement.

À titre de restriction au principe général selon lequel les actes du demandeur ne doivent pas être soumis à une norme d'examen trop sévère, les cours anglaises ont laissé entendre qu'en déterminant les mesures qu'il doit prendre le demandeur doit prendre en considération les intérêts du défendeur autant que les siens. Dans l'arrêt *Darbishire v. Warran*, [1963] 1 W.L.R. 1067 (C.A.), la cour souligne que, même si le demandeur peut avoir agi raisonnablement en ce qui le concerne, la question véritable est de savoir si le demandeur a agi raisonnablement par rapport au défendeur et compte tenu de son obligation de limiter le préjudice: le lord juge Harman, à la p. 1072; le lord juge Pearson, à la p. 1076. Il faut souligner que cette règle n'a jamais été suivie au Canada et que, dans le domaine du droit des contrats, les cours anglaises ont conclu que le demandeur [TRADUCTION] «n'est pas tenu de soigner les intérêts de celui qui a rompu le contrat»: *Harlow & Jones, Ltd. v. Panex (International), Ltd.*, [1967] 2 Lloyd's Rep. 509, le juge Roskill, à la p. 530.

En déterminant le caractère raisonnable ou déraisonnable du refus de subir un traitement médical, il va de soi que le juge des faits doit également tenir compte du risque auquel l'intervention chirurgicale expose le demandeur (*Taylor*

the case of tort is clear. The plaintiff is "bound to act not only in his own interests, but in the interests of the party who would have to pay damages, and keep down the damages, so far as it is reasonable and proper, by acting reasonably in the matter" (*Smailes & Sons* v. *Hans Dessen & Co.* ((1905) 94 L.T. 492; on appeal (1906) 95 L.T. 809), per *Channel* J. at p. 493. And as *Mayo* J. said in *Fishlock* v. *Plummer* ([1950] S.A.S.R. 176, at p. 181): "If any part of his (the plaintiff's) damage was sustained by reason of his own negligent or unreasonable behaviour, the plaintiff will not be recouped as to that part." However, "the question what is reasonable for the plaintiff to do in mitigation of damages is not a question of law, but one of fact in the circumstances of each particular case, the burden of proof being upon the defendant" (*Halsbury's Laws of England*, 3rd ed. vol. 11, par. 477, p. 290). The authorities show that once the plaintiff has "made out a prima facie case of damages, actual or prospective, to a given amount", the burden lies upon the defendant to prove circumstances whereby the loss could have been diminished. Not only must the defendant discharge the onus of showing that the plaintiff could have mitigated his loss if he had reacted reasonably, but he must also show how and to what extent that loss could have been minimized (*Roper* v. *Johnson* ((1873) L.R. 8 C.P. 167), per *Grove* J. at p. 184: *Criss* v. *Alexander (No. 2)* ((1928), 28 S.R. (N.S.W.) 587; 45 W.N. 187), per *Street* C.J. at p. 596).

Walters J. then dealt with the defendant's submission that the plaintiff's duty to mitigate in a case of compensation neurosis included a duty to bring on the action for an early trial. He said, at p. 574:

It cannot be disputed that the plaintiff could have taken earlier steps to expedite the trial of the action, but it was equally open to the defendant to have done so, at least by October 1970. Moreover, in the period between April 1970 and June 1970, there had been a delay of two months on the part of the defendant in answering the interrogatories delivered for his examination, and until the answers had been filed, application could not have been made for entry of the action for trial. And it is to be noticed that a summons for leave to enter the action for trial was issued three days following the filing of the answers to the interrogatories. Another matter which I am unable to overlook is the initial delay on the

de limitation du préjudice dans une affaire de quasi-délit est clair. Le demandeur est «tenu d'agir non seulement dans son propre intérêt, mais aussi dans l'intérêt de la partie qui aura à payer des dommages-intérêts, et d'empêcher le préjudice d'augmenter pour autant qu'il est raisonnable et approprié de le faire, en agissant raisonnablement dans les circonstances» (*Smailes & Sons* v. *Hans Dessen & Co.* ((1905), 94 L.T. 492; en appel (1906), 95 L.T. 809), le juge *Channel* à la p. 493. Comme l'affirme le juge *Mayo* dans l'arrêt *Fishlock* v. *Plummer* ([1950] S.A.S.R. 176, à la p. 181): «Si une part quelconque de son préjudice [celui du demandeur] résulte de sa propre conduite fautive ou déraisonnable, le demandeur ne sera pas dédommagé pour cette part.» Toutefois, «la question de savoir ce qui est raisonnable pour le demandeur de faire pour limiter le préjudice n'est pas une question de droit, mais une question de fait selon les circonstances de chaque cas particulier, et il incombe au défendeur d'en faire la preuve» (*Halsbury's Laws of England*, 3rd ed., vol. 11, par. 477, p. 290). Il ressort de la jurisprudence que dès que le demandeur a produit «un commencement de preuve du préjudice présent ou futur, évalué à un certain montant», il incombe au défendeur d'établir les circonstances dans lesquelles les pertes auraient pu être réduites. Non seulement le défendeur doit-il démontrer que le demandeur aurait pu réduire ses pertes s'il avait réagi raisonnablement, mais il doit aussi démontrer comment et dans quelle mesure ces pertes auraient pu être réduites (*Roper* v. *Johnson* ((1873), L.R. 8 C.P. 167), le juge *Grove*, à la p. 184: *Criss* v. *Alexander (No. 2)* ((1928), 28 S.R. (N.S.W.) 587; 45 W.N. 187), le juge en chef *Street*, à la p. 596).

Le juge Walters aborde ensuite la prétention du défendeur que l'obligation du demandeur de limiter le préjudice dans un cas de névrose de transfert obsessif comportait l'obligation d'intenter l'action de manière à hâter la tenue du procès. Il affirme, à la p. 574:

[TRADUCTION] Il est incontestable que le demandeur aurait pu agir plus tôt pour hâter l'instruction de l'action, mais il était aussi loisible au défendeur de le faire au moins depuis octobre 1970. De plus, pendant la période comprise entre avril 1970 et juin 1970, deux mois se sont écoulés avant que le défendeur ne réponde à l'interrogatoire écrit qui lui avait été soumis, et la demande d'inscription de l'action pour audition n'aurait pu être faite avant le dépôt de ces réponses. Il y a lieu de noter que la requête visant à obtenir l'autorisation d'inscrire l'action pour audition a été produite dans les trois jours suivant le dépôt des réponses à l'interrogatoire écrit. Un autre point que je ne puis passer sous silence

rt of the defendant in filing his defence to the statement of claim.

Looking at the conduct of the parties, I am unable to say that any blame lies with one side rather than the other, and I am not persuaded that any mischief done can be solely ascribed to the plaintiff. In any case, apart from the prognosis given in evidence by Mr. Schaeffer, there is not a great deal to show to what extent the plaintiff's neurosis might have been relieved if the action had been brought to trial sooner. I cannot speculate as to the extent to which the plaintiff might have minimized his loss by bringing on his action for an earlier trial. And in all the circumstances, I do not think that the defendant has persuaded me that the plaintiff has been unreasonable in failing to take steps to minimize his damages, or that it has been proved that he is responsible for consequences of his injuries which might have been avoided or materially lessened, so that his damages ought to be calculated at a time prior to the actual date of assessment. It seems to me that after looking to all that has happened, there can be no warrant for abating the award of geneal damages.

n *Plenty v. Argus*, [1975] W.A.R. 155, Jackson C.J. referred to the two aspects of the defendant's burden of proof. He said, at pp. 157-58:

There can be no doubt but that upon this issue the onus was at trial upon the respondent to this appeal and the learned trial Judge so held. In the course of argument before us, however, it did appear that doubt did exist as to what was involved in the discharge of that onus. The question giving rise to that doubt can be posed by asking whether in such a case as this the defendant in order to discharge the onus that the plaintiff had failed to mitigate his damage must prove, on the balance of probabilities, that the plaintiff acted unreasonably in not submitting himself to the advised treatment, and in addition, and to the same standard of persuasion that the treatment, if carried out, would cure, or, to a certain degree cure the plaintiff's condition, or whether on the other hand, the issue to which the onus attaches is but the single issue, it being whether the plaintiff in refusing the treatment had failed to do something which in reason he ought to have done to mitigate his damage. In all the personal injury negligence cases so far reported, it appears to have been established on the balance of abilities both that the plaintiff had acted unreasonand that had the operation been carried out, the incapacity would have been removed or reduced to a

est le fait qu'au départ le défendeur a tardé à produire sa défense à la déclaration.

Considérant la conduite des parties, je suis incapable d'affirmer que l'une est plus blâmable que l'autre, mais je ne suis pas convaincu que tout méfait commis puisse être attribué exclusivement au demandeur. De toute façon, sauf pour le pronostic soumis en preuve par M. Schaeffer, il y a peu de chose qui démontre dans quelle mesure la névrose du demandeur aurait pu être soulagée si l'action avait été instruite plus tôt. Je ne puis spéculer sur la mesure dans laquelle le demandeur aurait pu minimiser le préjudice subi s'il avait fait instruire son action plus tôt. Dans ces circonstances, je ne crois pas que le défendeur m'a convaincu que le demandeur a été déraisonnable en ne prenant pas les mesures nécessaires pour limiter le préjudice subi, ou qu'il a été prouvé qu'il est responsable de certaines conséquences de ses blessures qui auraient pu être évitées ou largement diminuées, de sorte que ses dommages-intérêts auraient dû être calculés à une date antérieure à celle à laquelle ils ont été effectivement évalués. Il me semble, après avoir examiné tout ce qui s'est produit, que rien ne peut justifier une réduction du montant des dommages-intérêts accordés.

Dans l'arrêt *Plenty v. Argus*, [1975] W.A.R. 155, le juge en chef Jackson a mentionné les deux aspects du fardeau de la preuve imposé au défendeur. Il affirme, aux pp. 157 et 158:

[TRADUCTION] Il ne peut y avoir de doute que sur ce point au procès, le fardeau de la preuve incombait à l'intimé au présent appel et c'est ce qu'a conclu le savant juge de première instance. Pendant les plaidoiries en cette cour, il est par contre apparu qu'il y avait un doute quant à ce qu'il fallait faire pour s'acquitter de ce fardeau. La question qui soulève ce doute peut être posée en se demandant si, dans un cas comme celui-ci, le défendeur doit, pour s'acquitter du fardeau de prouver que le demandeur a omis de limiter le préjudice qu'il a subi, prouver, selon la prépondérance des probabilités, que le demandeur a agi de façon déraisonnable en ne subissant pas le traitement recommandé et, selon le même critère de persuasion, que, s'il avait été administré, le traitement aurait permis de guérir le demandeur totalement ou partiellement, ou, d'autre part, si le point qu'il s'agit d'établir se résume uniquement à déterminer si en refusant le traitement le demandeur a omis de faire quelque chose qu'il aurait raisonnablement dû faire pour limiter le préjudice subi. Dans toutes les affaires de blessures corporelles imputables à une faute publiées jusqu'ici, il semble avoir été établi, selon la prépondérance des probabilités, à la fois que le demandeur a agi

certain degree. In such cases the onus is discharged on either view and with the result that damages are assessed "as they would properly have been assessable if he had, in fact, undergone the operation and secured the degree of recovery to be expected from it": McAuley v London Transport Executive [1957] 2 Lloyd's Rep 500 at 505 per Jenkins LJ. [Emphasis added.]

A recent English case which is hard to reconcile with the Canadian and Australian authorities and, indeed, with earlier English authorities, is *Selvanayagam v. University of the West Indies*, [1983] 1 All E.R. 824. In that case the Privy Council held that a plaintiff who rejects a medical recommendation in favour of surgery must, in order to discharge the burden on him to prove that he acted reasonably in regard to his duty to mitigate his damage, prove that his refusal was reasonable. The trial judge had placed the onus on the plaintiff (appellant) and the Court of Appeal had treated this as a basis for review. Lord Scarman said they were wrong. Quoting from his reasons, at p. 827:

> The rule that a plaintiff who rejects a medical recommendation in favour of surgery must show that he acted reasonably is based on the principle that a plaintiff is under a duty to act reasonably so as to mitigate his damage.

While this articulation of the duty to mitigate is obviously correct, Lord Scarman's placing of the burden of proof of mitigation on the plaintiff seems to be in sharp contrast to a long line of earlier English authority and, as has been seen, is contrary to the general principles of mitigation of damages enunciated by this Court in *Red Deer*, *supra*, and *Asamera Oil*, *supra*.

4. The Consequences of an Unreasonable Refusal of Treatment

Turning now to the implication of a finding of unreasonableness for the plaintiff's recovery, it is clear that the so-called "duty to mitigate" derives

de façon déraisonnable et que si l'opération avait eu lieu son incapacité aurait soit diminué soit disparu. Dans ces cas, l'obligation est remplie à l'un et l'autre point de vue de sorte que les dommages-intérêts sont évalués «tout comme on aurait pu les évaluer s'il avait subi l'opération et s'était assuré le degré de guérison qui est censé en découler»: McAuley v London Transport Executive, [1957] 2 Lloyd's Rep. 500, à la p. 505, le lord juge Jenkins. [C'est moi qui souligne.]

L'arrêt *Selvanayagam v. University of the West Indies*, [1983] 1 All E.R. 824, est une décision anglaise récente difficile à concilier avec la jurisprudence canadienne et australienne et même avec la jurisprudence anglaise antérieure. Dans cet arrêt, le Conseil privé a conclu que le demandeur qui refuse de subir une intervention chirurgicale recommandée par les médecins doit, pour s'acquitter du fardeau qui lui incombe de prouver qu'il a agi de façon raisonnable quant à son obligation de limiter le préjudice subi, prouver que son refus était raisonnable. Le juge de première instance avait imposé cette obligation au demandeur (l'appelant) et la Cour d'appel avait considéré cela comme un motif de révision. Lord Scarman a dit qu'elle avait fait erreur. Il affirme ceci dans ses motifs, à la p. 827:

> [TRADUCTION] La règle voulant que le demandeur qui rejette la recommandation des médecins de subir une intervention chirurgicale doit démontrer qu'il a agi de façon raisonnable se fonde sur le principe que le demandeur a l'obligation d'agir raisonnablement de façon à limiter le préjudice.

Bien que cette formulation de l'obligation de limiter le préjudice soit manifestement correcte, l'imposition au demandeur, par lord Scarman, de l'obligation de prouver la limitation du préjudice semble contraster sensiblement avec un long courant de jurisprudence anglaise antérieure et, comme nous l'avons vu, est contraire aux principes généraux de la limitation du préjudice énoncés par cette Cour dans les arrêts *Red Deer* et *Asamera Oil*, précités.

4. Les conséquences du refus déraisonnable de subir un traitement

Pour ce qui est maintenant de l'incidence d'une constatation du caractère déraisonnable du refus sur l'indemnisation du demandeur, il est clair que

from the general proposition that a plaintiff cannot recover from the defendant damages which he himself could have avoided by the taking of reasonable steps. As Pearson L.J. pointed out in *Darbishire v. Warran*, *supra*, it is not a "duty" in the strict sense. A breach of it is not actionable. Quoting from his reasons at p. 1075:

> . . . it is important to appreciate the true nature of the so-called "duty to mitigate the loss" or "duty to minimize the damage." The plaintiff is not under any contractual obligation to adopt the cheaper method: if he wishes to adopt the more expensive method, he is at liberty to do so and by doing so he commits no wrong against the defendant or anyone else. The true meaning is that the plaintiff is not entitled to charge the defendant by way of damages with any greater sum than that which he reasonably needs to expend for the purpose of making good the loss. In short, he is fully entitled to be as extravagant as he pleases but not at the expense of the defendant.

Mitigation has to do with post-accident events. In this respect it should perhaps be contrasted with contributory negligence and perceived as more closely aligned with *novus actus interveniens*. It differs from the latter, however, in that the *novus actus* may be the act of a third party whereas mitigation (or its failure) is exclusively the act of the claimant. Overhanging all three concepts, mitigation, contributory negligence and *novus actus*, are the general principles of foreseeability and remoteness as they apply to post-accident events.

The appellant in the case at bar invoked some of these general doctrines of tort law. He submitted "that the majority in the Court of Appeal have failed to take into account the fact that the plaintiff's unreasonable refusal constituted a *novus actus* and, from the defendant's standpoint, such refusal was not reasonably foreseeable and the damages claimed are too remote". I do not find

ce qu'on appelle «l'obligation de limiter le préjudice» découle du principe général selon lequel un demandeur ne peut se faire indemniser par le défendeur pour le préjudice qu'il aurait pu lui-même éviter en prenant des mesures raisonnables. Comme le souligne le lord juge Pearson dans l'arrêt *Darbishire v. Warran*, précité, il ne s'agit pas d'une «obligation» au sens strict. Le manquement à ce genre d'obligation n'ouvre pas droit à des poursuites. Voici ce qu'il affirme dans ses motifs, à la p. 1075:

> [TRADUCTION] . . . il est important de saisir la vraie nature de ce qu'on appelle «l'obligation de réduire les pertes» ou «l'obligation de limiter le préjudice.» Le demandeur n'a pas d'obligation contractuelle de choisir la méthode la plus économique: s'il souhaite adopter la méthode la plus coûteuse, il a la liberté de le faire et ne commet pas de faute contre le défendeur ou qui que ce soit d'autre en le faisant. Cela signifie en réalité que le demandeur n'a pas le droit de faire payer au défendeur, sous forme de dommages-intérêts, une somme plus considérable que celle dont il a raisonnablement besoin pour réparer la perte subie. En bref, il a tout à fait le droit d'être aussi extravagant qu'il le veut, mais il ne peut le faire aux dépens du défendeur.

La limitation du préjudice se rapporte aux événements survenus après l'accident. À cet égard, il faut peut-être la mettre en contraste avec le concept de la faute de la victime et la percevoir comme se rapprochant davantage du *novus actus interveniens*. Toutefois, elle diffère de ce dernier concept, en ce que le *novus actus* peut être le fait d'un tiers alors que la limitation du préjudice (ou l'omission de limiter le préjudice) est exclusivement le fait du réclamant. Au-dessus de ces trois concepts de limitation du préjudice, de la faute de la victime et du *novus actus*, il y a les principes généraux de la prévisibilité et de l'absence de lien de causalité dans la mesure où ils s'appliquent aux événements postérieurs à l'accident.

En l'espèce, l'appelant a invoqué certains de ces principes généraux de la responsabilité délictuelle. Il a soutenu [TRADUCTION] «que la Cour d'appel à la majorité n'a pas tenu compte du fait que le refus déraisonnable du demandeur constitue un *novus actus*, que pour le défendeur ce refus n'était pas raisonnablement prévisible et que les dommages-intérêts sont réclamés trop indirects». Je ne trouve

such an approach helpful in a case of this kind. It seems to me that by hypothesis the whole of the plaintiff's damages are reasonably foreseeable and would be recoverable were it not for the additional fact that a portion of them was reasonably avoidable by the plaintiff. I have difficulty in seeing how the failure to avoid what is a reasonably avoidable loss can in and of itself make the remaining unavoidable loss unforeseeable. Nor, it seems to me does the doctrine of proximate cause, also invoked by the appellant, elucidate the problem. References to "proximate cause" and "intervening cause", in my opinion, predetermine the legal issue but do not provide a rationale for it. I find the following passage from 22 Am Jur 2d, Damages § 30, at p. 52 more illuminating:

> Other courts have suggested that the doctrine of avoidable consequence is an extension of the proximate cause principle—that is, if the plaintiff could reasonably have avoided the damages which resulted, then the activity of the defendant can no longer be considered the proximate cause of those damages. While this statement can be accepted as theoretically valid (since "proximate cause" probably means nothing more than the cause which is recognized by law as the cause of the damages), it is not precise enough to express the idea contained in the doctrine of avoidable consequences. For example, if defendant's negligent activity caused plaintiff's broken leg and much of plaintiff's pain could have been avoided by consulting a doctor, it is unnecessarily ambiguous to state that the failure to consult a doctor prevented the negligent activity from being the proximate cause of a portion of the pain, but not from being the proximate cause of the rest of the pain. It is more precise to state that consulting a doctor would have avoided a certain portion of the pain and, thus, damages cannot be recovered for the avoidable pain.

Essentially the same point may be made with respect to *novus actus interveniens*. The concept does not advance the analysis in any helpful way. Obviously mitigation and *novus actus* may coincide in cases such as the case at bar but talking in terms of *novus actus* is, in my view, of little assistance in defining the scope of the duty to mitigate.

pas ce point de vue utile dans un cas de ce genre. Il me semble que, hypothétiquement, l'ensemble du préjudice subi par le demandeur est raisonnablement prévisible et serait indemnisable si ce n'était du fait additionnel qu'une partie de ce préjudice aurait pu raisonnablement être évitée par le demandeur. Il m'est difficile de voir comment l'omission d'éviter ce qui constitue une perte raisonnablement évitable peut en soi rendre imprévisibles les autres pertes inévitables. Il ne me semble pas non plus que le principe de la cause immédiate, également invoqué par l'appelant, règle la question. Les mentions de la «cause immédiate» et de la «cause nouvelle» ont pour effet, à mon avis, de prédéterminer la question de droit, mais ils n'en donnent pas la raison d'être. Je trouve plus instructif le passage suivant tiré de 22 Am Jur 2d, Damages, paragraphe 30, à la p. 52:

> [TRADUCTION] D'autres cours ont laissé entendre que la doctrine des conséquences évitables est une extension du principe de la cause immédiate—c'est-à-dire que si le demandeur avait pu raisonnablement éviter le préjudice subi, alors l'activité du défendeur ne peut plus être considérée comme la cause immédiate de ce préjudice. Même si cet énoncé est acceptable du point de vue théorique (puisque «cause immédiate» ne signifie probablement rien de plus que la cause reconnue en droit comme la cause du préjudice), il n'est pas assez précis pour exprimer l'idée contenue dans la doctrine des conséquences évitables. Par exemple, si l'acte fautif du défendeur a causé la fracture d'une jambe du demandeur et que le demandeur aurait pu s'éviter beaucoup de souffrances s'il avait consulté un médecin, il est inutilement ambigu d'affirmer que l'omission de consulter un médecin a empêché l'acte fautif d'être la cause immédiate d'une partie des souffrances, mais non pas d'être la cause immédiate des autres souffrances. Il est plus précis de dire que la consultation d'un médecin aurait permis d'éviter une certaine partie des souffrances et qu'en conséquence il n'est pas possible d'obtenir des dommages-intérêts pour les souffrances évitables.

On peut soutenir essentiellement la même chose en ce qui concerne le *novus actus interveniens*. Ce concept n'apporte absolument rien d'utile à l'analyse. Manifestement, la limitation du préjudice et le *novus actus* peuvent coïncider dans des cas comme celui en l'espèce, mais parler en termes de *novus actus* est à mon avis de peu d'utilité pour définir la portée de l'obligation de limiter le préjudice.

What then counts as an unavoidable loss in a case like this where there has been found to be an unreasonable refusal of surgery? The answer given by MacKinnon A.C.J.O. is that one looks to what would have happened on a balance of probabilities had the operation in fact taken place. The majority approach, on the other hand, is to determine what damages are avoidable by assuming that the plaintiff has agreed to an operation which has not yet been performed. If the majority is correct, then the courts would normally take account of any "substantial possibility" of failure and the amount by which full compensation would be discounted—in this case 70 per cent— would represent his avoidable loss.

There is a paucity of direct authority on this issue. The following passage from the judgment of Jenkins L.J. in *McAuley*, *supra*, at p. 505, may be viewed as support for the approach taken by the majority:

> If he receives medical advice to the effect that an operation will have a 90 per cent. chance of success, and is strongly recommended to undergo the operation and does not do so, then the result must be, I think, that he has acted unreasonably, and that the damages ought to be assessed as they would properly have been assessable if he had, in fact, undergone the operation and secured the degree of recovery to be expected from it. [Emphasis added.]

It seems to me not only to be implicit in the English authorities but also to be common ground between the majority and the dissent in the Court of Appeal in this case that, even after an unreasonable refusal of surgery, the plaintiff is still entitled to claim unavoidable losses assuming, of course, that they are otherwise recoverable. MacKinnon A.C.J.O. would, it is true, deny all subsequent recovery in this case where on the balance of probabilities (70 per cent) surgery would lead to a full recovery, but if there was a 50-100 per cent chance of no more than an 80 per cent recovery at the outside, it seems to me that his approach would necessarily permit a plaintiff to recover the remaining 20 per cent of his damages as unavoidable loss.

Que faut-il considérer comme perte inévitable dans un cas comme celui-ci où on a conclu qu'il y a eu refus déraisonnable de subir l'intervention chirurgicale? Le juge en chef adjoint MacKinnon de l'Ontario a répondu qu'il faut examiner ce qui se serait produit, selon la prépondérance des probabilités, si l'opération avait eu lieu. Selon la majorité, d'autre part, il s'agit de déterminer quel préjudice est évitable en présumant que le demandeur a consenti à subir une opération qui n'a pas encore eu lieu. Si la majorité a raison, les cours devraient donc normalement tenir compte de toute «possibilité réelle» d'échec et le pourcentage dont le plein dédommagement serait diminué—en l'espèce 70 pour 100—représenterait sa perte évitable.

La jurisprudence portant directement sur ce point est rare. On peut considérer que l'extrait suivant des motifs du lord juge Jenkins dans l'arrêt *McAuley*, précité, à la p. 505, étaye le point de vue adopté par la cour à la majorité:

> [TRADUCTION] Si les médecins lui disent que l'opération a 90 pour 100 de chances de réussir, qu'ils l'a lui recommandent fortement et qu'il ne la subit pas, alors il s'ensuit d'après moi qu'il a agi de façon déraisonnable et que les dommages-intérêts devraient être évalués comme on aurait pu les évaluer s'il avait subi l'opération et s'était assuré le degré de guérison qui est censé en découler. [C'est moi qui souligne.]

Il me paraît non seulement implicite dans la jurisprudence anglaise, mais aussi reconnu par le juge dissident et les juges formant la majorité en Cour d'appel en l'espèce, que même après avoir refusé déraisonnablement de subir l'intervention chirurgicale, le demandeur a quand même le droit de réclamer des dommages-intérêts pour les pertes inévitables, en supposant bien sûr qu'il est possible par ailleurs de se faire indemniser pour ces pertes. Il est vrai que le juge en chef adjoint MacKinnon aurait refusé tout autre dédommagement en l'espèce parce que, selon la prépondérance des probabilités (70 pour 100), l'intervention chirurgicale aurait entraîné une guérison complète, mais s'il y avait eu entre 50 et 100 pour 100 de chances de guérison à 80 pour 100 au maximum, il me semble que son point de vue permettrait nécessairement à un demandeur d'obtenir, pour les autres 20 pour 100 du préjudice subi, une indemnité à titre de perte inévitable.

As Blair J.A. points out, support is also to be found for the majority approach in a number of Australian cases, notably *Newell v. Lucas*, [1964-65] N.S.W.R. 1597. In *Plenty v. Argus*, *supra*, Burt J. seems to have adopted it in the following *obiter* statement at p. 159:

> And if a finding is made that a plaintiff in the face of an uncertain prognosis acted unreasonably in not submitting himself to surgery or treatment, then it would seem that his damages should be assessed having regard to his condition as it is, discounted by the evaluation of the lost chance, or as one would if the assessment were made in advance of the carrying out of the advised treatment.

In my view the majority approach is consistent with first principles as expressed by Lord Diplock in *Mallett v. McMonagle*, [1970] A.C. 166, at p. 176:

> The role of the court in making an assessment of damages which depends upon its view as to what will be and what would have been is to be contrasted with its ordinary function in civil actions of determining what was. In determining what did happen in the past a court decides on the balance of probabilities. Anything that is more probable than not it treats as certain. But in assessing damages which depend upon its view as to what will happen in the future or would have happened in the future if something had not happened in the past, the court must make an estimate as to what are the chances that a particular thing will or would have happened and reflect those chances, whether they are more or less than even, in the amount of damages which it awards.

See also Lord Reid in *Davies v. Taylor*, [1972] 3 All E.R. 836 (H.L.), at p. 838. This position is essentially the one adopted by Lacourcière J.A. in *Schrump v. Koot* (1978), 18 O.R. (2d) 337, which Blair J.A. cites in support of his position. MacKinnon A.C.J.O. attempts to distinguish this latter case on the ground that it applies only to assessing the risk or likelihood of future developments but, as the passage from Lord Diplock makes clear, the balance of probabilities test is confined to determining what did in fact happen in the past. In assessing damages the court determines not only

Comme le souligne le juge d'appel Blair, le point de vue de la majorité est étayé par un certain nombre de décisions australiennes dont *Newell v. Lucas*, [1964-65] N.S.W.R. 1597. Dans l'arrêt *Plenty v. Argus*, précité, le juge Burt semble l'avoir adopté dans l'opinion incidente suivante, à la p. 159:

> [TRADUCTION] Et si l'on conclut que, face à un pronostic incertain, le demandeur a agi de façon déraisonnable en ne subissant pas l'intervention chirurgicale ou le traitement, alors il semblerait qu'il faille évaluer ses dommages-intérêts en fonction de son état actuel, mais en les réduisant du montant auquel on évalue l'occasion ratée, ou comme si on faisait l'évaluation avant l'administration du traitement recommandé.

À mon avis, le point de vue de la majorité est compatible avec les principes premiers énoncés par lord Diplock dans l'arrêt *Mallett v. McMonagle*, [1970] A.C. 166, à la p. 176:

> [TRADUCTION] Le rôle que joue la cour lorsqu'elle fait une évaluation des dommages-intérêts qui repose sur sa perception de ce qui va se produire ou de ce qui se serait produit doit être mis en contraste avcec le rôle ordinaire qu'elle joue dans des poursuites civiles et qui consiste à déterminer ce qui s'est produit. En déterminant ce qui est arrivé dans le passé, une cour se fonde sur la prépondérance des probabilités. Ce qui est plus probable que moins probable est tenu pour certain. Mais en faisant une évaluation des dommages-intérêts qui repose sur sa perception de ce qui va se produire dans l'avenir ou de ce qui se serait produit par la suite si quelque chose ne s'était pas produit dans le passé, la cour doit estimer les chances qu'un événement particulier se produise ou celles qu'il se serait produit et traduire ces chances, qu'elles soient plus ou moins égales, dans le montant des dommages-intérêts qu'elle accorde.

Voir également les motifs de lord Reid dans *Davies v. Taylor*, [1972] 3 All E.R. 836 (H.L.), à la p. 838. Cette position est essentiellement celle adoptée par le juge Lacourcière dans l'arrêt *Schrump v. Koot* (1978), 18 O.R. (2d) 337, que le juge Blair cite à l'appui de son point de vue. Le juge en chef adjoint MacKinnon de l'Ontario tente de faire la distinction avec ce dernier arrêt pour le motif qu'il s'applique seulement à l'évaluation du risque ou de la probabilité d'événements futurs, mais, comme il ressort clairement du passage de lord Diplock, le critère de la prépondérance des

what will happen but also what would have happened by estimating the chance of the relevant event occurring, which chance is then to be directly reflected in the amount of damages. The general rule stated by Lord Diplock would therefore seem to be applicable to this case, suggesting that the majority approach is at least *prima facie* correct. The issue then becomes, it seems to me, a question of whether there are any reasons to take this particular type of case outside the general rule.

MacKinnon A.C.J.O. suggests that the majority approach bypasses the trial judge's initial finding of unreasonableness. With respect, I think he must be in error in this since the respondent is precluded by that finding from claiming full compensation for the losses he has already suffered. The same response can be made to the appellant's submission that the uncertainty in the evidence results from the plaintiff's unreasonable conduct and that he ought not to be able to "profit" from it. The finding that his refusal to undergo surgery was unreasonable precludes the plaintiff from recovering his actual loss. To hold that his remaining compensation should be determined on the basis of principles higher than those normally applied in assessing tort damages would, it seems to me, be to punish him for not undergoing surgery. This would be contrary to the general judicial policy that "it is not the prerogative of the court to require that any person undergo surgery to any degree" (*McCarthy v. MacPherson's Estate* (1977), 14 Nfld. & P.E.I.R. 294 (P.E.I.C.A.), at p. 297).

Nor am I swayed by the appellant's submission that a respondent may, because he is free to change his mind about the surgery, effectively be overcompensated. As long as he is *bona fide* in his present claim that he does not intend to have the operation and is not deliberately taking a calculat-

probabilités n'est applicable que pour déterminer ce qui s'est réellement produit dans le passé. Dans son évaluation des dommages-intérêts, la cour détermine non seulement ce qui va se produire, mais encore ce qui se serait produit en évaluant la probabilité de l'événement pertinent, laquelle probabilité doit se refléter directement dans le montant des dommages-intérêts. La règle générale énoncée par lord Diplock semble donc applicable en l'espèce, ce qui laisse entendre que le point de vue de la majorité est juste de prime abord tout au moins. Il s'agit alors, me semble-t-il, de déterminer s'il y a quelque motif de soustraire ce type particulier d'affaire à l'application de la règle générale.

Le juge en chef adjoint MacKinnon laisse entendre que le point de vue de la majorité ne tient pas compte de la constatation initiale du caractère déraisonnable par le juge de première instance. Avec égards, je crois qu'il doit faire erreur sous ce rapport puisque cette constatation empêche l'intimé de réclamer le plein dédommagement pour les pertes qu'il a déjà subies. On peut répondre la même chose à la prétention de l'appelant selon laquelle l'incertitude dans la preuve résulte de la conduite déraisonnable du demandeur et qu'il ne devrait pas être en mesure d'en «profiter». La conclusion que son refus de subir l'intervention chirurgicale est déraisonnable empêche le demandeur d'être dédommagé pour ses pertes réelles. Conclure qu'il y a lieu de fixer le reste de son indemnité en fonction de principes plus stricts que ceux qu'on applique normalement à l'évaluation des dommages-intérêts en matière délictuelle équivaudrait, me semble-t-il, à le punir pour ne pas avoir subi l'intervention chirurgicale. Cela serait contraire à la politique générale des tribunaux selon laquelle [TRADUCTION] «Il n'appartient pas à la cour d'obliger quiconque à se soumettre à la moindre intervention chirurgicale» (*McCarthy v. MacPherson's Estate* (1977), 14 Nfld. & P.E.I.R. 294 (C.A.I.-P.-É.), à la p. 297).

Je ne suis pas non plus influencée par la prétention de l'appelant qu'un intimé, parce qu'il est libre de changer d'avis au sujet de l'intervention chirurgicale, peut vraiment être dédommagé en trop. Pour autant qu'il est de bonne foi en affirmant qu'il n'a pas l'intention de subir l'opération et qu'il

ed risk that he will come out ahead by recovering 30 per cent of his damages now and then later have the surgery with a 70 per cent chance of complete success (an intention which would amount to fraud on the court in any event), there does not seem to me to be any problem arising from the fact that he might change his mind in the future and be overcompensated in the result. The potential for over or under compensation is, it seems to me, a pervasive difficulty with the present "once and for all" method of awarding tort damages. The situation presented by this case is only one example of that more comprehensive problem; it does not, in and of itself, call for a special solution of any sort. It should also be kept in mind that, while it is true that if the respondent does decide to have the operation at some future time there is a 70 per cent chance that he will be somewhat overcompensated, it is also true that there exists a 30 per cent possibility that he will be very substantially undercompensated.

I would respectfully adopt the approach of the majority of the Court of Appeal to this issue.

5. Conclusions

The case law makes it clear that the question of whether a refusal of treatment is reasonable or not is for the trier of fact. Since the respondent (appellant by cross-appeal) did not in the Court of Appeal expressly impugn the objective test applied by the trial judge, the Court of Appeal was correct in refusing to interfere with the trial judge's finding. The respondent cannot be permitted to impugn the objective test for the first time in this Court.

For the reasons given I would dismiss the appeal. Counsel are agreed, however, that Blair J.A. made a mathematical error in his calculations and that the overall figure for damages, instead of being $103,651, should have been $96,146. The dismissal of the appeal is therefore subject to this variation in the Court of Appeal's order.

ne prend pas délibérément un risque calculé de réaliser un profit en obtenant 30 pour 100 de chances de ses dommages-intérêts maintenant pour ensuite subir une intervention chirurgicale comportant 70 pour 100 de réussite complète (intention qui, en tout état de cause, équivaudrait à tromper la cour), il ne me semble y avoir aucun problème découlant du fait qu'il pourrait à l'avenir changer d'avis et en définitive être dédommagé en trop. La possibilité d'être dédommagé en trop ou de ne pas l'être assez constitue, me semble-t-il, une difficulté inhérente à la méthode actuelle qui a cours en matière délictuelle et qui consiste à accorder des dommages-intérêts «une fois pour toutes». La situation qui se présente en l'espèce n'est qu'une illustration de ce problème plus général; elle n'exige pas en soi de solution spéciale. Il faut également se rappeler que, même s'il est vrai que si l'intimé décide de subir l'opération plus tard il y a 70 pour 100 de chances qu'il soit quelque peu dédommagé en trop, il est également vrai qu'il existe 30 pour 100 de possibilités qu'il soit très insuffisamment dédommagé.

Avec égards, je suis d'avis d'adopter le point de vue de la majorité de la Cour d'appel sur ce point.

5. Conclusions

Il ressort clairement de la jurisprudence qu'il appartient au juge des faits de déterminer si le refus de subir un traitement est raisonnable ou déraisonnable. Puisque l'intimé, (l'appelant dans le pourvoi incident) n'a pas, en Cour d'appel, expressément contesté le critère objectif appliqué par le juge de première instance, la Cour d'appel a eu raison de refuser de modifier la conclusion du juge de première instance. On ne peut pas permettre à l'intimé de contester ce critère objectif pour la première fois en cette Cour.

Pour les motifs que j'ai exprimés, je suis d'avis de rejeter le pourvoi. Cependant, les avocats s'accordent pour dire que le juge Blair a commis une erreur de calcul et que la somme totale des dommages-intérêts devrait être de 96 146 $ au lieu de 103 651 $. Le pourvoi est en conséquence rejeté sous réserve de cette modification de l'ordonnance de la Cour d'appel.

I would also dismiss the respondent's cross-appeal which was directed to Blair J.A.'s method of calculation of the appellant's damages. While it is not entirely clear from his reasons how he used the more detailed breakdown of possible results from the surgery to arrive at the second discount of one-third, I do not believe that this kind of determination is susceptible of precise calculation. It would, however, have been of assistance to the respondent on the cross-appeal if Blair J.A. had attempted to relate the percentage predictions of result to the discount.

Leave to appeal was granted in this case in terms that the appellant pay the costs of the appeal on a solicitor-client basis in any event of the cause forthwith after taxation thereof. Costs in the courts below were left to the disposition of this Court.

I cannot accept the submission of counsel for the respondent that the costs of the cross-appeal are covered by the order on the leave application. There is nothing in the order to indicate that a cross-appeal was contemplated although I do not doubt the respondent's right to proceed with one once leave to appeal was granted to the appellant. I would therefore dismiss the cross-appeal with costs. I would not interfere with the disposition of costs in the courts below.

Appeal dismissed and cross-appeal dismissed with costs.

Solicitors for the appellant: Phelan, O'Brien, Shannon & Lawer, Toronto.

Solicitors for the respondent: Morris and Lewis, Toronto.

Je suis aussi d'avis de rejeter le pourvoi incident de l'intimé portant sur la méthode employée par le juge Blair pour calculer les dommages-intérêts de l'appelant. Bien que ses motifs ne montrent pas tout à fait clairement comment il s'est servi de l'état plus détaillé des résultats possibles de l'intervention chirurgicale pour arriver à la deuxième diminution d'un tiers, je ne crois pas que ce genre de détermination se prête à un calcul précis. Il aurait toutefois été utile à l'intimé dans le pourvoi incident si le juge Blair avait tenté d'établir le rapport entre les prévisions de succès en pourcentage et la diminution des dommages-intérêts.

L'autorisation de pourvoi accordée en l'espèce prévoyait que l'appelant paierait les dépens du pourvoi sur la base procureur-client quelle que soit l'issue de la cause, immédiatement après leur taxation. Les dépens dans les cours d'instance inférieure ont été laissés à la décision de cette Cour.

Je ne puis accepter la prétention de l'avocat de l'intimé que l'ordonnance d'autorisation du pourvoi s'applique aux dépens du pourvoi incident. Il n'y a rien dans l'ordonnance qui indique qu'un pourvoi incident était envisagé même si je ne doute pas que l'intimé avait le droit de le former après que l'appelant eut obtenu l'autorisation de se pourvoir. Je suis donc d'avis de rejeter le pourvoi incident avec dépens et de ne pas modifier la répartition des dépens dans les cours d'instance inférieure.

Pourvoi et pourvoi incident rejetés avec dépens.

Procureurs de l'appelant: Phelan, O'Brien, Shannon & Lawer, Toronto.

Procureurs de l'intimé: Morris and Lewis, Toronto.

Newfoundland Supreme Court Trial Division

Citation: Abitibi-Price Inc. v. Voith Hydro Inc. et al.
Date: 1992-12-18
Docket: 1989 No. 1178

Between:
Abitibi-Price Inc. (Plaintiff)
and
Voith Hydro Inc. (First Defendant) and Magnetek National Electrical Coil Inc. (Second Defendant)

Cameron, J.

Counsel:
David B. Orsborn and Augustine F. Bruce, for the plaintiff;
Edward M. Roberts, Q.C., Donald H. Burrage and Glen Noel, for the defendants.

[1] Cameron, J.: The defendants have admitted liability and consented to an order for judgment with damages to be assessed and costs to be taxed.

[2] The outstanding issues are:

1. Quantum of damages;
2. Did the plaintiff contribute to its own injury; and
3. Did the plaintiff fail to mitigate its loss.

Background:

[3] The plaintiff (Abitibi-Price) is the owner and operator of a paper mill at Grand Falls in the Province of Newfoundland. The mill has existed at Grand Falls since the early part of this century. While the plaintiff has not been the owner for all of that time, for the purpose of this action no distinction will be made between Abitibi-Price and prior owners. Nothing turns on this point.

[4] When it was originally constructed the mill and indeed the community of Grand Falls relied on the power produced by the mill. Gradually the plaintiff's need for power increased and it now relies on a combination of

power purchased from Newfoundland and Labrador Hydro and that produced in its own facilities at Grand Falls and elsewhere, though there are still occasions when the plaintiff produces power in excess of its own needs. It may, on such occasions, sell power to Newfoundland and Labrador Hydro or wheel power to another of its mills.

[5] Generator No. 4 is the largest single generator at the Grand Falls mill. Like the other hydrogenerators it is located in the power house, an area which, at present, is exclusively devoted to the generation of power. This action is for damages for loss occurring as a result of a fire in Generator No. 4.

[6] At the risk of oversimplifying, but in the hope that the descriptions which follow will be easier to understand, I shall briefly describe a hydrogenerator. There are two major parts; the turbine and the generator. Water enters the turbine through gates which regulate the rate of flow and thereby the rate of rotation of the turbine. The revolving turbine causes the shaft and the rotor which is attached to the shaft to rotate.

[7] The rotor turns at the centre of the unit and is energized to become, in fact, an electro-magnet. Surrounding the rotor is a stator which does not move. The stator contains copper bars or coils in which the current flows. These coils are connected to each other in a pattern. Ultimately current flowing through the coils travels to the bus rings. Bus rings are conductors which are located on the outer part of the stator. The current passes to the main leads via the bus rings. It was defective brazing of a coil group jumper connector (a short group of copper strands used to join coils) which caused the chain of events which ultimately resulted in the fire in Generator No. 4 on July 2, 1987.

[8] Generator No. 4 has an internal "deluge" system which is activated manually. When the system is activated by connecting a hose and turning a valve, water is sprayed from pipe located inside the generator.

[9] Unlike the other hydrogenerators at Grand Falls, Generator No. 4 has a vertical shaft. Form its installation 1938 to 1986 on two occasions (1954 and 1973) the turbine had to be replaced. On both of those occasions the owner also had the windings and bus rings cleaned and varnish insulation applied.

[10] In 1984 it was determined that once again the turbine was pitted to such an extent that replacement was in order. Proposals were sought from the first defendant for the replacement of the turbine. The plaintiff concluded that in light of the age of the windings and the fact that the generator was to be down for an extended period of time for the replacement of the turbine, it would be an appropriate time to have a rewinding completed as well. However Abitibi-Price did not wish to deal with two contractors and the first defendant (Voith) agreed to subcontract the work for the rewinding to the second defendant (Magnetek) then known as McGraw-Edison Company, National Electric Coil Division. Because of the advances in technology there was an added incentive to have the rewind completed. Abitibi-Price was assured that following the rewind the rated capacity of Generator No. 4 would be increased by 8% using the same water volumes. The rewind was completed between July 1st, 1986 and September 25th, 1986.

[11] Following completion of the rewind Abitibi-Price employees observed that the generator was running at temperatures up to approximately 20 degrees higher than prior to rewind. The plaintiff was assured by the second defendant that this was not a problem because of the increased rating of the insulation used in the rewind.

[12] The incident giving rise to this action, a fire in Generator No. 4, occurred on July 2, 1987. Prior to that time there had never been a fire in Generator No. 4 or any other hydrogenerator at Grand Falls. On one occasion there had been an accidental flooding of Generator No. 4. This occurred in 1949 when a valve linked to the deluge system within the generator was opened and the generator was flooded. The generator was not operating at the time. As a result of this accidental flooding the generator was shut down for four days and went back into operation without any difficulty thereafter.

[13] Because of the admission of liability by the defendants there is no need to examine in detail the cause of the damage, except as it relates to the issue of contributory negligence. Simply put, brazing in the field during the rewinding was substandard and certain work required to be completed under the contract including reinsulation of bus rings was not done. As the result of the defective brazing an arc occurred which started the fire.

Damages:

[14] The parties are agreed that given the damage to Generator No. 4, a complete rewind was necessary. However, the defendants contend that they are not liable for all of the resulting loss to the plaintiff. Rather they allege negligence by the plaintiff in its response to the fire.

[15] I shall first calculate the damages based on the necessity of a complete rewind. Any issue of contributory negligence or mitigation will be examined later.

Special Damages: Repair

[16] The parties were able to agree respecting most of the repair costs. The plaintiff claims $1,318,086 under this heading ($1,335,060 less salvage). For the most part the defendants accept the claim as being the reasonable result of having to do a complete rewind of the generator. However, there are differences between the parties respecting the allocation to this claim by Abitibi-Price of certain costs of their employees. These are $42,507 for Central Engineering and $6,723 for supervision at Grand Falls.

[17] The $42,507 represents, on the evidence of Mr. B. Budgell, salary costs of professionals located at Ontario who devoted part of their time to the repair of fire damage and who, had they not been devoting their time to Generator No. 4, would have been doing other work which would have been generating revenue for Abitibi-Price, or alternatively a temporary assistant could have been laid off sooner. These people habitually kept records of the time devoted to various projects or divisions and the figure of $42,507 was derived from those records. I find that the plaintiff is entitled to and has established on the evidence, its claim for $42,507 as part of its costs for repairing Generator No. 4.

[18] The $6,723 represents allocation of salaries at Grand Falls. The mere fact that the allocation was made at Grand Falls is not sufficient to establish the claim. It is therefore denied.

Replacement Power Cost:

[19] It is agreed that to minimize the damages flowing from the fire, it was appropriate for the plaintiff to purchase sufficient replacement power to enable the mill to continue to operate at maximum output. The parties also agree on the method of calculation of replacement power costs and, with one major exception, the data to be used in the calculation. The parties disagree respecting the amount of power Abitibi-Price would have been able to produce had Generator No. 4 been operating between July 2nd, 1987 and November 13th, 1987, the plaintiff estimating 114,898,000 KWH (kilowatt hours) and the defendants 100,090,000 KWH. (See Consents 36, 45, 46 and 47 for various "scenarios" respecting the potential for generation of power at Grand Falls and the costs of replacement power). The plaintiff claims for replacement of power $3,720,576 (plaintiff's submission, p. 13). The defendants submit $2,521,315 is the proper figure (defendant's submission, p. 46).

[20] Except for the occasional small contribution from generators fuelled by oil, the power produced at the Grand Falls mill is hydro-generated. There are eight hydrogenerators. Numbers 1, 2, and 3 which were designed about 1905 and installed between 1908 and 1911 have rated capacities of 1500 Kw each. Numbers 5, 6, 7 and 8, each have rated capacities of 4000 Kw. Generator No. 4, installed in 1937, since the 1986 rewind has had a rated capacity of 27,000 Kw (29,700 KVA). (Evidence of Mr. Budgell; H.B. #1: Dr. Jolly in PJ #1, pp. 1-2 states the capacity to be 27.6 MW). Units #1-4 produce 50 cycle power and #5-8, 60 cycle power. There is a converter on site to convert 50 cycle power to 60 cycle and vice versa, as required. The mill utilizes both. The source of the water for hydrogeneration is the Exploits River which flows past the mill. The object is to maximize the use of the water available and to minimize spillage (water flowing past the mill but not being utilized).

[21] The quantity of water flowing past the mill is only partially within the control of Abitibi-Price. There is a dam located 60 miles upstream (the Exploits Dam) which is operated by the plaintiff to attempt to regulate the water flow. Using the available knowledge respecting rainfall, snow accumulation and past experience as well as the known production requirements at the mill, Abitibi-Price attempts by the manipulation of gates

at the Exploits Dam to ensure that the water available at Grand Falls is consistent with that required to most efficiently produce the power needed at any one time. However, the regulation by Abitibi-Price of water flow is more art than science. For one thing there are both large and small tributaries, over which the plaintiff has no control, flowing into the Exploits River between the Exploits Dam and the mill.

[22] The process of regulating the water flow by opening or closing gates at the Exploits Dam is one which requires lead time of from 12 hours to in excess of 24 hours, depending on the season. There will be occasions when unforeseen events, for example, a sudden breakdown of a paper machine, will result in much less power than anticipated being required. On such occasions Abitibi-Price may decrease the power purchased from Newfoundland and Labrador Hydro. There is very little storage available in the Grand Falls Millpond and therefore if the water does not go through the penstocks it is often spilled. Spillage might occur if there is a sudden increase in water, e.g., unexpected heavy rainfall. In the spring the levels of water may be so high that even using the Exploits Dam there is no way to limit the amount of water reaching Grand Falls to that required by the mill.

[23] Fortuitously Water Survey Canada maintains a measurement station at Grand Falls. This station is located below the mill and measures the water flowing past the mill as well as that entering the Exploits River from a small stream (Stony Brook) located down river from the mill. In determining the amount of water available to Abitibi-Price the parties agree that the Water Survey Canada figures are the best evidence. However, some adjustments must be made to those figures, the most obvious adjustment being the deduction of the amount flowing into the Exploits River from Stony Brook.

[24] Further, not all water reaching the Grand Falls mill is used for power production. At the mill site there is also a darn (Millpond Dam). On the right of the Mill-pond dam there is a fish ladder. Under an agreement with the Federal Government, Abitibi-Price must, at certain times of the year (roughly May to September), divert to the ladder or the river bed sufficient water to enable salmon to travel up or down river (200 cfs). Also the mill requires some water for other than power production. There were no statistics produced for mill process water. Estimates ranged from 70 cfs (cubic feet per second) to 100 cfs. I accept the evidence of Mr. Budgell and Mr. Cater that 70 cfs was the best estimate for usage in 1987.

[25] On the left side of the river at the Millpond Dam there is as what is described as the "forebay" for the power system. It is from this area that water enters the system for direction to the generators. To enter the forebay the water travels through gates (designed to keep foreign bodies including ice out of the system) into the forebay and then through racks in the forebay to one of three penstocks. Penstocks are large pipes connecting the forebay with the generators. For Generator No. 4 there is a specifically dedicated penstock. The water travels down the penstocks, through the generators and is subsequently released back into the Exploits River above the Water Services Canada measuring site.

[26] The difference between the elevation of the water at the entrance to the forebay and its elevation when it exits the generator (tailwater height) is known as the gross head and, as counsel for the plaintiff so aptly put it, the gross head represents potential energy. The more elevation at the entrance to the forebay the greater the potential energy. It can be seen then that it is to Abitibi-Price's advantage to keep the level of water at the Millpond Dam as high as possible without spillage. Generally speaking the gross heads available to Abitibi-Price at Grand Falls would be between 107 and 109 feet, depending on whether the flash boards were installed on the Millpond Dam.

[27] However, there was not sufficient water available during the whole of the down time following the fire (July 2, 1987 to November 13, 1987) to run the eight generators at Grand Falls at full capacity.

[28] The plaintiff's submission respecting the power which could have been produced was based on an accumulation of data available from different sources respecting each element influencing the production of power. All of these separate pieces of information were then put together to arrive at conversion factors (kw/cfs) for each generator. The conversion factors were in turn used to calculate the power which could have been produced by those generators given the amount of water available. The defendant, with the aid of a computer model developed by the witness, Dr. J.P. Jolly, used a "global" approach to determine efficiency, what counsel for the defendant described as the water in, power out approach.

(i) The Plaintiff's Approach To Calculation Of Power Lost:

[29] Over the years Abitibi-Price has maintained statistics on water flow at

Grand Falls. The figures were calculated with the aid of the output/flow/efficiency curves provided by the manufacturers of the hydro units plus the estimated spillage over the Millpond Dam. However, Water Service Canada figures have been consistently about 25% higher than those recorded by Abitibi-Price. In September of 1989 and in the Spring of 1990 two experiments were conducted by Water Service Canada which led Abitibi-Price to accept that indeed the Water Services Canada figures were more accurate. As a result the parties were in a position to accept the Water Services Canada figures for water flow at Grand Falls in the Summer of 1987. (However, one witness for the plaintiff still expressed some doubt about the accuracy of the Water Service Canada figures in certain weather conditions).

[30] The conclusion that Water Services Canada figures were accurate caused Abitibi-Price in 1990 to revise the conversion factors used by the company to determine the water flow by reference to the power produced by each generating unit. These calculations were not performed for the purpose of this case. Abitibi-Price was at the time considering the feasibility of further power productions on the Exploits River. It was then in Abitibi-Price's interest to be as accurate as reasonably possible in determining the conversion factors.

[31] The evidence of the plaintiff respecting how the conversion factors were calculated and the power which could have been produced was provided primarily by Mr. Bertram Budgell, a professional engineer who has been employed with Abitibi-Price since 1958, much of that time at Grand Falls, Newfoundland.

[32] Clearly the "potential energy" just outside the forebay at the Millpond could not all be utilized in power production. Mr. Budgell identified three areas where losses would occur. Those were: in the route the water takes into and out of the units; in the turbines; and, in the generators. (Here the reader must take care to distinguish between the efficiency of a unit, e.g., Generator No. 4, and the efficiency of the electrical component of a unit, also referred to as the generator). The defendants do not dispute that losses occur in the areas identified by Mr. Budgell but they do dispute the reliability of the data he used and therefore his conclusions.

[33] Mr. Budgell first calculated the loss attributable to each step from

head water to tail water, excluding within the units themselves. These losses are deducted from the gross head to provide the net head.

[34] Mr. Budgell used 96% efficiency for the generating portion of the unit to arrive at a figure for output from the turbine. He then turned to the turbine efficiency curves to determine the cfs necessary to produce that amount of power off the turbine. If one divides the kw off a unit by the cfs used in the turbine one gets the conversion factor which is expressed as kw/cfs. Clearly the cfs required will depend on the net head and the rate power is being taken off. With the same load being taken off a higher head would produce a greater kw/cfs. Any conversion factor produced by the plaintiff in this manner cannot be expected to be precise for any given moment but should fairly reflect the average.

[35] In arriving at a figure for net head Mr. Budgell identified four areas where there was energy loss due to friction, that is, where there is loss of energy in the water because it has to pass through these various areas. For example, for Generator No. 4 the first loss is due to the travelling from outside the forebay to the penstock which involves passing through gates and racks where Mr. Budgell estimated the loss to be 1.3 feet. The loss travelling through the length of the penstock itself he estimated to be 4.5 feet. (There is a commonly accepted formula for determining head loss travelling over a distance). Mr. Budgell allotted a one foot head loss by virtue of the existence of the surge tank, the burp pipe which allows air to be taken into the pipe to prevent buckling of the penstock, and the bend in the penstock. Finally he estimated a loss of .8 feet in the draft tube where the water exits the generator. Similar calculations were performed for other units and penstocks, though of course with different results. All other units receive water from one of two penstocks which are interconnected.

[36] The existence of these friction losses is not disputed by the defendants. However the defendants submit that the plaintiff has not proved the frictional losses, that the evidence of Mr. Budgell respecting frictional losses amounts to hearsay. Mr. Budgell's evidence was based on information he received from both Voith (the first defendant) and another consultant, Acres Consulting International Inc.

[37] In respect of the estimate of 4.5 ft. loss for travelling the penstock for No. 4 Generator, this is based on information received from the original

suppliers and is supported by the work done by Voith in 1984 (see Consent No. 38). In fact, the figure in Consent No. 38 is slightly higher than 4.5. The figure of 1' head loss for the surge tank, burp pipe and bend was obtained from Acres originally but accepted as reasonable by Mr. Roth of Voith, as was the figure of .8 for the draft tube.

[38] In respect of the calculation of losses for the other generators, the figure of 4.7' is used for the penstock. This, of course, is similar to the figure used for No. 4 and closer to that used by Voith in Consent No. 38. The distance to be travelled is similar and as a result I conclude this figure is reasonable. The figure of 2.6' for bifurcation, surge tank, etc., once again was accepted as being reasonable by Mr. Roth after having been supplied by Acres. The minimum loss of 4.7 ft. at the draft tube was supplied by Mr. Roth of Voith to Mr. Budgell and constitutes an admission. Counsel for the defendants has pointed to Mr. Budgell's evidence of the experience of both Abitibi-Price and Voith at Bishops Falls as in support of his submission that there is much lacking in the state of the knowledge about draft tube losses. However, since the source of the best estimates was either Voith itself or confirmed by Voith, the defendants should be held to these figures in the absence of evidence to the contrary.

[39] The figure of 1.3' for losses at the intake to the penstock, which is common to all generators, was described by Mr. Budgell as having come from both Acres and Voith, though in earlier testimony Mr. Budgell seemed less confident of Voith's confirmation. So then the figures for friction losses used by Mr. Budgell were either supported by other admissible evidence or admitted by Voith's agent at some point. This evidence is therefore admissible. The defendants produced no evidence to contradict these figures for friction losses or the evidence that the admissions were made. I accept Mr. Budgell's evidence respecting friction losses.

[40] Parenthetically, an objection to the admissibility of evidence should be raised when the evidence is tendered.

[41] Within the units themselves there are two areas which account for potential energy losses; the turbine, and the electrical component. The parties agree that in respect of the generator efficiency (electrical components as opposed to that of the whole system) an appropriate figure is approximately 96 or 97%. Mr. Budgell used 96% in his calculations. In a

report by Voith to Abitibi respecting Generator No. 4 prior to rehabilitation (Consent No. 38) the author, Mr. Fisher, used 97%. I find 96% to be reasonable.

[42] The turbine turns the shaft which allows mechanical energy to be converted into electrical energy. A turbine's efficiency will vary according to the range of operation. With respect to the efficiency of the turbine of unit No. 4, when performing the calculation Mr. Budgell made use of curves which had been provided to the plaintiff by Voith when submitting its proposal for the replacement of the turbine.

[43] Voith in developing its efficiency curves had used a curve showing head loss which was provided to Voith by Abitibi-Price (see BB #7). However, those curves did not reflect all of the friction losses identified by Mr. Budgell and therefore all of those friction losses were not considered by Voith when they were providing curves for efficiency of Generator No. 4.

[44] On the basis of a factional loss of slightly in excess of 4.6 feet Voith produced for Abitibi-Price two curves showing the cfs utilized for particular levels of output from the turbine at gross heads of 107 and 109 feet. Because the curves which had been provided by Voith were based on the assumptions already stated respecting the lead loss Mr. Budgell produced another curve, the same shape as those which had been provided for 107' and 109' gross head but adjusted for the change in net head. The plaintiff argues that the validity of the curves produced by Mr. Budgell has in no way been lessened. The curves remain the same shape as the ones for 107 and 109 gross head (102.5 and 104.5 net head). The peak efficiency merely moves. The respondent argues that Voith cannot be held to the figures provided in the efficiency curve because there is no evidence to support the view that the curve maintains the same shape when the net head changes.

[45] I accept the efficiency curves for the turbine produced by Voith as being accurate. Prior to installation, changes were made in the design of the turbine to ensure the efficiencies indicated in the curves would be met. The issue then becomes whether the amendments to these curves produced by Mr. Budgell can be relied upon. The most telling support for the curves produced by Mr. Budgell is the fact of the similarity in shape between curves based on net heads of 102.5' and 104.5'. The net head utilized by Mr. Budgell was 100.4'. If the figures for 104.5' net head and 102.5' net head

result in a similar shaped curve, it seems only reasonable that a change of another 2' would not alter completely the shape of the curve but rather it would have a similar shape but in a slightly different location.

[46] I conclude then that the efficiency curve for the turbine, as adjusted by Mr. Budgell, is a reasonable representation of the expected figures and a reasonable inference from the information provided to Abitibi-Price by the first defendant.

[47] At the request of Abitibi-Price, Voith had in February 1990 provided new turbine output curves for Generators No. 5, 6, 7 and 8 on the basis of certain assumed net head figures (95' and 100'). Mr. Budgell drew a curve for 97.5' midway between the curves for 95' and 100'. Of course the friction losses for those generators would be different than for No. 4. However, friction losses for Nos. 1, 2, and 3 which use the same two interlocking penstocks as Nos. 5, 6, 7 and 8 would have a similar figure. Voith is therefore not in a position to dispute the figures generated by the Voith curves for Nos. 5, 6, 7 and 8 at the net heads specified for the curves. No curves were available for Nos. 1-3. However there was information from the manufacturer respecting efficiency which was used to estimate a figure. The 1990 revised conversion factors are for Generators Nos. 1, 2 and 3, 4.83 kilowatts per cfs; for Generator No. 4, 7.5 kilowatts per cfs; and for Generators Nos. 5, 6, 7 and 8, 4.3 kilowatts per cfs.

[48] For calculation of its claim the plaintiff developed new conversion factors based on data available respecting June 1987 which I am satisfied is representative of a normal operating period. A range of conversion factors was developed for different loading patterns and an average determined. Then using the average net heads for July to November a conversion factor was developed for each month. For unit No. 4 the range was from 7.33 to 7.43 kw/cfs; for Nos. 5-8 the range was from 5.13 to 5.57. For unit Nos. 1-3 the figure of 4.83 which had been calculated in 1990 was used. The reason given for no new factors being developed for units Nos. 1-3 was because of the small contribution they make to the claim both because they would be the first to be shut down and because they produce such a small portion of the total power produced.

[49] The factors used for No. 4 are less than the 1990 factor. For Nos. 5-8 they are higher than the 4.3 used in the 1990 figure. If one examines the

basis of the 4.3 factor it can be seen that it is based on taking 393,600 kwh off Nos. 5-8 in 24 hours (25,100 more kwh than the highest figure hypothetically taken off for the calculation of the claim). In other words 4.13 or perhaps less than that figure could be expected if operating at that level. But greater efficiency can be gained by operating at lower than maximum levels and this is reflected in the calculations for June 1967. However the figures in the claim do not represent maximum efficiency at the net heads applicable for the period Generator No. 4 was not operating.

[50] In determining the power which could be produced from the water available as measured by Water Services Canada the plaintiff deducted 200 cfs for the salmon ladder and 135 cfs for other factors such as mill production and the outflow from Stony Brook. I accept these figures as being, reasonable averages for the Summer of 1987. (On the basis of Appendix F of PJ No. 2 and Dr. Jolly's ratio of flow in Great Rattling Brook to Stony Brook 65 cfs for Stony Brook would be an over estimation for July, August and September and an under estimate for October and November).

[51] When a point was reached where there was insufficient water, by these calculations, to run all generators the order of deemed shutdown was that commonly used by Abitibi-Price with No. 4 being the last to be shut down.

(ii) The Defendants' Approach:

[52] The defendants' submission respecting replacement power is based on an analysis completed by Dr. J.P. Jolly, an expert in the fields of hydrology, hydraulics, stream gauging and hydrometric analysis of river flow. Dr. Jolly was not qualified to give evidence respecting generator design or efficiency. His approach has the attraction of being simplistic. He concedes this was the first time he used it and he had not seen it used elsewhere.

[53] In his calculations of gross efficiencies, Dr. Jolly relied on the records of Water Services Canada for the flow in the Exploits River. He then made a deduction for the flow from Stony Brook to arrive at the volume of water available to the Mill. To calculate gross efficiencies Dr. Jolly ignored figures for mill use and the salmon ladder, where applicable, on the basis that the volumes were so small as not to materially affect the outcome. If one accepts 70 cfs as a reasonable figure for mill use I find that applying Dr. Jolly's

method of calculation (P.J. #4) to Appendix E, Table 1 of P.J. #2 (the data used to calculate the gross efficiency of Generator No. 4) the deduction of 70 cfs from that available for power production results in increases in gross efficiency rates of up to 1.9%.

[54] Abitibi-Price records were used to determine gross heads and spillage over the dam. When those records reflected no spillage Dr. Jolly assumed for the purpose of the calculations contained in his report that there was in fact none.

[55] There are no measurements of flows in Stony Brook. There are measurements for Great Rattling Brook, a neighbouring tributary which flows into the Exploits River down stream from Stony Brook. To arrive at a figure for the flow from Stony Brook, Dr. Jolly prorated the figure for flow in Great Rattling Brook at the ratio of the drainage areas for each of the streams, that of Stony Brook being the smaller. The measured flows on the Exploits were not considered to be a good comparable because the Exploits is in part a regulated river. I accept that the Exploits River would have been a poor comparable.

[56] Dr. Jolly's first task was to determine the gross efficiency of unit No. 4. He examined the Abitibi-Price records to find days on which only Generator No. 4 was operating. He was able to locate 18 such days. Of the 18 days, all but four days in March 1987 were eliminated for various reasons. For example, six days were eliminated because there had been spillage recorded and Dr. Jolly doubted the reliability of the figures respecting spillage. Using the available water as determined from the Water Services Canada data adjusted for Stony Brook and the energy produced as calculated from the hourly readings noted by Abitibi-Price documents, the gross efficiency of the unit for each of the four days was calculated and then plotted on a graph. The curve produced reflected gross efficiencies at loadings from 11.8 to 22.2 megawatts. Dr. Jolly concluded that 69%, which happens to be the efficiency calculated on March 21st, 1987 when the loading was 22.2 megawatts, was the maximum gross efficiency for Generator No. 4. This assumes that after 22.2 megawatts the "curve" becomes a horizontal line. (The data provided by Voith for turbine efficiency would suggest the curve should go higher and then slope downward).

[57] Dr. Jolly then chose a number of days in which only unit No. 4 and

units 5 to 8 were operating. The total number of days chosen was 27. Of those, all but four in January 1986 were eliminated. Dr. Jolly then determined the efficiency of the ensemble (5-8 & 4) on the basis of those four days and from the result, assuming the maximum gross efficiency of No. 4 to be 69%, calculated the efficiency of units 5 to 8. The assumption was made that the efficiencies for units 5 to 8 would be the same for each unit and less than No. 4.1 find this assumption to be reasonable for the purpose of performing the required calculations.

[58] The third step was to determine the efficiencies of the ensembles composed of units 1 to 3 and 5 to 8. In this case 22 days were chosen when those units alone were operating and the same process as noted above was used to determine the efficiencies of the two ensembles together and by mathematical calculation the efficiency of units 1 to 3. Here it was assumed that the efficiency of Nos. 1 to 3 would be less than Nos. 5 to 8.1 accept that assumption as being reasonable. The assumption that the efficiency of Nos. 1-3 is less than Nos. 5-8 which is less than No. 4 is consistent with the plaintiff's position respecting the efficiencies of these units.

[59] Efficiency curves were also developed for units 1-3 and 5-8. However, here Dr. Jolly assumed that the curves for ensembles 1-3 and 5-8 would have the same shape as the curve for unit 4 adjusted, of course, for the facts that the capacities of the units and the maximum efficiencies were different.

[60] Maximum gross efficiency of all eight units was then calculated using data when all units were operating. Dr. Jolly chose dates after the 1986 rewind and prior to the fire. Since what was to be determined was what could have been produced had the fire not occurred and the rewind was to result in a change in the rated capacity it was appropriate to discard prerewind data, though this might cause one to question the validity of the data used to determine the gross efficiency of ensemble 5-8 since the statistics used to determine the gross efficiency of No. 4 and No. 5-8 combined come from three days in January 1986. (I was not convinced that PJ. No. 14 answered this question). Dr. Jolly also excluded dates after the fire. A review of Appendix D, Table 4 in P.J. #2, shows dramatic variations in gross efficiency in 1989 and 1990 when gross efficiency figures went, by Dr. Jolly's calculations, as high as 96% (December 1989), well above what would be possible according to Dr. Jolly's conclusion. These figures could not be

explained by the work done on the second rewind. It could only effect the efficiency of the electrical component, which the parties agree was 96 to 97% prior to the fire. Another difficulty I have with this portion of Dr. Jolly's report can be found on pp. 3-12 (P.J. #1) where he says:

> "To determine the maximum gross efficiency when all units were operating (i.e., plant capacity) data for twenty-seven days were considered. These are given in Table 4 of the Appendix D. Since the maximum gross efficiency of unit #4 has been established to be .69 and the maximum efficiency of unit ensemble #4, #5-8 to be approximately 0.63 and that of unit ensemble #1-3, #5-8 to be 0.52, data for dates when the calculated gross efficiencies were higher than 0.69 were withdrawn from further consideration."

It is obvious then that if the material was inconsistent with the initial determination respecting Generator No. 4 it was eliminated. Dr. Jolly's conclusions could do nothing but support the earlier determinations and assumptions.

[61] Dr. Jolly described two different checks on his results for gross, efficiencies; the daily continuity check, and the monthly check. Dr. Jolly was willing to concede that the daily check was directed primarily towards combinations 1 to 3 and 5 to 8 as it proceeded on the premise that 69% efficiency for No. 4 was correct.

[62] Dr. Jolly also took comfort respecting his conclusions for units 5-8 and 1-3 from the actual productions at Grand Falls during the Summer of 1987 when No. 4 was being repaired, which he found to be consistent with his findings. However, the parties were relatively close on their views of the efficiencies of units 1-3 and 5-8. It is the disagreement in opinion respecting unit No. 4, which produces such a large proportion of the power, that accounts for most of the discrepancy in the estimates of power which could have been produced had unit No. 4 been operating in the Summer of 1987.

[63] The monthly flow test was a comparison of the Water Services of Canada figures for water flow in the Exploits River for seven months in 1986 and 1987 (adjusted for Stony Brook) and the water passing through the turbines as calculated using the percentage for gross efficiency determined by Dr. Jolly plus the spillage as noted on Abitibi-Price records, though on pp.

2-5 of his report Dr. Jolly had concluded spillage flows were "grossly underestimated". In evidence Dr. Jolly stated that on average spillage was understated. He believed any errors which might be present in the figure for one day would be less if monthly statistics were used, the errors would even out over time. On the evidence of Mr. Cater and Mr. Budgell it appears that except for a possible error in measurement, which is calculated on the basis of water depth near the Millpond Dam, it is highly unlikely that spillage would be underestimated. This is particularly evident under Winter conditions when portions of the flash boards may give way or when due to ice conditions there may be lifting of the boards and leakage below the top of the dam. From this monthly comparison Dr. Jolly concluded the efficiencies calculated were accurate at higher loadings, less so as the loadings dropped off.

[64] The monthly flow continuity chart, as originally presented showed percentage differences between Dr. Jolly's calculated efficiency and the seven months chosen ranged from -10.7 to +5.4. Dr. Jolly took comfort from the fact that there were three negative and four positive numbers which he said supported the validity of his conclusions respecting gross efficiency.

[65] During cross-examination Dr. Jolly performed the calculations to produce three other charts using the same seven months. However in these three cases he used calculated spillage figures rather than "actual" (which were in fact calculated by the plaintiff). Table X-A represents the same analysis as described above using Dr. Jolly's calculated spillages. Tables X-B & X-C represent the data when the spillage curves are forced to "come in under certain assumptions". Table X-A resulted in percentage differences from Dr. Jolly's figures of -9.6 to +7.6 with six of the seven comparisons being on the plus side. Tables X-B and X-C resulted in a better distribution of the negative and positive percentage differences and, for that reason, Dr. Jolly viewed the results as being more reliable, though it seems to me that this is once again rejecting the results which do not agree with the original conclusion rather than questioning whether the original conclusion was valid.

[66] When this approach was used but substituting Abitibi-Price's conversion factors to arrive at the available water, the results were all negative, indicating to Dr. Jolly that the "Abitibi-Price" calculations are based on higher than actual gross efficiency.

[67] To determine the amount of power which could have been produced

from the water available in the Summer of 1987 the curves produced for No. 4 and the ensembles were utilized. Dr. Jolly assumed No. 4 unit would be loaded first and brought to maximum load. This would be followed by the next most efficient ensemble, Nos. 5-8, and finally by ensemble 1-3. This is consistent with the historical pattern of use. In these calculations lower than maximum values for efficiency were used if less than maximum load was hypothetically being used. The calculations were performed with the aid of a computer model produced by Dr. Jolly. One potential difficulty arising from the use of the computer program is that it did not utilize the curve which resulted from the original calculations by Dr. Jolly but a series of straight lines. Dr. Jolly opined, in cross-examination, that this would result in less than 1% error in the result.

[68] Having determined the gross efficiencies for the various combinations of units a number of scenarios were developed using different load combinations. Dr. Jolly chose scenario number 2 as best representing the historical pattern used by Abitibi-Price and it is this scenario which is the foundation of the defendants' submissions.

[69] By examining the history of power generation for the 8 units, Dr. Jolly determined the maximum capacity for production by these units over a 24 hour period. These maximums are higher than the rated capacity but the records of Abitibi-Price indicate that it would not be unusual for a particular generator to be run at its maximum capacity. Having determined the maximum capacity, Dr. Jolly then compared this to the actual figures for the month of June 1987 to arrive at what he described as a utilization factor of .96. In June the actual use of the generation capacity at Grand Falls was .96 of the maximum capacity of those units. The utilization factor was then applied to his findings respecting the power which could have been produced between July 2 and November 13, 1987 at maximum load.

[70] In cross-examination Dr. Jolly agreed that his utilization factor is predicated on the assumption that if the Generators are down or run at less than maximum, the water continues to go through the penstocks (or presumably over the dam as spillage). He was prepared to agree that if this assumption is wrong then his figures for potential power generation are out by 4%.

[71] It do not accept the basis for the application of the utilization factor,

particularly in times of low water. Dr. Jolly has not established that the system is so finely tuned that reduction of power taken off from maximum to something less results in spillage. An examination of Consent No. 23 (Power Logs) brings me to the conclusion that had No. 4 been operating it is unlikely there would have been any spillage from the last week of August to the end of October and minimal spillage for the balance of the relevant period. The more likely scenario is that the power taken off in June was less than maximum because of the unavailability of water to maintain peak production over long periods of time or even more likely, because the maximum production does not represent the most efficient use of water, the highest turbine efficiency being at less than maximum use.

[72] Counsel for the defendants argues that Table XV of Dr. Jolly's report is a comparison of the actual energy produced in June 1987 (as recorded by Abitibi-Price) and the amount which could have been produced as calculated by Dr. Jolly, the latter being 4% higher than the former. He cites this as support for the accuracy of Dr. Jolly's opinion respecting gross efficiencies. With respect, I conclude this is not a correct interpretation of the evidence. The evidence of Dr. Jolly was that the "Shawmont" figure in Table XV represents not the amount derived using Dr. Jolly's gross efficiency calculations but a calculation, once again using Abitibi-Price data, of the amount which could have been produced if all units operated at maximum capacity. The amount actually produced in June 1987 was 96% of the maximum. This comparison became the basis of the utilization factor discussed above.

[73] In performing his calculations, Dr. Jolly made four assumptions (See P.J. #7). These are:

1. The gross efficiency of all the units within a group are the same;
2. Mill process water rates are small;
3. Great Rattling Brook portrays the Stony Brook flows on the same day; and
4. Each unit has similar gross efficiency versus load characteristics.

[74] Of course, the first assumption would have no effect on the calculations respecting unit No. 4. I have found it to be a reasonable assumption for the purpose of these calculations, though in practice one

would not expect all generators in any one group to perform with exactly the same efficiency.

[75] I agree that in the context of the amount of water used at Grand Falls the mill process rates are low. However, I have already noted the impact on gross efficiency rates of deducting 70 cfs from the available water.

[76] Dr. Jolly chose to compare Stony Brook to great Rattling Brook because they have neighbouring drainage basins and on the assumption the topography would be similar. Great Rattling Brook is the larger of the two. The assumption is that the ratio of drainage basins equals the ratio of water flow in the tributaries. Dr. Jolly conceded that the assumption could not be relied upon in flood conditions, during Spring runoff, in storm conditions or when Great Rattling Brook water flow is greater than 20% of the flow in the Exploits River.

[77] As to the fourth assumption the defendants provided no evidence to support the assumption that each unit had similar gross efficiency versus load characteristics. The area was by Dr. Jolly's own admission outside his area of expertise.

[78] While being cross-examined, Dr. Jolly produced in P.J. #13 a reworked curve for efficiency for unit 4 based on use of the meter showing 24 hour output readings rather than the hourly readings he had used in the calculations used in P.J. No. 1. I am satisfied that in this case the more accurate readings are the 24 hour readings, which represent totals for the period, although Dr. Jolly states that in general in his work they assume the hourly readings are more accurate. Dr. Jolly was willing to agree that if the 24 hour figures were more accurate, then the efficiency of Generator No. 4 would be closer to 71% than 69%. He did not do the calculations to determine how this would follow through with the other units and I am therefore not in a position to determine whether this change would be similarly reflected in other units or whether the total efficiency would be the same.

[79] The gross efficiency for No. 4 Generator was determined by reference to four dates in March. While I understand Dr. Jolly's reluctance to use other days when the validity of the conclusion might be doubted because of questionable data, I find the use by Dr. Jolly of such a small sample

undermines my confidence in his results. Dr. Jolly himself indicated that he would have preferred to have 10 in his sample. Dr. Jolly had no difficulty with the fact that all samples were in March. However, the records demonstrate that Grand Falls experience both Winter and Spring temperatures during that month. The dates chosen by Dr. Jolly were March 9, 13, 19 and 21, 1987. A reference to the Grand Falls Climatological Station report (G.C. #1) shows that on the 9th and 13th temperatures were below zero (-21.5° on the 13th) and snow depth was 60 cm. However, by mid-March temperatures were above zero and several days of rain followed. The hydro power log for March 19th notes "losing loads on #4 gen at times because of ice in wheel". By March 21st the depth of the snow was 32 cm. Clearly Spring arrived at Grand Falls.

[80] If Dr. Jolly's assumptions about the relationship between Great Rattling Brook and Stony Brook are valid the increase in flow in Great Rattling Brook from the 19th to the 21st (7.6 cms to 26 cms) would indicate Spring runoff was also beginning at Stony Brook but Dr. Jolly has also noted that the comparison of the two streams is unreliable during Spring runoff.

[81] Since the data for March 21, 1987 established for Dr. Jolly the peak efficiency rating the change in weather before that date leads me to conclude that I can place less weight on the March 21 data. Further when explaining why he chose to exclude March 22, 1987 (because Great Rattling Brook was in flood), Dr. Jolly conceded that an error of 150 cfs in the flow rates in Stony Brook could result in a 3% difference in the gross efficiency rates of Generator No. 4.

[82] The dates used by Abitibi-Price to determine the conversion factor were only five, once again a small sample. However these have the advantage of being in June 1987, under conditions similar to those which prevailed during the down time and without the concerns that arise during run off. The method chosen by the plaintiff also has the advantage of not being influenced by spillage figures which both parties agree are unreliable.

[83] Dr. Jolly was given the production figures and gross heads for September 24, 25 & 26, 1989. When the cfs necessary to produce the energy was calculated using Dr. Jolly's gross efficiency method the water required was in excess of that in the river while the Abitibi-Price method of calculation produced results within an acceptable range of the measured

water. Dr. Jolly, except to state the dates used were for 1989 when there would be no reasons to expect increased efficiency, gave no explanation for the discrepancy.

Conclusion Respecting Power Loss

[84] When faced with the approach used by Mr. Budgell and that used by Dr. Jolly I am persuaded that the approach used by Mr. Budgell probably produces the more reliable estimate of the power which could have been produced. Mr. Budgell's approach is the traditional one, accepted by the industry. Much of the data which formed the basis of the claim was provided by or acknowledged by Voith. The method used by Dr. Jolly, as has been noted, had the disadvantage of being susceptible to error as a result of relatively small errors in water flow either as spillage or in the flow in Great Rattling Brook/Stony Brook.

[85] I find that in the absence of contributory negligence or failure to mitigate the plaintiff has established the cost of replacement of power of $3,720,576.

Mitigation And Contributory Negligence:

[86] In *Red Deer College v. Michaels,* [1976] 2 S.C.R. 324; 5 N.R. 99; 57 D.L.R.(3d) 386, at p. 390 D.L.R., Chief Justice Laskin stated in respect of mitigation:

> "The primary rule in breach of contract cases, that a wronged plaintiff is entitled to be put in as good position as he would have been in if there had been proper performance by the defendant, is subject to the qualification that the defendant cannot be called upon to pay for avoidable losses which would result in an increase in the quantum of damages payable to the plaintiff. The reference in the case law to a 'duty' to mitigate should be understood in this sense.
>
> "In short, a wrong plaintiff is entitled to recover damages for the losses he has suffered but the extent of those losses may depend upon whether he has taken reasonable steps to avoid their unreasonable accumulation."

[87] The burden of proving that the plaintiff failed in its duty to mitigate lies on the defendants. The question of what constitutes reasonable mitigation and what steps the plaintiff was required to take are questions of fact which depend upon the circumstances of each case.

[88] The alternate argument which has been raised by the defendants is an allegation of contributory negligence on the part of the plaintiff. I shall leave aside the issue of whether contributory negligence can be applied to apportion liability in contract cases since the action against the defendant who has raised contributory negligence is framed in contract, except to note that in *Wells Construction Limited v. Thomas Fuller Construction Co. (1958)* (1986), 61 Nfld. & P.E.I.R. 91; 185 A.P.R. 91; 22 C.L.R. 144 (Nfld. S.C.), the court applied the Contributory Negligence Act to a claim in contract. The second defendant against whom the action is framed in negligence did not raise contributory negligence.

[89] Under legal theory, it is quite easy to distinguish between contributory negligence and mitigation. In practice the line may not be so easily drawn. Contributory negligence arises when a loss occurs because of two or more causes. In this case the allegation is that one cause was an act or omission of the plaintiff. In contributory negligence the actions giving rise to the loss occur prior to or at the time of the loss. The theory of contributory negligence is that those who are responsible for the loss bear their proportion of the liability.

[90] In their arguments neither the plaintiff nor the defendants were concerned with the distinction between mitigation and contributory negligence except as to its impact on the method of calculation of damages. This attitude was based on the view that under either heading the task of the defendants was the same and the principles to be applied were the same.

[91] The duty to mitigate arises after the breach or wrongful act and after the plaintiff becomes aware that the defendants wrongful acts have caused a loss. In this case the defendants argue the plaintiff failed to respond properly to the fire and it failed to properly train its employees so that they could do so. I conclude the issue raised is properly one of mitigation. We are concerned with what the plaintiff did after the breach by the defendants.

[92] The argument of the defendants that the fire brigade was not

properly trained, which will be discussed later, is not relevant to the issue of mitigation where the question is whether the plaintiff took reasonable steps to avoid an unreasonable accumulation of damages except the response of a properly trained fire brigade is relevant in a determination of whether the response of Abitibi-Price was reasonable.

[93] The issue of what steps should have been taken can be reduced, quite simply, to at what point should the deluge system have been activated. If the defendants establish the deluge system should have been utilized earlier they must also prove that action would have reduced the damages.

[94] Counsel for the plaintiff put the position correctly when he submitted that a finding of failure to mitigate does not deprive the plaintiff of all damages. The result is merely to reduce the award by an amount which reflects the likelihood that the mitigating action would have succeeded. In this case if it was unreasonable for the plaintiff to have waited as long as it did to activate the deluge system but reasonable action would have while perhaps lessening the amount of damage still left the plaintiff in a position where it would have required a rewind there would be no lessening of damages.

[95] Having concluded there is no issue of contributory negligence I would add that had I approached the issue from that perspective the outcome would not have been different.

The Incident As Observed From Outside Generator No. 4

[96] The incident giving rise to this action occurred over approximately 55 minutes early on the morning of July 2, 1987. At 12:05 there was only the operator, Michael Lawlor, and the assistant operator, Winston Ellsworth, in the power house. Mr. Lawlor was at the operator's room on the mezzanine level and Mr. Ellsworth on the floor below near Generator No. 1. Both gentlemen were occupied with the Generator No. 1 which they were attempting to put on line. Both heard a loud bang. Mr. Lawlor's instrument panel told him the location of the problem and which differential relay had tripped. Mr. Lawlor advised Mr. Ellsworth and they went immediately to Generator No. 4.

[97] I pause here to explain that Generator No. 4 is several storey's high

and portions of it can be observed from the mezzanine level or the operating floor level (one below) or from the pit (one below operating floor). A photograph of Generator No. 4 is reproduced in Schedule A. At the mezzanine level, which is located about the level of the stairs leading onto the generator at the right of the picture, one can see the plates covering the top of the windings and the upper portion of the generator. At the operating floor level one can easily observe the two rows of square ventilation holes which are located around the exterior of the larger part of Generator No. 4.

[98] Mr. Ellsworth and Mr. Lawlor met at the mezzanine level where they observed smoke and sparks (or as Mr. Ellsworth described it flankers) coming from the vents on the side of the generator. Mr. Lawlor directed Mr. Ellsworth to put the brakes on, that is stop the generator from rotating, while Mr. Lawlor called in the alarm. At this time the rotor was revolving well in excess of the operating level of 120 rpm. Mr. Ellsworth started the exhaust fans to clear the smoke from the generator room and descended by ladder to the operating floor to follow directions. The gates controlling the water flowing into the turbine had to be closed by the operator from the mezzanine floor. Mr. Ellsworth states that he had to wait for this to be completed, about one minute, before the brakes could be applied. The process of braking takes some time though Mr. Ellsworth concedes he did not follow the normal procedure in this case and believes it took about three minutes for the brakes to go on. His recollection is that by the time members of the Mill's fire brigade had arrived the rotation had stopped but he believes that Mr. Gill, the Electrical Superintendent, and Mr. Daye the Fire Chief, arrived before the rotation had stopped.

[99] It was Mr. Lawlor's view that the firemen came about five to ten minutes after the incident started. Both Mr. Lawlor and Mr. Ellsworth were aware of the existence of the deluge system in Generator No. 4. Indeed Mr. Lawlor raised the use of the system with Mr. Gill when Mr. Gill arrived. Mr. Gill determined that no water should be applied at that time. On the arrival of the fire department the operator and the assistant operator directed their attention to keeping the mill in operation while the fire brigade dealt with the problem at Generator No. 4.

[100] As it happened, because of another unrelated incident which occurred earlier in the day, there were more senior management on site than might be expected at that hour. When the alarm, which is in fact the whistle,

sounded both Donald Butler, Production Superintendent, and David Gill were on site. They went to the incident together arriving, by Mr. Gill's estimation, about five minutes after the sounding of the alarm. I should note that while they were on the mill complex the power house, a separate building, is some distance from the office in which Mr. Gill and Mr. Butler were located when the whistle sounded. The estimates of five minutes from alarm, or five to ten minutes from the trip by Mr. Lawlor and Mr. Ellsworth are reasonable for the distance to be travelled. Both Mr. Gill and Mr. Butler observed smoke coming from the doors as they approached the power house and both noted the odour of burning insulation. The fire chief, Art Daye arrived shortly after Mr. Gill and Mr. Butler. Mr. Daye's report noted he arrived at the scene at 12:12 a.m.

[101] When Mr. Gill and Mr. Butler saw generator No. 4, both noted smoke emitting from the square ventilation holes around the circumference of the generator and from the top out of the centre. Mr. Gill also noted blistering on a top plate. Mr. Gill and Mr. Butler differ as to whether or not the generator was rotating at the time of their arrival. I find it is probable it was rotating. Mr. Daye believed it was spinning when he arrived at 12:12 a.m.

[102] Mr. Gill set about checking if the breaker had tripped, if the field breaker was off and the governor closed. He did this personally and says it took him about five minutes to do so and to walk around the generator. He found no evidence of heat on the side opposite the area where the blistering was observed though subsequent investigations would conclude that was where the fire started. By that time the rotation had stopped. The order was given to have the breaker racked out which by Mr. Gill's estimation took another five to ten minutes. He believed that this step was necessary to ensure the safety of persons fighting the fire, although at that point he was not prepared to concede that a fire was what they were dealing with.

[103] By this time it was approximately 12:25. During the next 30 to 35 minutes CO2 and other chemicals were applied by the firefighters through the vent holes and when one of the deck plates warped the firefighters attempted to raise the plate further and insert chemicals through the opening. Mr. Gill states emphatically that he never saw any flame or glow though he concedes he did see ember on wood. Both Mr. Gill and Mr. Butler agree that in the 15 to 20 minutes immediately preceding 1:00 o'clock the discoloration and blistering on the top of the plates was getting worse and a decision was

made by Mr. Cater, the senior person on site at the time, to use the deluge system. The deluge system was applied approximately 1:00 a.m. and by 1:15 the "fire" was declared to be out.

[104] The issue raised by defence is not whether or not the decision made by the fire chief and management of Abitibi-Price on July 2, 1987 was correct but whether it was reasonable. When they arrived on site Mr. Butler and Mr. Gill, both of whom were aware of the deluge system, agreed that it should not, at that stage, be used. Mr. Gill, as I have noted, advised Mr. Lawlor of that fact. Mr. Butler told the fire chief, Mr. Daye, that no water should be applied to the generator and instructed that he use fire extinguishers with CO2. As it transpired, Mr. Daye, the Fire Chief, was not aware of the deluge system although some of his men were, having been advised of that fact by Mr. Daye's predecessor.

[105] Mr. Gill, advised the court of his reasoning respecting the inadvisability of using the deluge system immediately upon his arrival at Generator No. 4. Mr. Gill proceeded on the basis that they were dealing with an electrical fault. He believed the area of scorching to be the site of the electrical fault. Because of prior experience with other types of motors including a 12,000 horsepower motor, Mr. Gill thought that if water were applied to the generator it would certainly result in a rewind and lengthy downtime. He cited the absence of flame (I am satisfied there was no flame visible when Mr. Gill arrived) and the fact that the RTS's were reading 90 degrees when he arrived as factors which would support his belief that there was no fire. He stated, and I find, that it was not unusual to have the odour of burning insulation and smoke in machinery in the absence of flame. Further, it was his belief that there was little within the generator to support a flame in any event. In this, he relied on the belief that the rewind which had been contracted was completed as contracted and that as a result the old bus ring insulation (Class B) had been replaced by Class F. insulation. In fact, it had not been replaced. Mr. Butler's thoughts respecting the use of the deluge system were consistent with those of Mr. Gill.

[106] The concerns expressed by Abitibi-Price personnel are echoed to some extent by the material contained in H.B. No. 20, the submission of the British Columbia Hydro and Power Authority to the I.E.E.E. working group on hydro plant controls. It states that one should not utilize the deluge system unless absolutely necessary and notes the cost of cleanup, etc. It described

the deluge system as a last ditch stand "to prevent burning up the unit". Further, it notes that "most internal faults will not result in a fire unless operating history was to attempt repetitive reenergization due to faulty flags or improper inspection following a trip operation, or the unit was excessively dirty or otherwise contaminated by combustibles present on the windings (assuming use of essentially noncombustible winding insulation materials)".

[107] The defendants argue that there is no basis for the expressed concern of some of the plaintiff's witnesses who believed the application of the deluge system might result in greater damage to Generator No. 4 or under certain conditions endanger firefighters.

[108] The defendants submit there is no support for the view that either difficulties with drying coils or thermal shock might result. Mr. Butler and Mr. Gill both referred to a 12,000 hp. motor which had to be rewound after water from a cooling line was sprayed onto the motor. I do hot agree with defence counsel's characterization of 12,000 hp. as a small motor. Its rated capacity (11,600 kva) is slightly in excess of *IA* the capacity of Generator No. 4. The Loss Report (DG#1) noted there was "insulation failure due to thermal shocking by near freezing water which sprayed onto the motor windings". The motor had been manufactured in 1974.

[109] Of course Generator No. 4 had itself been flooded, without damage, on an earlier occasion but it had not been operating at the time. Mr. Erhard was of the opinion that there would be no risk to windings as a result of the application of water from the deluge system. I find the express concerns to be reasonable in light of the experience of those working at Grand Falls.

[110] The racking out of the breakers was part of the safety procedures in force in the plant. I accept Dr. Erhard's evidence that it was not necessary in this case. No doubt it was wise.

[111] Mr. George (Tommy) Cater was the senior engineer responsible for the power house at the time of the incident. He had worked at the Grand Falls mill for approximately 40 years. He, too, agreed that the deluge system should not be applied immediately. It was only after Mr. Cater saw that the blistering of the paint on the top of the generator was worsening and spreading around the generator that he, with the fact that there was oil stored at the top of the generator in mind, decided that the deluge system should be

applied. At this point, the security of the building became a factor.

[112] I have no hesitation in concluding on the evidence of Messrs. Gill, Butler and Cater that they honestly believed, at the time, that they were taking the appropriate action, and further, that their experience led them naturally to this belief. Should they have known better.

[113] The defendants argue that Abitibi-Price fire brigade did not meet industry standards in training and the decisions made by senior management persons during the event were not reasonable when viewed in light of what those individuals should reasonably have been expected to know because of their positions or in light of industry standards for training.

The Fire Brigade:

[114] The Abitibi-Price fire brigade is a voluntary organization though members are paid for attendance at fires if the fire occurs when they are not on shift. It is made up of individuals who work in different areas of the Mill. Members are recruited from different trades so that there will be persons present who are familiar with each area and type of machinery which might be involved in any particular incident. The fire equipment man who maintained fire protection equipment at the Mill was also a member of the fire brigade. At the time of the incident, the fire chief, who was also the head of security, was employed in part to act as fire chief and could be regarded as a professional firefighter. As one might expect the organization was hierarchical.

[115] On the evidence of one witness there might be as many as 50 fires per year, most around paper machines. The fire brigade for the community of Grand Falls would not respond to a fire at the mill unless asked to do so.

[116] The defendants called Mr. Luke Morrison, an instructor with Professional Loss Control, to give evidence respecting industry standard for the training of fire brigades. He was qualified as an expert in organization, training, equipping and response for industrial fire brigades. In fact, the Fire Chief, Mr. Daye had attended one of Mr. Morrison's training programs. Mr. Morrison was also qualified as an expert in cause, development growth and spread of fire.

[117] Mr. Morrison stated that practice bulletin No. 600 of the National Fire Protection Association (see A.D. No. 1) was an appropriate standard by which to judge the Abitibi-Price brigade. He opined that a brigade which had no training and no preplan and no knowledge of the fire protection system would not meet the NFPA Standard No. 600. The fire chief, Art Daye, agreed that NFPA standard was that of the industry. Training sessions as specified by the NFPA standard were scheduled. However, it is clear the schedule was not always met. Some but not all of the members called had attended training sessions in the power house. While Mr. Morrison was critical at what he interpreted as a lack of planning and training on the part of the fire brigade at Grand Falls, he did not state how that lack of training was evident in the behaviour of the firefighters during the incident except to note that it would have been much easier to utilize the deluge system and that raising the plate increased the amount of flame under that plate. Mr. Morrison agreed that the action taken in any situation might vary with the priorities of the person taking the action, e.g., protection of human safety, protection of a physical structure or protection of certain equipment. In a plant one would expect that after human safety, priority to be given to what is vital to production.

[118] It is clear that Mr. Art Daye and the deputy chief were not aware of the deluge system. However, had he known it would not have made a difference to Mr. Daye's conduct on the night in question because, as he stated it, he always took the advice of the people familiar with the equipment when dealing with equipment fires. That is he would have taken Mr. Butler's advice, or direction, about the matter of the use of water even if he had been aware of the deluge system. Other members of the brigade who were aware of the deluge system were vague about the method of activating it. However I am unable to conclude that this lack of knowledge, in the circumstances of this case, in any way influenced what occurred on July 2, 1987. The operator and the assistant operator as well as the senior management on site that evening knew of the deluge system. A decision was made by management officials of Abitibi-Price not to use the deluge system. Mr. Daye was specifically instructed not to apply water. There is nothing in the evidence to indicate that the system was not used because of lack of knowledge of its existence or that when it was used there was further delay because of lack of knowledge how to operate the system. The raising of the plate will be examined later.

[119] What also seems clear is that the methods chosen to fight the fire, that is the application of CO2 through the vents and the gap in the plate did not, and could not, given the design of Generator No. 4, have reached the fire. The only benefit which could have been obtained was the cooling down of some plates.

[120] Mr. Morrison was critical of the fact that senior management made decisions which should have been made by those whose responsibility it was to fight the fire. Once again it seems to me it is not who made the decision but whether it was a reasonable one.

The Deluge System:

[121] It is clear from the evidence of Mr. Lawlor and Mr. Ellsworth that they knew of the deluge system and how it operated. It is equally clear that there were at Grand Falls no written instructions on the operation of the deluge system or when it might be appropriate to utilize that system. Mr. Brian McGrath, an electrical engineer and former President of Churchill Falls (Labrador) Corporation conducted, for the defendants, a survey of the fire protection systems existing in a number of utilities in Newfoundland and Labrador. One of the utilities examined was that of the Deer Lake Power Co. Ltd. at Deer Lake, which was originally established to supply power to a paper mill at Corner Brook. The deluge systems at Deer Lake are manually operated. The evidence of Mr. McGrath would indicate that prior to February 11th, 1988 there were no written instructions to the operator at Deer Lake on the use of the deluge system. The instructions issued on that date states:

> "This fire protection system floods the stator winding and is to be operated if it is certain that the stator winding is on fire." (B.M.G. No. 2)

[122] Mr. McGrath found that Newfoundland Light & Power Co. Ltd., has no fire protection system on its generating units.

[123] The Newfoundland and Labrador Hydro units utilized automatic deluge systems, at least where the systems are located at remote sites. However, at Bay d'Espoir there is a manual system. There is also an operator's manual. It indicates that in the event of fire the system should be turned on. There is however, a warning that before the sprinkler system is activated the operator should ensure "the Unit is de-energized and that the

D.C. is taken off the Unit. By placing on the ground switch, this will dissipate any residual charge left in the Unit".

[124] Mr. McGrath was also able to speak to the situation at Churchill Falls. The units at Churchill Falls which are much newer and much larger than those at Grand Falls, have an automatically activated deluge system. Mr. McGrath described three incidents where a deluge system was used at Churchill Falls. In all cases there had been phase to phase faults and in all but one occasion total rewinds of the. affected generator were carried out but there were also other factors contributing to the need for a rewind. On one occasion there was only a partial rewind. However, on the evidence, it is clear that replacement of coils is easier at Churchill Falls because of the configuration of the coils. (On the evidence of Mr. Erhard in order to replace one coil in Generator No. 4 it would be necessary to move 50 to 70 coils).

[125] Mr. Ralph Erhard, a designer of generators, was clearly of the view that the appropriate system of fire protection was an automatic deluge system. Indeed he believed they should operate whenever there was a fault whether a fire resulted or not. However, he conceded that it is the customer's decision whether an automatic or manual, or indeed any system is installed. Mr. Erhard's view was that any manual system should be turned on immediately.

[126] Mr. Luke Morrison referred, in his evidence, to the NFPA Recommended Practice for Fire Protection for Hydroelectric Generating Plants (see A.D. No. 2) which had been issued June 10, 1987 to come into effect June 30, 1987. This document acknowledges that there was, at the time, no uniform operating procedures for generating plants. Among the recommendations included in the N.F.P.A. document was that for the protection of generator windings, there be a deluge system using either gas or water. No recommendation is given to install automatic rather than manual water spray systems, (p. 851-15)

[127] Mr. Helmut Brosz presented the court with a number of guides for fire protection systems. These were provided by Mr. Brosz without comment as he acknowledged this was outside his area of expertise. These guides included the Ontario Hydro Rotating Machine Manual (H.B. No. 21), the I.E.E.E. Guide for Operation and Maintenance of Hydro-Generators (H.B. No. 19), the British Columbia Hydro and Power Authority Practices as of 1980

(H.B. No. 20), I.E.E.E. Guide for Small Hydroelectric Projects (January 20, 1982) (H.B. No. 22) and other information concerning large projects (H.B. No. 23, 24 and 25).

[128] On reviewing all of the evidence respecting deluge systems I find that there was, in 1987, no industry standard that all generators have automatically activated deluge systems, nor was there a standard instruction respecting the activation of a manual system.

Inside Generator No. 4:

[129] The premise upon which the argument of the defendants respecting mitigation is made is that the incident commenced with an arc which within seconds caused the alarm to sound and that had the deluge system been activated within, say seven minutes of the trip, the damage which would have resulted to generator No. 4 would have been much less serious and could have been repaired without the necessity of a complete rewind (defendant's brief, p. 73). If this premise is accepted the downtime and therefore the amount of power which would have been purchased would also be much less than that claimed.

[130] At trial, both parties presented opinion evidence respecting the spread of the fire and the amount of damage which would have occurred at several stages along the way.

[131] To assist the reader in understanding the evidence respecting the fire I shall describe the portion of the generator involved. As has been noted the stator is the stationary portion of the generator. It is circular with the rotor placed in the "hole" in the middle. In the case of Generator No. 4, there are in the stator 390 slots into which 390 coils are placed. In the 1986 rewind each coil was connected to the next by a series of jumpers, short pieces containing one grouping of 16 strands located outside and above the slots. Aside from via these jumpers the coils do not touch. However, there is a rather tedious procedure whereby the coils are eased into place because in this circle of overlapping coils there is always one coil under a portion of one neighbouring coil and over a portion of another.

[132] Each coil has three groups, each comprised of 16 strands, of copper.

Each strand of copper is surrounded by strand insulation composed of fused daglas. Each group (or turn) is surrounded by insulation composed of glass/polyester matte backed mica tape. Around the three groups there are also further types of insulation comprised of polyester matte backed mica tape and glass tape in corona shielding which is then impregnated with a resin. For the coils themselves, this impregnation is done in the shop by immersing the coils in the resin. Finally corona shielding paint is applied. In, the stator, the major part of the coil is within an iron frame in which the slots are located and a small portion of each coil is outside the frame, top and bottom. At the top, one group of 16 strands are exposed at each side of the coil for the purpose of making the connections with the jumpers.

[133] Metal sleeves were used to hold a group of 16 strands from a coil to the 16 strands from a jumper and the two were brazed. When the brazing was complete the insulation of this portion was completed in the field and the resin applied.

[134] Mr. Morrison was not employed for the purpose of examining the incident at Generator No. 4 until September of 1991. As is obvious, he therefore did not examine the Generator following the fire. In forming his opinion, he relied on descriptions given by witnesses, photographs of the damage to Generator No. 4, reports prepared for the parties or their insurers, and Power House logs. Mr. Morrison accepted the conclusion of others that the fire began at the site of the arc near the neutral lead. He believed the energy from the fault ignited the insulating paint on the end windings and perhaps the bus rings and with the assistance of the rotation of the rotor the fire spread in a counter-clockwise direction around the stator to the area near the main lead within the first five minutes. Certainly the existence of the blistering paint on the plate at the time Mr. Daye and Mr. Gill arrived would support the view that by that time (somewhere between 12:10 and 12:12) and before the rotation stopped the fire was well-established at the site of the main lead. It was Mr. Morrison's view that after the rotation stopped the fire could travel both clockwise and counter-clockwise, Mr. Brosz held a similar view about the direction of travel of the fire after rotation ceased. However, Mr. Morrison proceeded on the belief that the scorching started after the rotor stopped. On the evidence, this is not the case, though I am satisfied before the rotor stopped the scorching was confined to one relatively small area. It was after the rotor stopped that it spread and one of the plates lifted.

[135] Mr. Morrison concluded that, except near the fault the fire did not damage anything other than the paint on the surface of the insulation of the end windings and the bus rings and surfaces of wood blocks. He opined that the temperature inside the generator never exceeded 200°C (that would have been reached about five minutes after the rotor stopped), although in his report he had stated the maximum temperature was 400°C. On this basis he opined that there was no burning of insulation.

[136] By determining how much combustible material was inside the upper portion of Generator No. 4, the ignition temperature (temperature at which the materials were self-supporting in combustion) for each of these items and the heat of combustion (heat released during combustion) Mr. Morrison calculated the maximum temperature likely to be felt inside the Generator if there was total combustion. He then adjusted to take into account the area which saw no burning, inefficiency of burning inside the generator and the fact that the wood blocks (½ the fuel) were not totally consumed. He estimated the amount consumed based on photographs. Next he calculated heat losses. An example would be heat to increase the temperature of the steel. Having completed his calculations he concluded the insulation would not have seen temperatures above 200°C except for the time the flame may be consuming the paint on the insulation and therefore the insulation would not have become involved in burning. In arriving at the amount of heat released Mr. Morrison was concerned only with the fire. He did not include anything for the heat released by the arc, nor did he include the insulation in his list of combustibles as he was trying to determine if there was sufficient heat to involve the insulation.

[137] Later in his evidence when it was pointed out to him that he had omitted in his calculation of the combustible material the ties and spacer blocks (780) between the coils, Mr. Morrison conceded that perhaps his figure for average temperature should be 220°C. However, the figure of 220° was arrived at without the knowledge of mass and heat of combustion that had been necessary for the initial calculation.

[138] Mr. Morrison stated that in order to burn, the paint had to reach a temperature of 400°C (the ignition temperature). He conceded that for the period of time the flame was consuming the paint on the exterior layer of tape that tape was somewhere between 200°C and 400°C. He opined that when the flame passed the temperature dropped to the average of around 200°C.

He also acknowledged that flame temperature could reach as high as 1000°C. However, using the analogy of passing ones hand through a flame without burning it, Mr. Morrison opined that the energy being generated by the burning paint was being dissipated so quickly that the insulation was not involved.

[139] He concluded that had the fire been extinguished within the first 10 minutes, apart from the area near the main leads (and presumably the area of the fault), the only repairs which would have been necessary would have been to repaint the bus rings and end windings. He went so far as to state there had been no insulation damage after 55 minutes of fire, a conclusion that is not supported by the physical evidence. Further, the report prepared for the first defendant by, among others, Mr. Erhard, notes that there were places where the bright red paint was still evident though the insulation underneath and disintegrated (R.E. #1, p. 4).

[140] Mr. Morrison conceded that he was not an expert in insulation and he was not in a position to give an opinion respecting the effect of either heat or flame on the insulation used in Generator No. 4. He agreed that the melting point of polyester was approximately 250°C and its ignition would be approximately 450°C.

[141] Mr. Morrison reasoned that the heavier damage near the main leads was in fact caused by additional oxygen being made available to the fire after the firemen raised the cover plate. Of course, it was only after the plate had warped, probably because of the heat generated by burning material, and an opening of about ½ to 1 inch appeared firemen got the idea of raising that plate further to facilitate the application of CO2 to what they assumed was the site of the fire. In fact the height of the opening was increased by the firemen only to about 1½ to 2 inches at the centre of a distance of about 18 to 24 inches. While the firemen were attempting to lift the plate they discovered two or three bolts had broken off in the plate.

[142] As to the area around the fault Mr. Morrison concluded that accepting Mr. Brosz's calculation of the energy released initially (14,400 kw cycles or 227.5 BTU's) the maximum area of ignition would have been a radius of 17.3 in. (about l/10th of the area Mr. Brosz believed would be damaged by the arc).

[143] Mr. Helmut G. Brosz was qualified as an expert in failure analysis of electrical equipment, damage assessment, and propagation of fire. He is a professional engineer and described himself as a forensic and testing engineer.

[144] The incident occurred July 2, 1987. Mr. Brosz was contacted by the insurers for Abitibi-Price that same day. He travelled to Grand Falls on the 5th of July to inspect and photograph what was then visible. Mr. Brosz visited Grand Falls on a number of other occasions and one or two of his colleagues remained on the scene while the generator was being dismantled.

[145] On examination of the physical evidence, Mr. Brosz concluded, and this is not disputed, that there were several occurrences of poor brazing in the work completed by the second defendant.

[146] At trial, Mr. Brosz advanced two theories of what occurred within Generator No. 4. The first theory advanced by Mr. Brosz, one subsequently abandoned by the plaintiff, was that there was sufficient damage to the coils prior to the fire to require a complete rewind. This theory had not formed part of Mr. Brosz's report but was developed after he had submitted his report. In arriving at his first theory, Mr. Brosz noted the increase in operating temperature which had concerned Abitibi-Price immediately after the rewind in 1986 and that no heat sinks had been used in the brazing in 1986. These factors coupled with Mr. Brosz's view that the failure had occurred after all of the current had been carried by one single strand which caused temperatures to reach the point that the copper melted led Mr. Brosz to suggest Generator No. 4 was damaged beyond repair -before the Generator tripped because the coils had been exposed to temperatures high enough to damage the insulation.

[147] In light of the fact that the plaintiffs have abandoned this particular theory, there is no need to examine it in detail. However, I feel compelled to note that in fact the evidence does not support the view that no heat sinks were used when the brazing was being done in 1986. Mr. Brosz described a heat sink as a clamp. One is placed on either side of the area being brazed. The purpose is to divert heat from the brazing process, which utilizes flame in excess of 700°C, to the clamps and to prevent the heat travelling down the coils to damage coil insulation. On the evidence I am satisfied that other types of heat sinks are habitually used in the industry and are acceptable.

Wet asbestos, an acceptable form of heat sink, was wrapped around the copper strands on either side of the brazing and placed underneath the brazing activity on the evidence of Mr. Boone, who completed some of the brazing. This is supported by a photograph taken at the time of the 1986 rewind. I should note that Mr. Boone was also of the view that the poor brazing, which is admitted, was done on another shift than the one he worked and there is no evidence respecting the use of heat sinks on that shift.

[148] In respect of the increase in operating temperatures, evidence subsequently revealed that this occurred because of an error in the positioning of the transposition in the coil. (A transposition is, in fact, just a twist). On the evidence of Mr. Pelletier, it is clear that this change in transposition could cause an increase in temperature in the range experienced after the 1986 rewind of Generator No. 4. It is certainly more probable that the increase in temperature was due to this error in placement of the transposition rather than because of the effect of the defective brazing of jumpers.

[149] The insulation which had been used for the coils in the 1986 rewind was Class F and on the basis of the information provided the extra 20° did not result in the insulation being exposed to temperatures outside those recommended for that class.

[150] As stated, Mr. Brosz advanced the view that because one single strand of copper was carrying all of the current it melted and an arc developed. Under this theory, the heat in the area of the failure would have reached temperatures which would have ignited the insulation long before the melting of the copper. However, the evidence does not support the view that even if one strand were carrying all of the current the temperatures would be such that the melting point of copper would be attained. It is clear then that in respect of the issue of damage to Generator No. 4 we must be concerned with what occurred seconds before, during and after Generator No. 4 tripped off at 12:05 a.m. and not with events which might have occurred prior to that time. The defendants argue that the many weaknesses of Mr. Brosz's first theory should indicate that I cannot place any weight on his second theory.

[151] The second theory of Mr. Brosz, the one on which the plaintiff now

relies, is in fact a continuation of the first. However it can stand independent of the first. The second theory is that when jumper (C-47-48) opened circuited, that is when a space developed between copper from the coil and the copper in the jumper, and there was no longer a copper pathway for the current to follow an arc occurred (an in phase arc). Mr. Brosz estimates that this arc would have lasted approximately five seconds. During this time, there would have been burning of insulation and, indeed, melting of copper at the site of the arc and copper vapour would have been produced. As the copper melts the distance the current must travel in air becomes wider and wider. Eventually the arc jumped from C47-48 to another jumper (a phase to phase arc). When the phase to phase arc occurred, the differential relay would have sensed the fault and tripped, that is taking the generator off line through the activation of a circuit breaker. Mr. Brosz opined that once the arc ceased no more copper vapour was produced but prior to that the fire was already in progress. In the observations made at the scene after the fire, Mr. Brosz noted no coil damage within the slots or at the bottom end of the coil. Fire damage was observed on the upper part of the coil above and at the core laminations. At p. 12 of his report, Mr. Brosz concluded that the heat from the arc and the radiation associated with arcing temperatures in excess of 5,000°C damaged all coils, semi-conducting coil, gradient paints, ring bust insulation, ring bust group jumpers and coil jumpers over an arc of about 130° from slot 13 through to slot 272. In respect of the utilization of the deluge at that stage, he concludes:

> "If deluge water had been applied at this time, the generator would require a dry out. Such dry out might not be successful and would cause additional damage to sections of the generator not otherwise damaged at this time."

Mr. Brosz also concludes that in the first 10 minutes the fire extended to what he described as fire zone two burning paints on coils, group jumpers and coil jumpers over an arc of about 185° in a counter-clockwise direction from slot 360 to slot 138. This means that under Mr. Brosz's theory by that time, before rotation had stopped, about 265 coils were involved and he concludes:

> "A total rewind is necessary at this point since the burnt and scorched insulation of the coils cannot be repaired in the field."

[152] There is clearly a marked difference in the views of Mr. Brosz and

Mr. Morrison respecting the damage to the generator in the first 10 minutes though they generally agree on how the fire progressed.

[153] It is agreed by all parties that after the fire was extinguished the damage was so great as to require a complete rewind.

[154] Mr. Ralph Erhard was qualified as an expert in design, construction, operation, maintenance and repair of large salient pole apparatus. Mr. Erhard has degrees in both electrical and mechanical engineering and worked for Westinghouse from 1942 to 1981. The Grand Falls generator is a salient pole apparatus, the type in which Mr. Erhard has his expertise. From the beginning, it was clear that Mr. Erhard was not claiming expertise in fire nor in the progress of fire. To that extent then, much of his evidence respecting the damage to the, generator was based on a straight line arithmetical assumption, an assumption that is not supported by the evidence of either Mr. Morrison or Mr. Brosz both of whom described rapid spread of the fire in a counter-clockwise direction during the first minutes, before rotation stopped and slow progress in both directions thereafter.

[155] Mr. Erhard was prepared to agree that there would have been damage to the insulation on coils near the arc both from the exposure to flame and from thermal radiation. Mr. Erhard was not in a position to quantify the extent of this damage.

[156] In respect of the ability to repair damage in the field it was Mr. Erhard's view that if there were damage to coils within 4" of the stator core, repairs in the field would not be possible. Mr. Boone, who would have had to perform such repairs in his work, indicated that it would not be possible below the shoulder or bend in the coil to perform repairs in the field.

[157] Mr. Erhard indicated he might recommend repairs be made in the field if there were a small number of coils but if such were the circumstances he would seek an extended warranty.

[158] It was Mr. Erhard's view that if 16 mils of insulation had been degraded he might repair one or two coils in the field but if one were dealing with 10 or more he would have to question the economics of doing it in that manner. Mr. Erhard had agreed that even if no fire had occurred it would be necessary to replace all of the jumpers because of the defective brazing.

[159] As stated earlier the issue raised by the defendants is whether the plaintiff acted reasonably to protect itself and if it did not have the defendants established that the lessening of damage would mean a rewind was not necessary.

[160] The weight of the evidence is that immediate application of the deluge system was not required by the industry standard or the facts known to Abitibi-Price employees at the time.

[161] Counsel for the defendants submit (p. 40 of brief) that the operator would have turned on the deluge as soon as possible. I found Mr. Lawlor's evidence to be qualified. He stated he would need to know for sure there was a fire and he would await until rotation had stopped and he had made sure everything was off.

[162] I conclude that the events of the first 10 minutes were necessary to access the situation. No one other than Mr. Erhard would have used the deluge system immediately. I further conclude that it was reasonable to treat the situation as a fault until it became clear it was a fire, which would have been up to 25-30 minutes before activation of the deluge system. Both Mr. Gill and Mr. Butler noted initial diminution of smoke when CO2 was first applied.

[163] However the defendants have failed to establish that an earlier application of the deluge system would have prevented the necessity of a rewind.

[164] Mr. Morrison acknowledges there would have been burned insulation from the arc within a radius of 17½ in. If burning occurred within this area damage from thermal radiation and melting copper carried by the wind would have resulted in a greater area. The fire had clearly spread almost halfway around the Generator within the first five to seven minutes. The blistering paint indicates it was, within that time, well-established at the main leads. Mr. Morrison's conclusion that there would be no damage to the insulation if the paint were not burned is contradicted by the evidence of Mr. Erhard. His belief that the glass tape would have acted as a barrier to protect the insulation was undermined by the fact that it was impregnated with resin. His conclusion that the temperature to which the insulation was exposed did not exceed 200° is undermined by the omission of certain materials, his own

evidence that the fire did not burn at an even rate and the physical evidence of deteriorated insulation even where the paint had not burned off. I am unable to accept Mr. Morrison's evidence that except in the area of the main leads and the fault there would have been no damage to insulation had the deluge system been applied in the first 25 minutes or indeed the first 10 minutes. I am not suggesting that all coils in the generator were damaged beyond repair by that time, or indeed after 55 minutes. I find that the damage was so great that the only practical solution was a total rewind.

Interest:

[165] The plaintiff seeks interest under the *Judgment Interest Act*. Under the *Act* and *Regulations,* 9% has been established as the interest rate applicable. However, the plaintiff asks that I exercise the discretion provided under s. 3(3) to award at a rate and for a period other than that specified under s. 4 of the *Act*.

[166] The plaintiff argues that it is just to award interest at a rate that reflects the actual loss to Abitibi-Price and "the commercial realities of the situation". It submits that the appropriate rate would be the prime rate adopted by the Royal Bank of Canada, Canada's largest chartered bank. It further submits that the calculations should be made on the basis of one month periods rather than the three month period referred to in s. 4(2)(a). However, Abitibi-Price has brought no evidence as to the cost to it of borrowing money or its loss of potential income.

[167] I have been referred to *Phoenix Press Co. v. Vinto Engineering* (1982), 34 A.R. 244, as authority for the proposition that I might take judicial notice of the rates. That case can be distinguished on a number of grounds. In the first place it was determined under provisions respecting the payment of interest of the *Judicature Act* then in force in Alberta and under which there was no rate set. The judge actually specified the particular rate applicable (12%). While in the circumstances of a case such as this one, I would be open to the submission that the rate of interest paid by the plaintiff on borrowed money represents an appropriate figure for payment of interest, I would not be prepared to do so in the absence of evidence respecting the borrowing rates applicable to Abitibi-Price, evidence which was certainly within the control of the plaintiff and could have been provided to the court. In

the absence of such evidence, the rate set out in the *Judgment Interest Act* should be applied.

Summary

[168] The plaintiff is awarded the following:

(i) For Repair of Generator No. 4---------- $1,311,363

For Replacement of power---------- 3,720,576

Total$---------- 5,031,939

[169] The plaintiff shall have interest on the amount awarded as specified by the *Judgment Interest Act.*

[170] The plaintiff sought and I hereby grant leave to make submissions respecting costs. Either party may bring the matter on.

[171] This was a lengthy trial. The evidence was often of a technical nature. I am grateful to counsel for their courtesy, patience and guidance through the labyrinth. Order accordingly.

Southcott Estates Inc. v. Toronto Catholic District School Board, 2012 SCC 51, [2012] 2 SCR 675

SUPREME COURT OF CANADA

CITATION: Southcott Estates Inc. *v.* Toronto Catholic District School Board, 2012 SCC 51, [2012] 2 S.C.R. 675

DATE: 20121017
DOCKET: 33778

BETWEEN:

Southcott Estates Inc.
Appellant / Respondent on cross-appeal
and
Toronto Catholic District School Board
Respondent / Appellant on cross-appeal

CORAM: McLachlin C.J. and LeBel, Deschamps, Abella, Rothstein, Cromwell and Karakatsanis JJ.

REASONS FOR JUDGMENT: (paras. 1 to 63)	Karakatsanis J. (LeBel, Deschamps, Abella, Rothstein and Cromwell JJ. concurring)
DISSENTING REASONS: (paras. 64 to 99)	McLachlin C.J.

Southcott Estates Inc. *v.* Toronto Catholic District School Board, 2012 SCC 51, [2012] 2 S.C.R. 675

Southcott Estates Inc. *Appellant/Respondent on cross-appeal*

v.

Toronto Catholic District School Board *Respondent/Appellant on cross-appeal*

Indexed as: Southcott Estates Inc. *v.* Toronto Catholic District School Board

2012 SCC 51

File No.: 33778.

2012: March 20; 2012: October 17.

Present: McLachlin C.J. and LeBel, Deschamps, Abella, Rothstein, Cromwell and Karakatsanis JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Contracts — Commercial contracts — Remedies — Specific performance — Duty to mitigate — Single-purpose company entering into agreement for purchase of land — Vendor breaching contractual obligations — Company seeking specific performance — Whether single-purpose company must mitigate its losses — Whether plaintiff seeking specific performance has obligation to mitigate its losses — Whether trial judge erred in concluding there were no comparable properties available for mitigation.

The appellant S is a single-purpose company incorporated solely for the purpose of a specific land purchase, with no assets other than money advanced to it by its parent company for the deposit relating to such purchase. It entered into an agreement of purchase and sale for a specific property with the respondent. When the respondent failed to satisfy a condition and refused to extend the closing date, S sought specific performance of the contract. It argued that it was not required to mitigate its losses. The trial judge refused to award specific performance but awarded damages to S in the amount of $1,935,500. The Court of Appeal concluded that the respondent had breached its contractual obligations but that S had failed to take available steps to mitigate its losses. It reduced the damage award to a nominal sum.

Held (McLachlin C.J. dissenting): The appeal and cross-appeal should be dismissed.

Per LeBel, Deschamps, Abella, Rothstein, Cromwell and Karakatsanis JJ.: Mitigation is a doctrine based on fairness and common sense, which seeks to do justice between the parties in the particular circumstances of the case. As a general rule, a plaintiff will not be able to recover those losses which he could have avoided by taking reasonable steps.

The main issue is whether S, a single-purpose corporation, was excused from mitigating its losses when the vendor breached the agreement of purchase and sale, and particularly when it had promptly brought an action for specific performance. As a separate legal entity, S was required to mitigate by making diligent efforts to find a substitute property. Those who choose the benefits of incorporation must bear the corresponding burdens. One such responsibility is to take steps to mitigate losses. A plaintiff cannot recover losses that could reasonably have been avoided. S sought specific performance and was therefore ready to complete the purchase. Its alternative claim for consequential damages was predicated upon its access to capital to complete the agreement of purchase and sale. As such, both claims were premised upon resources that were not tied up as a result of the breach alleged. S can hardly argue that the same money would not have been available for mitigation. In the absence of actual evidence of impecuniosity, finding that losses cannot be reasonably avoided, simply because the corporation is a single-purpose corporation within a larger group of companies, would give these corporations an unfair advantage. If single-purpose corporations were not required to mitigate their losses, this could expose defendants contracting with such corporations to higher damage awards.

This Court has recognized that there may be situations in which a plaintiff's inaction is justifiable notwithstanding its failure to obtain an order for specific performance. If the plaintiff has a "fair, real, and substantial justification" or a "substantial and legitimate interest" in specific performance, its refusal to purchase other property may be reasonable, depending upon the circumstances of the case. A plaintiff deprived of an investment property does not have a "fair, real, and substantial justification" or a "substantial and legitimate interest" in specific performance unless he can show that money is not a complete remedy because the land has "a peculiar and special value" to him. S has not demonstrated such a claim and therefore cannot justify its inaction. S was engaged in a commercial transaction for the purpose of making a profit. The property's particular qualities were only of value due to their ability to further profitability, for which damages were an adequate remedy.

Where it is alleged that the plaintiff has failed to mitigate, the defendant bears the burden of proving that the plaintiff has failed to make reasonable efforts to mitigate and that mitigation was possible. Whether or not there were comparable properties and whether they are profitable is a finding of fact. The trial judge made a palpable and overriding error in finding there were no comparable mitigation opportunities. He failed to consider the reasonable and available inferences arising from expert evidence regarding other land suitable for development sold in the area, the investment properties purchased by the parent company of S and the absence of evidence to the contrary. The respondent discharged the burden of showing that there were other comparable development properties available in the relevant time period to mitigate the losses.

Per McLachlin C.J. (dissenting): The Board, having breached the contract, bears the onus of proving that S unreasonably failed to mitigate its loss. This entails establishing, on a balance of probabilities: (1) that an opportunity to mitigate the loss was available to S; and (2) that S unreasonably failed to pursue that opportunity. The trial judge's finding that the Board failed to establish that S had an opportunity to mitigate is sufficient to dispose of the appeal. This finding was grounded in the evidence and did not constitute palpable and overriding error. The Board failed to prove that another property comparable to the one that S sought to purchase was available. Neither the evidence of the Board's expert witness nor that of purchases by other subsidiaries of S's parent company established that a comparable property was available for S.

Moreover, S could not be unreasonable in failing to mitigate its loss because it reasonably maintained its action for specific performance. The act of filing a claim for specific performance is inconsistent with the act of acquiring a substitute property. A plaintiff, acting reasonably, cannot pursue specific performance and mitigate its potential loss of damages at the same time. There is no basis on which to conclude that S acted unreasonably in maintaining its suit for specific performance instead of mitigating its loss. S had a "fair, real, and substantial justification" for claiming specific performance. The property was uniquely suited to S's needs for single-family residential development within the City of Toronto. The evidence supported the view that there were no comparable substitute properties.

Furthermore, it is difficult to conclude that S unreasonably failed to mitigate given that S lacked the financial capacity to go into the market and purchase a substitute property.

Cases Cited

By Karakatsanis J.

Referred to: *Asamera Oil Corp. v. Seal Oil & General Corp.*, 1978 CanLII 16 (SCC), [1979] 1 S.C.R. 633; *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London, Ltd.*, [1912] A.C. 673; *British Columbia v. Canadian Forest Products Ltd.*, 2004 SCC 38 (CanLII), 2004 SCC 38, [2004] 2 S.C.R. 74; *Red Deer College v. Michaels*, 1975 CanLII 15 (SCC), [1976] 2 S.C.R. 324; *Evans v. Teamsters Local Union No. 31*, 2008 SCC 20 (CanLII), 2008 SCC 20, [2008] 1 S.C.R. 661; *Redpath Industries Ltd. v. Cisco (The)*, 1993 CanLII 3025 (FCA), [1994] 2 F.C. 279; *Kosmopoulos v. Constitution Insurance Co.*, 1987 CanLII 75 (SCC), [1987] 1

S.C.R. 2; *Semelhago v. Paramadevan*, 1996 CanLII 209 (SCC), [1996] 2 S.C.R. 415; *Adderley v. Dixon* (1824), 1 Sim. & St. 607, 57 E.R. 239; *Housen v. Nikolaisen*, 2002 SCC 33 (CanLII), 2002 SCC 33, [2002] 2 S.C.R. 235.

By McLachlin C.J. (dissenting)

Asamera Oil Corp. v. Seal Oil & General Corp., 1978 CanLII 16 (SCC), [1979] 1 S.C.R. 633; *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London, Ltd.*, [1912] A.C. 673; *Dunkirk Colliery Co. v. Lever* (1878), 9 Ch. D. 20; *Janiak v. Ippolito*, 1985 CanLII 62 (SCC), [1985] 1 S.C.R. 146; *Darbishire v. Warran*, [1963] 1 W.L.R. 1067; *Red Deer College v. Michaels*, 1975 CanLII 15 (SCC), [1976] 2 S.C.R. 324; *Roper v. Johnson* (1873), L.R. 8 C.P. 167; *Lagden v. O'Connor*, [2003] UKHL 64, [2004] 1 All E.R. 277; *General Securities Ltd. v. Don Ingram Ltd.*, 1940 CanLII 28 (SCC), [1940] S.C.R. 670; *Andros Springs v. World Beauty*, [1970] P. 144; *Housen v. Nikolaisen*, 2002 SCC 33 (CanLII), 2002 SCC 33, [2002] 2 S.C.R. 235; *Apeco of Canada, Ltd. v. Windmill Place*, 1978 CanLII 186 (SCC), [1978] 2 S.C.R. 385; *Semelhago v. Paramadevan*, 1996 CanLII 209 (SCC), [1996] 2 S.C.R. 415.

Statutes and Regulations Cited

Education Act, R.S.O. 1990, c. E.2.

Authors Cited

Bates, Paul. "Mitigation of Damages: A Matter of Commercial Common Sense" (1992), 13 *Advocates' Q.* 273.

McGregor, Harvey. *McGregor on Damages*, 18th ed. London: Sweet & Maxwell/Thomson Reuters, 2009.

Siebrasse, Norman. "Damages in Lieu of Specific Performance: *Semelhago v. Paramadevan*" (1997), 76 *Can. Bar Rev.* 551.

Yorio, Edward. "A Defense of Equitable Defenses" (1990), 51 *Ohio St. L.J.* 1201.

APPEAL and CROSS-APPEAL from a judgment of the Ontario Court of Appeal (Sharpe, Blair and MacFarland JJ.A.), 2010 ONCA 310 (CanLII), 2010 ONCA 310, 104 O.R. (3d) 784, 261 O.A.C. 108, 319 D.L.R. (4th) 349, 93 R.P.R. (4th) 159, 71 B.L.R. (4th) 196, [2010] O.J. No. 1772 (QL), 2010 CarswellOnt 2602, setting aside a decision of Spiegel J. 2009 CanLII 3567 (ON SC), (2009), 78 R.P.R. (4th) 285, [2009] O.J. No. 428 (QL), 2009 CanLII 3567, 2009 CarswellOnt 494. Appeal and cross-appeal dismissed, McLachlin C.J. dissenting.

J. Thomas Curry, *Milton A. Davis* and *Paul-Erik Veel*, for the appellant/respondent on cross-appeal.

Andrew M. Robinson, *Elizabeth K. Ackman* and *Andrea Farkouh*, for the respondent/appellant on cross-appeal.

The judgment of LeBel, Deschamps, Abella, Rothstein, Cromwell and Karakatsanis JJ. was delivered by

KARAKATSANIS J. —

I. Introduction

[1] Real estate developers frequently create single-purpose corporations for the sole purpose of purchasing and developing properties for profit. The corporation has limited liability and no assets other than those that arise from the particular real estate investment. The issue raised in this appeal is whether such a single-purpose corporation is excused from mitigating its losses when the vendor breaches the agreement of purchase and sale, and particularly when it has promptly brought an action for specific performance. The further issue is whether the trial judge erred in his finding that there were no other "comparable" properties available to mitigate the loss.

[2] The appellant, Southcott Estates Inc., was part of the Ballantry Group of associated companies that acquired and developed land in the Greater Toronto Area ("GTA"). Southcott was a single-purpose corporation, without assets, created for the sole purpose of developing the property that is the subject of this action. When the vendor, the Toronto Catholic District School Board, failed to satisfy a condition and refused to extend the closing date, Southcott sought specific performance of the contract. It argues that it was not required to mitigate its losses.

[3] The trial judge ((2009), 78 R.P.R. (4th) 285) found that the Board had breached the agreement of purchase and sale and had failed to prove that Southcott could have mitigated its damages. He awarded damages for loss of chance of profit. He refused to order specific performance, finding that the property was not "unique" and damages were an adequate remedy.

[4] The Ontario Court of Appeal 2010 ONCA 310 (CanLII), (2010 ONCA 310, 104 O.R. (3d) 784) concluded that while the trial judge correctly found that the Board had breached its contractual obligations, he had erred in his approach to mitigation. The court concluded that Southcott had unreasonably failed to take available steps to mitigate its loss and reduced the damage award granted at trial to a nominal sum.

[5] Southcott did not appeal the trial judge's refusal to award specific performance. However, it maintains its losses were not avoidable. The questions raised in this appeal are:

1. Should a single-purpose company mitigate its losses?

2. To what extent must a plaintiff mitigate where the plaintiff has made a claim for specific performance?

3. Did the trial judge err in concluding that there was no evidence of comparable profitable properties available for mitigation?

[6] For the reasons that follow, I conclude that Southcott cannot recover losses that it could reasonably have avoided. I agree with the Court of Appeal that the trial judge erred in concluding that there was no evidence of other development properties that Southcott could have purchased in mitigation. I would dismiss the appeal.

II. Facts

[7] Southcott is a wholly owned subsidiary of Ballantry Homes Inc. and part of a larger group of companies called Ballantry Group of Companies ("Ballantry" or "Ballantry Group"). The Board is a School Board created pursuant to the *Education Act*, R.S.O. 1990, c. E.2, whose affairs were run by a publicly elected Board of Trustees.

[8] Having determined that certain land within a school property was surplus to its needs, the Board put it up for sale. Intending to use the land for residential development, Southcott agreed to purchase the 4.78 acres of land for $3.44 million. It paid a 10 percent deposit and the parties agreed to a closing date of August 31, 2004. It was a condition of the agreement that the Board obtain a severance from the Committee of Adjustments on or before the closing date. On August 30, 2004, the parties agreed to extend the closing date to January 31, 2005.

[9] The Board applied for a severance in November; it was advised that a development plan was necessary but chose to proceed without one. On December 16, 2004, at the municipality's request, the Committee of Adjustments deferred the severance application hearing as premature because it was not accompanied by a development plan. At that time, it became clear to Southcott and the Board that the transaction could not be completed by the closing date of January 31, 2005. The Board refused Southcott's request to extend the closing date, declared the transaction to be at an end, and returned Southcott's deposit.

[10] Southcott took the position that the Board had breached its obligation to use its best efforts to obtain the severance and commenced an action for specific performance or, in the alternative, for damages.

[11] Southcott admitted that it never had any intention to mitigate its loss and, indeed, never tried to mitigate (para. 137 of the trial judge's decision). Southcott was a single-purpose company incorporated solely for the purposes of this development project and had no assets other than the money advanced by Ballantry for the deposit. It never intended to purchase other land. In fact, Southcott's principal testified at trial that there was no question of it purchasing other land, given that it was involved in this litigation (para. 18 of the Court of Appeal's decision).

[12] The Board led expert evidence that 81 parcels of vacant development land in the GTA were sold between the date of breach and the date of trial. The land was suitable for residential development and within the parameters, of size and price, of other lands purchased by the Ballantry Group.

[13] Corporations within the Ballantry Group purchased seven parcels of land for development purposes during this same period. The principal of Ballantry testified that it was always in the market for new land, had the financial means to make the purchases, and it would have made these purchases even if Southcott had completed the land purchase from the Board (para. 138 of the trial judge's decision).

III. Decisions Below

[14] At trial, Spiegel J. concluded that the Board had failed to take all reasonable steps to fulfill the severance condition. It breached its best efforts obligation by failing to contact relevant city staff; delaying in processing the severance application; failing to include the proposed plan of use with the severance application; submitting an improper survey; failing to seek appropriate advice; ignoring the advice of the Committee of Adjustments; proceeding with the application for severance even after being advised that it was incomplete and failing to keep Southcott informed (paras. 71-87).

[15] The trial judge found that had the Board used its best efforts, the severance would likely have been granted, and the transaction would have been completed by the closing date. The trial judge was satisfied that the Board's breach caused Southcott's loss (paras. 93-116).

[16] Turning to remedy, Spiegel J. found that specific performance was not an appropriate remedy as the land did not have the quality of uniqueness (paras. 128-33).

[17] However, he concluded that Southcott was entitled to damages. He rejected the Board's argument that Southcott had in fact mitigated damages because the Ballantry Group made several purchases subsequent to the breach of the agreement:

> I find that these subsequent purchases were collateral, independent transactions that did not arise out of the consequences of the breach. In all the circumstances, I do not consider these transactions as mitigatory. [para. 143]

[18] The trial judge found that the Board had not discharged the onus of proving that Southcott failed to take advantage of a reasonable opportunity to mitigate its loss. He held that there was no evidence that any of the available properties were actually offered for sale or could have been profitably developed and he was not satisfied that the properties were comparable (paras. 144-46). He therefore awarded Southcott damages in the amount of $1,935,500 which represented the loss of a 60 percent chance to make profits in the amount of $3,225,827.

[19] On appeal, the Board did not dispute the findings that it had breached its obligation to use its best efforts to obtain the severance required to complete the sale. It challenged the findings of causation and mitigation.

[20] Sharpe J.A., writing for the Court of Appeal, rejected the first ground of the Board's appeal, that the trial judge erred in finding that the Board's breach was the cause of the failure to obtain the severance by the closing date (paras. 11-14).

[21] Regarding the issue of whether the losses could have been avoided, however, the Court of Appeal concluded that the trial judge had erred in law in finding that the Board had not shown that Southcott could have mitigated its losses. First, Southcott's admission that it had no intention of taking any steps to mitigate was sufficient to satisfy the onus resting upon the Board and to shift the evidentiary onus to Southcott to demonstrate that, even if it had attempted to mitigate, it could not have done so. Second, the trial judge erred in dealing with the Board's evidence regarding the land that was available: "By requiring the Board to prove . . . the profitability of individual parcels, the trial judge raised any bar the Board had to satisfy to an unrealistic level" (para. 25). Finally, the trial judge failed to consider that Ballantry's purchases of other lands clearly demonstrated that the directing mind of Southcott knew that investment quality lands, suitable for profitable development, were available on the market. The Court of Appeal stated that Southcott was a distinct legal entity that could not avoid mitigating its loss by arguing that it was a part of Ballantry: the obligation to mitigate rested with Southcott (paras. 24-27).

[22] The Court of Appeal concluded that while Southcott had made out its case for breach of contract, it failed to make out a case for either specific performance or damages. The appropriate award was for nominal damages in the amount of $1.

IV. Mitigation — General Principles

[23] This Court in *Asamera Oil Corp. v. Seal Oil & General Corp.*, 1978 CanLII 16 (SCC), [1979] 1 S.C.R. 633, cited (at pp. 660-61) with approval the statement of Viscount Haldane L.C. in *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London, Ltd.*, [1912] A.C. 673, at p. 689:

> The fundamental basis is thus compensation for pecuniary loss naturally flowing from the breach; but this first principle is qualified by a second, which imposes on a plaintiff the duty of taking all reasonable steps to mitigate the loss consequent on the breach, and debars him from claiming any part of the damage which is due to his neglect to take such steps.

[24] In *British Columbia v. Canadian Forest Products Ltd.*, 2004 SCC 38 (CanLII), 2004 SCC 38, [2004] 2 S.C.R. 74, at para. 176, this Court explained that "[l]osses that could reasonably have been avoided are, in effect, caused by the plaintiff's inaction, rather than the defendant's wrong." As a general rule, a plaintiff will not be able to recover for those losses which he could have avoided by taking reasonable steps.

Where it is alleged that the plaintiff has failed to mitigate, the burden of proof is on the defendant, who needs to prove both that the plaintiff has failed to make reasonable efforts to mitigate and that mitigation was possible (*Red Deer College v. Michaels*, 1975 CanLII 15 (SCC), [1976] 2 S.C.R. 324; *Asamera*; *Evans v. Teamsters Local Union No. 31*, 2008 SCC 20 (CanLII), 2008 SCC 20, [2008] 1 S.C.R. 661, at para. 30).

[25] On the other hand, a plaintiff who does take reasonable steps to mitigate loss may recover, as damages, the costs and expenses incurred in taking those reasonable steps, provided that the costs and expenses are reasonable and were truly incurred in mitigation of damages (see P. Bates, "Mitigation of Damages: A Matter of Commercial Common Sense" (1992), 13 *Advocates' Q.* 273). The valuation of damages is therefore a balancing process: as the Federal Court of Appeal stated in *Redpath Industries Ltd. v. Cisco (The)*, 1993 CanLII 3025 (FCA), [1994] 2 F.C. 279, at p. 302: "The Court must make sure that the victim is compensated for his loss; but it must at the same time make sure that the wrongdoer is not abused." Mitigation is a doctrine based on fairness and common sense, which seeks to do justice between the parties in the particular circumstances of the case.

A. *Should a Single-Purpose Company Mitigate its Losses?*

[26] Southcott argues that the Court of Appeal failed to recognize the unique circumstance of a single-purpose corporation in mitigating contractual loss; as a single-purpose company, it was impecunious and unable to mitigate without significant capital investment of the parent company or without the corporate mandate to do so. Further, it submits that it would be reasonably foreseeable to those contracting with a single-purpose corporation that such an entity would have finite resources and a confined corporate mandate. In this case, Southcott acted reasonably, within its ordinary course of business and promptly brought this lawsuit.

[27] Southcott sought specific performance and was therefore ready to complete the purchase. In any event, its alternative claim for consequential damages was predicated upon its access to capital to complete the agreement of purchase and sale. As such, both claims were premised upon resources, resources that were not tied up as a result of the breach alleged. Indeed, the alleged breach in this case did not affect Southcott's ability to obtain capital. Southcott can hardly argue that the same money would not have been available for mitigation.

[28] Further, the question is factual and it was not suggested at trial that Southcott had no access to capital or that borrowing money would have been unreasonably risky or costly. Southcott did not argue that it was impecunious at trial.

[29] In the absence of actual evidence of impecuniosity, finding that losses cannot be reasonably avoided, simply because it is a single-purpose corporation within a larger group of companies, would give an unfair advantage to those conducting business through single-purpose corporations. In addition, not requiring single-purpose corporations to mitigate would expose defendants contracting with such corporations to higher damage awards than those reasonably claimed by other plaintiffs, based solely upon their limited assets.

[30] The trial judge found that the purchases of development land by other corporations within the Ballantry Group did not in fact mitigate Southcott's loss; that finding is not challenged here. As noted above, he found that the other properties purchased by other members of the Ballantry group were "collateral" in the sense that the purchases would have occurred whether or not the defendant had breached its contract with Southcott (para. 143). However, because Southcott is a separate legal entity, purchases by other Ballantry corporations of other comparable property did not make those properties "unavailable" for mitigation. As a separate legal entity, Southcott was required to mitigate by making diligent efforts to find a substitute property. Those who choose the benefits of incorporation must bear the corresponding burdens: *Kosmopoulos v. Constitution Insurance Co.*, 1987 CanLII 75 (SCC), [1987] 1 S.C.R. 2, at pp. 10-12. Southcott is entitled to the benefits of limited liability, but it is also saddled with the responsibilities that all legal entities have. The requirement to take steps to mitigate losses is one such responsibility. A plaintiff cannot recover losses that could reasonably have been avoided. The overriding issue here is whether Southcott's inaction was reasonable, and if not, whether it could have reasonably mitigated if it had tried to do so.

B. *Southcott Was Required to Mitigate Losses Despite its Claim for Specific Performance*

[31] Specific performance is an equitable remedy that is difficult to reconcile with the principle of mitigation. Obviously, if Southcott had purchased a property in mitigation, it may not have been able to complete its agreement of purchase and sale of the Board's surplus land if ultimately successful in its claim for specific performance. When can a plaintiff seeking specific performance justify inaction and recover losses which may otherwise have been classified as avoidable?

[32] The trial judge found that Southcott did not have a viable claim for specific performance. He found that while the business opportunity may have been unique, the property itself was not. The trial judge found that what was at issue here was a straightforward business plan, the failure of which could be measured in damages (para. 132). The Court of Appeal agreed. The trial judge's decision not to order specific performance is not challenged in this appeal.

[33] However, Southcott submits that even though it was unsuccessful in its claim for specific performance, it proceeded expeditiously and the claim had real substance because the property was a unique opportunity, given its location and the rarity of such properties in the GTA. As a result, it says that it was not reasonable to attempt to mitigate; the remedy of specific performance would become illusory.

[34] Southcott suggests that there are two separate questions that a court must ask in cases where a plaintiff seeks specific performance: (1) should specific performance be awarded? And if the answer is no, (2) is this plaintiff justified in its mitigatory inaction? Southcott says that the trial judge conflated these two questions and did not consider whether it was justified in failing to mitigate.

[35] This Court dealt with this issue in *Asamera*, at pp. 668-69:

> Before a plaintiff can rely on a claim to specific performance so as to insulate himself from the consequences of failing to procure alternate property in mitigation of his losses, some fair, real, and substantial justification for his claim to performance must be found. . . .
>
> . . .
>
> . . . Where . . . circumstances reveal a substantial and legitimate interest in seeking [specific] performance as opposed to damages, then a plaintiff will be able to justify his inaction and on failing in his plea for specific performance might then [be able to] recover losses which in other circumstances might be classified as avoidable and thus unrecoverable . . . .

[36] This Court thus recognized that there may be situations in which a plaintiff's inaction is justifiable notwithstanding its failure to obtain an order for specific performance where circumstances reveal "some fair, real, and substantial justification" for his claim or "a substantial and legitimate interest" in seeking specific performance (*Asamera*, at pp. 668-69 (emphasis added)). This does not mean that a plaintiff with such a claim should not attempt to mitigate; rather it recognizes that such a claim for specific performance informs what is reasonable behaviour for the plaintiff in mitigation. See N. Siebrasse, "Damages in Lieu of Specific Performance: *Semelhago v. Paramadevan*" (1997), 76 *Can. Bar Rev.* 551.

[37] *Asamera* set out the general principles governing mitigation: was the plaintiff's inaction reasonable in the circumstances, and could the plaintiff have mitigated if it chose to do so. Those principles apply to a plaintiff seeking specific performance. If the plaintiff has a "substantial justification" or a "substantial and legitimate interest" in specific performance, its refusal to purchase other property may be reasonable, depending upon the circumstances of the case.

[38] The statements in *Asamera* dealing with specific performance and the determination of what is reasonable conduct must be read in light of *Semelhago v. Paramadevan*, 1996 CanLII 209 (SCC), [1996] 2 S.C.R. 415. In that case, the Court acknowledged that "[w]hile at one time the common law regarded every piece of real estate to be unique, with the progress of modern real estate development this is no longer the case" (para. 20). The Court thus found that it "cannot be assumed that damages for breach of contract for the purchase and sale of real estate will be an inadequate remedy in all cases" (para. 21). Specific performance will be available only where money cannot compensate fully for the loss, because of some "peculiar and special value" of the land to the plaintiff (para. 21, citing *Adderley v. Dixon* (1824), 1 Sim. & St. 607, 57 E.R. 239, at p. 240).

[39] The overriding issue is therefore whether Southcott's inaction was reasonable. Southcott argued at trial that the fact that the property was uniquely well situated gives it the unique character required to constitute a fair justification for specific performance (para. 119 of the trial judge's decision).

[40] I agree with the courts below that this is not a case where the plaintiff could reasonably refuse to mitigate. The trial judge made clear findings that the land was

nothing more unique to Southcott than a singularly good investment and that this was not a case in which damages were too speculative or uncertain to be a satisfactory remedy. The unique qualities related solely to the profitability of the development for which damages were an adequate remedy (paras. 126 and 128). The calculation of profits was not conjectural or speculative as the proposed development was not complex, and the only disagreement between the parties regarding the quantum of damages related to the timing and rate of sale of completed units (paras. 130 and 132).

[41] A plaintiff deprived of an investment property does not have a "fair, real, and substantial justification" or a "substantial and legitimate" interest in specific performance (*Asamera*, at pp. 668-69) unless he can show that money is not a complete remedy because the land has "a peculiar and special value" to him (*Semelhago*, at para. 21, citing *Adderley*, at p. 240). Southcott could not make such a claim. It was engaged in a commercial transaction for the purpose of making a profit. The property's particular qualities were only of value due to their ability to further profitability. Southcott cannot therefore justify its inaction.

C. *The Trial Judge Erred in Finding no Evidence of Comparable Profitable Properties Available for Mitigation*

[42] In this case, Southcott admitted that it made no efforts to mitigate — on the basis that it was not obliged to do so. Southcott submits that the Court of Appeal erred in shifting the onus to the plaintiff based on the admission by Southcott's principal that he had no intention to mitigate through Southcott. Southcott says that the Board did not provide the trial judge with evidence that there was a comparable profitable investment property available for sale. The trial judge found that there were no comparable or profitable properties. Southcott submits that the Court of Appeal erred in disregarding the trial judge's finding of fact and in substituting its own.

[43] The entirety of the trial judge's analysis on this issue was as follows:

> There was no evidence that the properties referred to [by the Board's expert] were actually available to the public for sale but only that they had been sold. Also there was no evidence that had these properties been purchased that they could have been profitably developed. In any event, I am not satisfied that the evidence established that these were comparable properties or that had they been purchased, that the plaintiff's loss would have been avoided or reduced. [para. 144]

[44] Regarding the failure to mitigate, the Court of Appeal found that the trial judge had erred in law:

> First, Southcott's admission that it had no intention of taking any steps to mitigate its loss was sufficient to satisfy the onus resting upon the Board to prove failure to mitigate and to shift the evidentiary onus to Southcott of demonstrating that, even if it had attempted to mitigate, it could not have done so. Southcott led no evidence to that effect. In my view, the trial judge erred by holding that the

> Board had failed to meet the onus imposed upon it to prove that Southcott had failed to mitigate its damages.
>
> . . . By requiring the Board to prove the precise manner in which 81 parcels of investment land had been sold or to prove the profitability of individual parcels, the trial judge raised any bar the Board had to satisfy to an unrealistic level, particularly in the face of Southcott's admission that it had no intention to mitigate and of the evidence that Ballantry actually did find other suitable development properties to purchase.
>
> Third, the trial judge erred in the manner in which he dealt with the evidence of purchases made by Ballantry. Those purchases clearly demonstrate that the directing mind of Southcott knew that investment-quality lands, suitable for profitable development, were available on the market. [paras. 24-26]

[45] As noted above, where it is alleged that a plaintiff has failed to mitigate damages, the onus of proof on a balance of probabilities lies with the defendant, who must establish not only that the plaintiff failed to take reasonable efforts to find a substitute, but also that a reasonable profitable substitute could be found.

[46] Thus, it would be an error to suggest that the defendant did not have the burden of showing that mitigation was possible even where the plaintiff made no attempt to do so. Further, while I agree that the trial judge erred in dealing with the Board's evidence regarding the availability of the 81 properties, the error is best approached as an evidentiary issue rather than as one engaging the burden of proof.

[47] The finding about whether Southcott could have mitigated involves applying a legal standard; it is a question of mixed fact and law. Whether or not there were comparable properties and whether they were profitable is a finding of fact. Implicit in the Court of Appeal's decision is the conclusion that the trial judge's findings of fact were unreasonable.

[48] For the reasons that follow, I agree with the Court of Appeal that the trial judge erred in principle by failing to consider relevant evidence. In particular, Ballantry's subsequent purchases were evidence that other development properties were reasonably available. These errors skewed his factual analysis on the issue of mitigation. I conclude that the trial judge made a palpable and overriding error in finding that there were no comparable profitable mitigation opportunities: see *Housen v. Nikolaisen*, 2002 SCC 33 (CanLII), 2002 SCC 33, [2002] 2 S.C.R. 235, at para. 10.

(1) The Expert Evidence of Comparable Properties

[49] At trial, the Board presented evidence that 81 parcels of raw land suitable for development and 49 properties subdivided into lots suitable for building were available for sale in the GTA and were in fact sold in the period between January 31, 2005 and the time

of trial (para. 136 of the trial judge's decision). The parameters that the Board's expert used in selecting alternative available parcels were sales of land between $1,000,000 and $27,000,000, that had an estimated time to develop of one year or less, and that could be developed for low to medium density residential. These parameters were chosen to match the parameters of the actual purchases made by the Ballantry Group.

[50] Nevertheless, the trial judge concluded that the Board had not discharged the onus of proving that Southcott failed to take advantage of a reasonable opportunity to mitigate. He found that: there was no evidence that the 81 properties were actually available to the public for sale; there was no evidence that, had these properties been purchased, they could have been profitably developed, and the plaintiff's loss could have been avoided or reduced; and in any event, these properties were not comparable properties.

[51] The trial judge failed to consider the available and reasonable inferences of the Board's evidence that there were 81 parcels of raw land suitable for development and 49 properties subdivided into lots suitable for building sold during the time period in issue here. In cross-examination, the Board's expert witness admitted being unaware of the marketing strategies used to sell the 81 properties sold during the period in which the Board suggested that Southcott could mitigate (A.R., at p. 232-33). However, notwithstanding that answer, it is an obvious inference that if 81 properties suitable for development were offered for sale, and were in fact sold, then investment properties were available to developers for sale, particularly in the absence of evidence to the contrary.

[52] Further, the trial judge failed to consider whether the fact that all of the properties the Board's expert testified to were capable of being brought to development in a year could support an inference that their development was profitable. Reasonable inferences of profitability could be drawn based upon the size and price of property or the fact that land was purchased for development purposes by experienced developers. The trial judge did not turn his mind to this evidence.

[53] Finally, the trial judge also failed to consider that an adverse inference against Southcott could be drawn from the fact that it led no evidence about the profitability of the alternative development opportunities.

(2) The Purchases by Ballantry

[54] I agree with the Court of Appeal that the trial judge also erred in failing to consider whether the purchases by the Ballantry corporations provided evidence of other profitable properties available in mitigation. As noted above, the trial judge found (at para. 143) that the other properties purchased by other members of the Ballantry Group were "collateral" in the sense that the transactions would have occurred whether or not the defendant had breached its contract with Southcott and did not represent actual mitigation due to Southcott's distinct legal personality. This is not challenged.

[55] The trial judge did not go on to consider, however, whether these transactions established that those same properties were evidence of "available"

comparable mitigation opportunities in the market. Because Southcott is a separate legal entity, purchases by other Ballantry corporations of other comparable property did not make those properties "unavailable" for mitigation. In effect, the trial judge ignored the separate legal personalities of Southcott and the other corporations in the Ballantry Group by failing to consider those purchases as evidence of the existence of mitigation opportunities.

[56] The Ballantry Group companies purchased seven other development properties subsequent to the breach of the agreement, ranging in size from 2.3 acres to 110.8 acres and in price from $3.3 million to $27.1 million. In particular, two specific purchases were clearly comparable. Southcott had agreed to purchase 4.78 acres of land for $3.44 million in August 2004. Ballantry corporations purchased 2.7 acres for $3.3 million in August 2005 and 2.3 acres for $6 million in December 2006.

[57] The defence raised by Southcott, which was accepted by the trial judge, was that the purchases by Ballantry Group of development lands in the GTA were purchases which would have been made in any event, regardless of whether Southcott purchased the Board's property. However, it is no answer to say that other companies in the same corporate group would have purchased the other available lands in any event. It was clear from the testimony of the president of Southcott and co-owner of Ballantry that the Ballantry Group was always purchasing promising development land and that the different companies were simply used as different vehicles to invest.

[58] It was a choice on the part of the principals of the Ballantry Group as to which corporate entity would be used for each purchase and they elected not to use Southcott. In addition, the trial judge found that "[t]he plaintiff['s] proposed development here was not complex, but rather a relatively straightforward plan for the development of 48 semi-detached residential units" (para. 132). In these circumstances, a straightforward development could have been carried out on a different property by Southcott, had it wanted to mitigate its loss. This corresponds to the modern reality recognized in *Semelhago* that "[r]esidential, business and industrial properties are all mass produced much in the same way as other consumer products" (para. 20).

[59] As the Court of Appeal concluded (paras. 25-26), the Ballantry Group's purchases of other properties was evidence that other suitable development lands *were* available and the decision not to purchase them in Southcott's name was based on other considerations. I agree with the Court of Appeal that the trial judge erred in failing to consider these purchases as evidence of other available and comparable development properties.

V. Conclusion

[60] In conclusion, the trial judge erred in failing to consider relevant evidence and made a palpable and overriding error of fact in concluding that Southcott could not have reasonably avoided its loss.

[61] He failed to take into account in his analysis of the mitigation issue that Southcott had simply refused to take any mitigatory action. He failed to consider the

evidence of Ballantry's purchases as supporting the inference that alternative parcels were available and that their development was sufficiently profitable to meet Ballantry's requirements. He conflated a lack of evidence regarding the marketing of parcels with a lack of evidence that any of the parcels had been available for sale. He failed to consider whether the fact that all of the properties the Board's expert testified were development properties capable of being brought to development in a year could support an inference that their development was profitable. Finally, he failed to consider the fact that Southcott did not lead evidence to challenge the Board's evidence regarding alternative development opportunities.

[62] In these circumstances, the Court of Appeal was entitled to look at the record and conclude that the trial judge's findings regarding mitigation were not available to him on the evidence. The evidence of the Ballantry purchases, in the context of Southcott's refusal to mitigate, established that there were opportunities to mitigate by purchasing other development land in the GTA. Failure to mitigate reduces damages. The Court of Appeal concluded that, based upon the investment properties purchased by Ballantry, and in the absence of evidence to the contrary, the Board discharged the burden of showing that other investment properties were available in the relevant time period to mitigate the losses and that the trial judge's finding that there were no comparable properties was not open to him on the evidence. I agree.

[63] I would dismiss the appeal with costs. In light of the result on the main appeal, I need not consider the cross-appeal. The cross-appeal should be dismissed without costs.

The following are the reasons delivered by

[64] THE CHIEF JUSTICE (dissenting) — Damages for breach of contract may be reduced if the plaintiff unreasonably fails to mitigate its loss. To show that a plaintiff unreasonably failed to mitigate its loss, the defendant who is in breach of the contract must establish: (1) that an opportunity to mitigate the loss existed; and (2) that the plaintiff acted unreasonably in failing to take that opportunity.

[65] The trial judge found as a fact that the defendant had not proved that Southcott had an opportunity to mitigate. This finding, in my view, was grounded in the evidence. This is sufficient to dispose of the appeal. However, if such opportunity were found to exist, I see no basis on which to conclude that Southcott acted unreasonably in maintaining its suit for specific performance instead of mitigating its loss. It follows, in my view, that the judgment of the Court of Appeal should be set aside, and the trial judge's conclusion that the plaintiff established breach of contract and damages should be restored.

I. Background

[66] The Toronto Catholic District School Board contracted with Southcott Estates Inc. for the sale of 4.78 acres of surplus land for $3.44 million. The closing date was August 31, 2004. Southcott was a wholly owned subsidiary of Ballantry Homes Inc.,

which was in the business of buying property and developing it for residential purposes. Southcott was a single-purpose company created expressly and only for the purpose of buying this parcel of land and developing it with single-family homes. Southcott had no assets except for the deposit it paid on the land.

[67] The land was part of a larger parcel on which school buildings were located so the agreement was conditional upon the Board obtaining a severance from the Committee of Adjustments on or before the closing date. The agreement was signed on June 14, 2004, but only became firm on August 23, 2004. The Board, realizing it might not be able to get severance of the property by the closing date of August 31, 2004, asked Southcott to extend the closing date to a fixed date after severance. Southcott was willing to extend the August 31 closing date, but insisted on a firm final date of January 31, 2005.

[68] The Board's application for severance was heard on December 16, 2004. It was deferred because the Board had failed to include a development plan in its application. This made it impossible for the Board to comply with the January 31, 2005 closing date. Southcott requested the Board to extend the closing date. The Board refused this request, declared the transaction to be at an end, and returned Southcott's deposit.

[69] Southcott took the position that the Board had breached its obligation to use its best efforts to obtain the severance and brought an action for specific performance or, in the alternative, damages.

[70] The trial judge held that the plaintiff was not entitled to an order for specific performance because the property was not sufficiently unique to satisfy the requirements of that remedy. However, he awarded damages in the amount of $1,935,500, representing the loss of a 60 percent chance to make profits in the amount of $3,225,827. He rejected the Board's argument that Southcott had failed to act reasonably to mitigate its loss, holding that the Board had not established as a matter of fact that mitigation opportunities were available.

[71] The Court of Appeal reversed the trial judge's decision and set aside the award for damages, essentially holding that the evidence, properly viewed, established an unreasonable failure to mitigate.

II. The Requirements of Mitigation

[72] The doctrine of mitigation holds that a plaintiff cannot recover damages for loss that could have been reasonably avoided: *Asamera Oil Corp. v. Sea Oil & General Corp.*, 1978 CanLII 16 (SCC), [1979] 1 S.C.R. 633, at p. 660; *British Westinghouse Electric and Manufacturing Co. v. Underground Electric Railways Company of London, Ltd.*, [1912] A.C. 673 (H.L.), at p. 689; *Dunkirk Colliery Co. v. Lever* (1878), 9 Ch. D. 20 (C.A.), at p. 25. A plaintiff is not contractually obliged to mitigate, and in this sense the term "duty to mitigate" is misleading. However, if the plaintiff unreasonably fails to mitigate, its damages for breach of contract may be reduced: *Janiak v. Ippolito*, 1985 CanLII 62 (SCC), [1985] 1 S.C.R. 146, at pp. 166-67; *Darbishire v. Warran*, [1963] 1 W.L.R. 1067 (C.A.), at p. 1075.

[73] The defendant, having breached the contract, bears the onus of proving that the plaintiff unreasonably failed to mitigate its loss: *Red Deer College v. Michaels*, 1975 CanLII 15 (SCC), [1976] 2 S.C.R. 324, at pp. 330-31; *Roper v. Johnson* (1873), L.R. 8 C.P. 167. This entails establishing, on a balance of probabilities: (1) that opportunities to mitigate the loss were available to the plaintiff; and (2) that the plaintiff unreasonably failed to pursue these opportunities.

[74] Failure to mitigate may not be unreasonable for a variety of reasons. One such reason may be a "fair, real, and substantial justification" for claiming specific performance: *Asamera*, at pp. 667-68. Another may be lack of financial resources: *McGregor on Damages* (18th ed. 2009), at para. 7-088. The rules for mitigation "do not require the injured party to do what he cannot afford to do when he is seeking to reduce the damages payable by the wrongdoer": *Lagden v. O'Connor*, [2003] UKHL 64, [2004] 1 All E.R. 277, at para. 51 (*per* Lord Hope); see also *General Securities Ltd. v. Don Ingram Ltd.*, 1940 CanLII 28 (SCC), [1940] S.C.R. 670.

[75] Unreasonable failure to mitigate loss reduces damages to the extent that mitigation would have avoided the loss: see *Andros Springs v. World Beauty*, [1970] P. 144 (C.A.), at p. 154 (*per* Lord Denning). If a mitigation opportunity would only partially avoid the plaintiff's loss, then only a partial reduction in damages can be justified.

III. Opportunity to Mitigate

[76] The trial judge found that the Board had not discharged its onus of proving that Southcott unreasonably failed to mitigate its loss because it did not establish that the opportunity to mitigate existed. This finding must stand unless it constitutes palpable and overriding error: *Housen v. Nikolaisen*, 2002 SCC 33 (CanLII), 2002 SCC 33, [2002] 2 S.C.R. 235, at para. 10.

[77] The Board sought to prove that mitigation opportunities existed in two ways — through the testimony of an expert witness and with evidence of purchases made by other Ballantry companies.

A. *The Evidence of the Expert Witness*

[78] The trial judge found that the Board's expert witness's evidence did not establish opportunity to mitigate the loss.

[79] The Board's expert presented evidence of 81 parcels of raw land and 49 subdivided properties that were purchased in the Greater Toronto Area ("GTA") between January 31, 2005 and the time of trial. The trial judge found a number of shortcomings in this evidence.

[80] First, there was no evidence that the alleged properties the expert referred to were actually available to Southcott; the Board's expert witness admitted to being entirely

unaware of whether substitute property was available to the public for sale during the period in which the Board suggested that Southcott could mitigate (A.R., at p. 233).

[81] Second, the evidence did not establish that these properties were comparable to Southcott's target property ((2009), 78 R.P.R. (4th) 285, at para. 144). Little was known about the properties identified by the Board's expert witness beyond their size, cost, and nearest major intersection. Most were outside the City of Toronto. The properties vary widely in both size and price, including parcels as large as 123.988 acres, as small as 0.251 acres, and costing as much as $23.77 million. The trial judge concluded that the comparability of these properties to Southcott's 4.78 acre target property had not been established.

[82] Third, the trial judge found that the evidence did not establish that alternate properties could have been profitably developed (para. 144). Only a profitable development would mitigate Southcott's loss; an unprofitable one would aggravate it. A plaintiff is not required to take foolish steps that would not reduce its loss. The Board's expert presented no evidence on the potential profitability of the properties he referred to.

[83] The Court of Appeal criticized the trial judge's finding that the evidence did not establish profitability, on the ground that he raised the burden of proof on the Board to an unrealistic level 2010 ONCA 310 (CanLII), (2010 ONCA 310, 104 O.R. (3d) 784, at para. 25). With respect, the burden was clear — the Board had to establish that alternate properties could have been profitably developed on a balance of probabilities. There is no indication that the trial judge failed to appreciate this basic principle. See *World Beauty*, at p. 154.

[84] The trial judge found that the Board's expert witness failed to establish that Southcott had opportunities to mitigate its loss. This finding finds support in the evidence and is not vitiated by legal error. It follows that it cannot be set aside: *Housen*.

B. *The Evidence of Purchases by Other Ballantry Companies*

[85] The second way the Board sought to discharge its onus of showing opportunity to mitigate was by evidence that other Ballantry companies had made purchases of development land in the GTA at the relevant time. The Board argued that these other Ballantry purchases had in fact mitigated the loss caused by the Board's breach.

[86] The trial judge accepted the Board's invitation to consider the matter from the perspective of the Ballantry Group as a whole, effectively piercing the corporate veil. He concluded that Ballantry's subsequent purchases were collateral, independent transactions that could not have avoided the loss arising from the Board's breach of contract (para. 143): see *Apeco of Canada, Ltd. v. Windmill Place*, 1978 CanLII 186 (SCC), [1978] 2 S.C.R. 385, at p. 389. Leaving aside the question of whether piercing the corporate veil in these circumstances was appropriate, the trial judge's analysis was not in error. The trial judge's reasoning was that the Ballantry Group, with extensive access to credit, was limited only by the number of properties it could find. The more good

properties it could find, the more money it stood to make. In this sense, other purchases by the Ballantry Group were collateral rather than substitutions for the Board's property.

[87] The trial judge, having dealt with the purchases of other Ballantry companies in this way, did not make a finding on whether these properties offered mitigation opportunities for Southcott, as an independent legal entity. The evidence, however, does not support such a finding, in my view. First, there was no evidence that the properties purchased by other Ballantry companies were available to Southcott. At best, Southcott would have been competing with its sister companies for these properties. Whether it would have succeeded in acquiring a comparable property was a matter of speculation.

[88] Second, the evidence did not establish that other Ballantry Group purchases were comparable to Southcott's target property. Under its contract with the Board, Southcott was purchasing a 4.78 acre parcel located in a desirable residential neighbourhood of the City of Toronto suited to the development of 48 semi-detached residential units (para. 132). There was no evidence that any of the other Ballantry purchases were comparable. It is not enough to show that some development land may have been available to companies which may have had different development strategies. Ballantry had wide ranging interests in residential real estate development throughout the GTA. Southcott had a narrower, specific development objective. To show opportunity to mitigate, the Board had to prove that a property comparable to the one that Southcott sought to purchase was available.

[89] I respectfully cannot agree that two of the subsequent Ballantry purchases were clearly comparable to Southcott's target property (Karakatsanis J., at para. 56). The first (a parcel of 2.7 acres for $3.3 million) was 43 percent smaller than Southcott's target property, cost 70 percent more per acre, and was purchased for the development of a retirement home. The second (a parcel of 2.3 acres for $6 million) was 51 percent smaller than Southcott's target property, cost 260 percent more per acre, and was purchased for development of a high rise building. On the record, these properties were not comparable to the property that Southcott sought to acquire: a 4.78 acre parcel suited to the development of 48 semi-detached residential units. The remaining Ballantry purchases were even less comparable to Southcott's target property. The Board had the burden of establishing the comparability of these properties. It failed to do so.

[90] I see no error in the trial judge's conclusion that the evidence as to other Ballantry properties did not establish opportunities to mitigate the loss suffered as a result of the Board's breach of contract.

IV. Did Southcott Act Reasonably?

[91] The trial judge's finding that the Board failed to establish that Southcott had opportunities to mitigate its loss is sufficient to dispose of the appeal. However, I offer the following comments on whether the Board established, as it was also required to do, that failure to take advantage of any proven opportunities for mitigation was unreasonable.

[92] In my view, it is difficult to conclude that Southcott acted unreasonably. The first reason is that it had a "fair, real, and substantial justification" for claiming specific

performance of the contract: *Asamera*, at pp. 667-68. In such circumstances, a plaintiff is not required to mitigate. As explained in *Asamera*, this is simply an application of the rule of mitigation requiring the plaintiff to act reasonably in the circumstances:

> Where those circumstances reveal a substantial and legitimate interest in seeking performance as opposed to damages, then a plaintiff will be able to justify his inaction and on failing in his plea for specific performance might then recover losses which in other circumstances might be classified as avoidable and thus unrecoverable . . . . [pp. 668-69]

[93] The act of filing a claim for specific performance is inconsistent with the act of acquiring a substitute property. A plaintiff, acting reasonably, cannot pursue specific performance and mitigate its loss at the same time. It makes no sense for a reasonable plaintiff seeking specific performance to effectively concede defeat and buy a substitute property. The plaintiff could end up with two properties — one it wanted and one it did not. Furthermore, an action for specific performance is often motivated by the unavailability of substitutes in the marketplace. A plaintiff's reasonable claim that substitutes are unavailable is inconsistent with the ability to acquire a substitute in the marketplace (E. Yorio, "A Defense of Equitable Defenses" (1990), 51 *Ohio St. L.J.* 1201).

[94] In the end, the trial judge dismissed the claim for specific performance. However, that does not mean that Southcott acted unreasonably in pursuing the claim. Whether a plaintiff had a "fair, real, and substantial justification" for maintaining a specific performance claim is a different question from whether specific performance should be granted at the conclusion of the trial when all the evidence is in and appraised by the trial judge. Plaintiffs can never be certain that an action for specific performance will succeed, particularly as this is an equitable, discretionary remedy. Demanding that losses be mitigated unless success in obtaining specific performance is assured would deter valid claims for specific performance and hold plaintiffs to an impossible standard.

[95] The trial judge, while ultimately rejecting Southcott's claim for specific performance, did not find that Southcott acted unreasonably in pursuing that remedy. Nor does there appear to be a basis for such a finding. It can be fairly argued that Southcott did not act unreasonably in pursuing specific performance of the contract. The property was uniquely suited to Southcott's needs for single-family residential development within the City of Toronto. Though the common law presumption of the uniqueness of real property no longer holds, a claim for specific performance may still be reasonable if a property has unique characteristics such that a substitute property is not readily available: *Semelhago v. Paramadevan*, 1996 CanLII 209 (SCC), [1996] 2 S.C.R. 415, at para. 22. Southcott's contention that there was no comparable substitute property found support in the evidence.

[96] Another reason for failing to acquire and develop a substitute property, assuming such a property had been available, is that Southcott lacked financial resources. Southcott did not have the financial capacity to go into the market and purchase a substitute property. It was a single-purpose company with no assets other than the $344,000 advanced to it by Ballantry for the deposit on the target property (trial judgment, at para. 137). Whether it could have obtained financing to buy a different property is at the very least speculative.

[97] In summary, I see no basis for concluding that Southcott acted unreasonably in failing to mitigate its loss, assuming that opportunities to do so were available.

V. Conclusion

[98] I see no basis upon which to set aside the trial judge's conclusion that the defendant did not prove that the plaintiff unreasonably failed to mitigate its loss. His conclusions find support in the evidence and the law.

[99] I would allow the appeal and restore the judgment of the trial judge.

Appeal dismissed with costs. Cross-appeal dismissed without costs, MCLACHLIN C.J. *dissenting.*

Solicitors for the appellant/respondent on cross-appeal: Lenczner Slaght Royce Smith Griffin, Toronto; Davis Moldaver, Toronto.

Solicitors for the respondent/appellant on cross-appeal: Miller Thomson, Toronto.

NORTH ATLANTIC REFINING LIMITED
P. O. BOX 40, COME BY CHANCE, NF A0B 1N0
TEL: (709) 463-8811 FAX: (709) 463-8076

Proposal for Supply of Additional Generation

RFP 000009

Attention: Manager of Materials Management

Materials Management Department
Newfoundland and Labrador Hydro
Hydro Place, 4th Floor
500 Columbus Drive
P.O. Box 12400
St. John's, Newfoundland
A1B 4K7

Newfoundland Gasification
04/09/97

Capital Cost Estimate Summary
(US$000)

Description	Direct Cost	Construction Management	Engineering	Total
Oxygen Plant	$34,000	$500	$1,500	$36,000
Power Generation	100,304	4,000	7,000	111,304
Acid Gas Removal	13,300	700	2,500	16,500
Gasification	49,000	1,200	7,000	57,200
Utilities and Common Facilities	22,300	1,300	4,000	27,600
HV Transmission Line	300	25	24	349
Spare Parts	1,500	0	50	1,550
Startup & Commissioning	4,000	0	0	4,000
Insurance	4,000	0	0	4,000
Newfoundland Construction Adds	15,000	0	0	15,000
Subtotals	243,704	7,725	22,074	273,503
Escalation				8,000
Contingency				13,000
Estimated EPC Price				$294,503

North Atlantic Cogeneration LTD.

Operating Cost Detail
Year 2000 Cost
($000)

O&M Description	
O&M Cost (Power Plant)	$8,145
O&M Cost (Gasifier)	7,576
Consumables & Water	268
Insurance	1,099
Property Tax	134
Administrative and General	1,340
Total Operating Cost	$18,562

North Atlantic Cogeneration LTD.

Capital Cost Estimate Summary
(Can. $000)

Description	Direct Cost	Construction Management	Engineering	Total
Oxygen Plant	$ 47,560	$ 670	$ 2,010	$ 50,240
Power Generation	145,507	5,360	9,380	160,247
Acid Gas Removal	19,822	938	3,350	24,110
Gasification	70,660	1,608	9,380	81,648
Utilities and Common Facilities	29,882	1,742	5,360	36,984
HV Transmission Line	402	34	32	468
Spare Parts	2,010	0	67	2,077
Startup & Commissioning	5,360	0	0	5,360
Insurance	5,360	0	0	5,360
Subtotals	$326,563	$10,352	$29,579	$366,494
Escalation				10,720
Contingency				17,420
Estimated EPC Price				$394,634

(Section 3 IV × 1.4)

P. U. 1(2007)

IN THE MATTER OF the *Public Utilities Act*, (R.S.N.L.) 1990, Chapter P-47 (the "*Act*"), and

AND

IN THE MATTER OF an Application by Newfoundland and Labrador Hydro ("Hydro") for the approval, pursuant to Sections 70, 71 and 75 of the *Act*, of certain rules, regulations and rates pertaining to the supply of electrical power and energy to one of its industrial customers, Aur Resources Inc.

WHEREAS Hydro is a corporation continued and existing under the *Hydro Corporation Act*, is a public utility within the meaning of the *Act* and is subject to the provisions of the *Electrical Power Control Act, 1994;* and

WHEREAS Hydro filed the within Application seeking approval of rates and rules and regulations in relation to the provision of services to Aur Resources Inc., a new Island Industrial Customer of Hydro (the "Application"); and

WHEREAS the Application seeks approval of a service agreement negotiated with Aur Resources Inc. which is consistent with the Service Agreements approved by the Board for the other Island Industrial Customers (the "Other Service Agreements"), except that for 2006 the

demand charge is based on the highest firm demand in the month rather than the year (the "Service Agreement"); and

WHEREAS the Application seeks approval of rates for Aur Resources Inc., which are consistent with the other Island Industrial Customers except that the rates exclude: 1) the Historical Plan Balance portion of the Rate Stabilization Plan ("RSP") that is payable by the other Island Industrial Customers; and 2) a specifically assigned charge until the appropriate specifically assigned charge can be determined with a full cost of service study in a general rate application; and

WHEREAS at the time of filing the Application Hydro provided the consent of Aur Resources Inc., to the making of the Application; and

WHEREAS on January 20, 2006 the Board issued Order No. P.U. 1(2006) approving, on an interim basis, rates for Aur Resources which included the Historical Plan Balance portion of the Rate Stabilization Plan, a specifically assigned charge of $150,000, and a demand charge which for 2006 is based on the highest firm demand in the month; and

WHEREAS on October 31, 2006 Hydro filed an agreement between Hydro, Aur Resources Inc., several other Island Industrial Customers and the Consumer Advocate setting out a consensus that the rates and rules and regulations for Aur Resources Inc., should be approved as proposed in the Application and that any amounts calculated by Hydro pursuant to the interim rates approved by the Board under Order No. P.U. 1(2006) that are in excess of the final rates

approved by the Board should be refunded or credited to Aur Resources Inc., (the "Agreement"); and

WHEREAS on December 15, 2006 Hydro filed letters from Abitibi Consolidated Inc., Stephenville Division and Abitibi Consolidated Inc., Grand Falls Division, the Island Industrial Customers not party to the Agreement, which letters confirm that neither customer objects to the Application being disposed of in accordance with the Agreement; and

WHEREAS by Orders Nos. P.U. 3(2005) and P.U. 12(2005) the Board approved capital monies to be spent by Hydro and to be recovered from Aur Resources Inc., for the engineering and construction of a transmission interconnection for the Duck Pond Mine being developed by Aur Resources Inc.; and

WHEREAS the Board has approved rate schedules and service agreements for each of Hydro's other Island Industrial Customers, which are similar to those proposed for Aur Resources Inc., except in relation to the demand charge for 2006, the Historical Plan Balance and the specifically assigned charge; and

WHEREAS in relation to the demand charge Hydro states in its response to information request PUB 1.0 NLH that the intent of basing the demand charge on firm monthly demand is to provide Aur Resources Inc., with reasonable flexibility during the construction, testing and commissioning processes that it will be undertaking in its first year of receiving power from the Island grid; and

WHEREAS in relation to the exclusion of the Historical Plan Balance of the Rate Stabilization Plan, Hydro states in its response to information request PUB 25 NLH that Aur Resources Inc., should not pay a portion of the Historical Plan Balance primarily on the principle of cost causation, in that all costs being recovered in the Industrial Customer RSP Historic Plan are costs incurred by the Industrial Customer class prior to 2004; and

WHEREAS in relation to the specifically assigned charge, as stated in its response to information request PUB 4.0 NLH, Hydro proposes to exclude the specifically assigned charge until the appropriate specifically assigned charges can be determined in a new test year cost of service study, given that the Board approved 2004 Cost of Service Study contained no specially assigned charges applicable to that customer; and

WHEREAS on October 5, 2006 the Board issued Order No. P.U. 31(2006) setting rates for the Island Industrial Customers in accordance with direction contained in an Order in Council issued pursuant to section 5.1 of the *EPCA*; and

WHEREAS the rates established for Aur Resources Inc. by Order No. P.U. 31(2006), to be consistent with Order No. P.U. 1(2006), should have been stated to be interim but the schedule inadvertently failed to make reference to the fact that the rates were interim; and

WHEREAS on December 14, 2006 the Board issued Order No. P.U. 41(2006) setting interim base rates for all Island Industrial Customers, including rates for Aur Resources Inc., effective January 1, 2007; and

WHEREAS in accordance with the provisions of the RSP and the usual practice, it is anticipated that Hydro will apply in January 2007 for interim approval of the rates arising from the rate stabilization adjustment for Island Industrial Customers effective on consumption on and after January 1, 2007, which will set out specific interim rates for Aur Resources Inc.; and

WHEREAS the Board is satisfied in the circumstances and, in particular in the context of the Agreement filed with the Board in this matter, that rates, rules and regulations for Aur Resources Inc., should be similar to those of the other Island Industrial customers of Hydro except that:

i) for 2006 the demand charge should be based on the highest firm demand in the month;

ii) rates should exclude the historical plan balance of the RSP; and

iii) until a new full cost of service study is completed and reviewed, rates should not include a specifically assigned charge.

IT IS THEREFORE ORDERED THAT:

1. Page 2 of Schedule "A" of PU 31(2006) shall be replaced with the attached page 2 of 2 Schedule "A", attached hereto as Schedule "A", which correctly sets out that the rates established for Aur Resources Inc., in Order No. P.U. 31(2006) are interim.

2. The Board approves, pursuant to section 75 of the *Act*:

   a. Firm and Non-Firm Rates for Aur Resources Inc., attached hereto as Schedule "B", to be effective for consumption on or after January 20, 2006 to and including September 30, 2006;

   b. Firm and Non-Firm Rates for Aur Resources Inc., attached hereto as Schedule "C", to be effective for consumption on or after October 1, 2006 to and including December 31, 2006; and

   c. Refund or credit to Aur Resources Inc., of the difference for 2006 between the rates developed in accordance with the Agreement and those approved in Order No. P.U. 1(2006)

3. The Service Agreement attached hereto as Schedule "D" is approved for the provision of service to Aur Resources Inc.

4. Hydro shall pay the expenses of the Board incurred in connection with this matter.

Dated at St. John's, Newfoundland and Labrador, this 18th day of January 2007.

Robert Noseworthy
Chair & Chief Executive Officer

Darlene Whalen, P.Eng.
Vice-Chair

G. Cheryl Blundon
Board Secretary

Schedule "A"

Order No. P.U. 1(2007)

Issued: January 18, 2007

NEWFOUNDLAND AND LABRADOR HYDRO

INDUSTRIAL – FIRM – INTERIM*

AUR RESOURCES INC.

Rate:

Demand Charge:

The rate for Firm Power, as defined and set out in the Industrial Service Agreements, shall be $6.17 per month per kilowatt of billing demand.

Firm Energy Charge:

Base Rate*	@ 2.675	¢ per kWh
RSP Adjustment	@ 1.223	¢ per kWh
Energy Rate	@ 3.898	¢ per kWh

***Subject to RSP Adjustment:**

RSP Adjustment refers to all applicable adjustments arising from the operation of Hydro's Rate Stabilization Plan, which levelizes variations in hydraulic production, fuel cost, load and rural rates.

Specifically Assigned Charges:

The specifically assigned charges for customer plant in service that is specifically assigned to Aur Resources Inc. shall be $150,000 per annum.

Adjustment for Losses:

If the metering point is on the load side of the transformer, either owned by the customer or specifically assigned to the customer, an adjustment for losses as determined in consultation with the customer prior to January 31 of each year, shall be applied.

General:

Details regarding the calculation and application of these rates are outlined in the Industrial Service Agreements signed with other Members of the Industrial Customer class.
This rate schedule does not include the Harmonized Sales Tax (HST) which applies to electricity bills.

***Replaces page 2 of 2 of Schedule "A" of Order No. P.U. 31(2006), Effective: October 1, 2006.**

Schedule "B"

Order No. P.U. 1(2007)

Issued: January 18, 2007

NEWFOUNDLAND AND LABRADOR HYDRO

INDUSTRIAL – FIRM

AUR RESOURCES INC.

Rate:

Demand Charge:

The rate for Firm Power, as defined and set out in the Industrial Service Agreements, shall be $6.17 per month per kilowatt of billing demand.

Firm Energy Charge:

Base Rate* .....@ 2.675 ¢ per kWh

RSP Adjustment
Current Plan.....@ (0.109) ¢ per kWh
Fuel Rider.....@ 0.640 ¢ per kWh

Total RSP Adjustment .....@ 0.531 ¢ per kWh

Energy Rate.....@ 3.206 ¢ per kWh

***Subject to RSP Adjustment:**

RSP Adjustment refers to all applicable adjustments arising from the operation of Hydro's Rate Stabilization Plan, which levelizes variations in hydraulic production, fuel cost, load and rural rates. Aur Resources Inc. is not subject to the Historic Plan component of the RSP Adjustment.

Adjustment for Losses:

If the metering point is on the load side of the transformer, either owned by the customer or specifically assigned to the customer, an adjustment for losses as determined in consultation with the customer prior to January 31 of each year, shall be applied.

General:

Details regarding the calculation and application of these rates are outlined in the Industrial Service Agreements signed with other Members of the Industrial Customer class.
This rate schedule does not include the Harmonized Sales Tax (HST) which applies to electricity bills.

NEWFOUNDLAND AND LABRADOR HYDRO
INDUSTRIAL – NON-FIRM
AUR RESOURCES INC.

Rate:

Non-Firm Energy Charge (¢ per kWh):

Non-Firm Energy is deemed to be supplied from thermal sources. The following formula shall apply to calculate the Non-Firm Energy rate:

$$\{(A \div B) \times (1 + C) \times (1 \div (1 - D))\} \times 100$$

A = the monthly average cost of fuel per barrel for the energy source in the current month or, in the month the source was last used

B = the conversion factor for the source used (kWh/bbl)

C = the administrative and variable operating and maintenance charge (10%)

D = the average system losses on the Island Interconnected grid for the last five years ending in 2002 (3.21%).

The energy sources and associated conversion factors are:

1. Holyrood, using No. 6 fuel with a conversion factor of 630 kWh/bbl
2. Gas turbines using No. 2 fuel with a conversion factor of 475 kWh/bbl
3. Diesels using No. 2 fuel with a conversion factor of 556 kWh/bbl.

Adjustment for Losses:

If the metering point is on the load side of the transformer, either owned by the customer or specifically assigned to the customer, an adjustment for losses as determined in consultation with the customer prior to January 31 of each year, shall be applied.

General:

Details regarding the calculation and application of these rates are outlined in the Industrial Service Agreements.
This rate schedule does not include the Harmonized Sales Tax (HST) which applies to electricity bills.

Schedule "C"

Order No. P.U. 1(2007)

Issued: January 18, 2007

NEWFOUNDLAND AND LABRADOR HYDRO

INDUSTRIAL – FIRM

AUR RESOURCES INC.

Rate:

Demand Charge:

The rate for Firm Power, as defined and set out in the Industrial Service Agreements, shall be $6.17 per month per kilowatt of billing demand.

Firm Energy Charge:

Base Rate* .....@ 2.675 ¢ per kWh

RSP Adjustment
Current Plan.....@ (0.162) ¢ per kWh
Fuel Rider.....@ 0.457 ¢ per kWh

Total RSP Adjustment .....@ 0.295 ¢ per kWh

Energy Rate.....@ 2.970 ¢ per kWh

***Subject to RSP Adjustment:**

RSP Adjustment refers to all applicable adjustments arising from the operation of Hydro's Rate Stabilization Plan, which levelizes variations in hydraulic production, fuel cost, load and rural rates. Aur Resources Inc. is not subject to the Historic Plan component of the RSP Adjustment.

Adjustment for Losses:

If the metering point is on the load side of the transformer, either owned by the customer or specifically assigned to the customer, an adjustment for losses as determined in consultation with the customer prior to January 31 of each year, shall be applied.

General:

Details regarding the calculation and application of these rates are outlined in the Industrial Service Agreements signed with other Members of the Industrial Customer class.
This rate schedule does not include the Harmonized Sales Tax (HST) which applies to electricity bills.

NEWFOUNDLAND AND LABRADOR HYDRO
INDUSTRIAL – NON-FIRM
AUR RESOURCES INC.

Rate:

Non-Firm Energy Charge (¢ per kWh):

Non-Firm Energy is deemed to be supplied from thermal sources. The following formula shall apply to calculate the Non-Firm Energy rate:

$$\{(A \div B) \times (1 + C) \times (1 \div (1 - D))\} \times 100$$

A = the monthly average cost of fuel per barrel for the energy source in the current month or, in the month the source was last used

B = the conversion factor for the source used (kWh/bbl)

C = the administrative and variable operating and maintenance charge (10%)

D = the average system losses on the Island Interconnected grid for the last five years ending in 2002 (3.21%).

The energy sources and associated conversion factors are:

4. Holyrood, using No. 6 fuel with a conversion factor of 630 kWh/bbl
5. Gas turbines using No. 2 fuel with a conversion factor of 475 kWh/bbl
6. Diesels using No. 2 fuel with a conversion factor of 556 kWh/bbl.

Adjustment for Losses:

If the metering point is on the load side of the transformer, either owned by the customer or specifically assigned to the customer, an adjustment for losses as determined in consultation with the customer prior to January 31 of each year, shall be applied.

General:

Details regarding the calculation and application of these rates are outlined in the Industrial Service Agreements.
This rate schedule does not include the Harmonized Sales Tax (HST) which applies to electricity bills.

Schedule "D"

Order No. P.U. 1 (2007)

Issued: January 18, 2007

THIS SERVICE AGREEMENT made at St. John's, in the Province of Newfoundland and Labrador on the 17th day of January, 2006.

BETWEEN: **NEWFOUNDLAND AND LABRADOR HYDRO**, a corporation and an agent of the Crown constituted by statute, renamed and continued by the Hydro Corporation Act, Revised Statutes of Newfoundland and Labrador, Chapter H-16, (hereinafter called "Hydro") of the first part;

AND **AUR RESOURCES INC.**, a company organized under the laws of the Canada (hereinafter called the "Customer") of the second part.

WHEREAS Hydro has agreed to sell Electrical Power and Energy to the Customer and the Customer has agreed to purchase the same from Hydro according to the Rates set by the Board of Commissioners of Public Utilities for the Province of Newfoundland and Labrador and by the terms of this Agreement;

THEREFORE THIS AGREEMENT WITNESSETH that the parties agree as follows:

ARTICLE 1
INTERPRETATION

1.01 In this Agreement, including the recitals, unless the context otherwise requires,

(a) **"Amount of Power on Order"** means the Power contracted for in accordance with Article 2;

(b) **"Billing Demand"** means the components of the Customer's monthly Power consumption for which Demand charges apply as determined in accordance with Articles 3 and 10;

(c) **"Board"** means the Board of Commissioners of Public Utilities for Newfoundland and Labrador;

(d) **"Demand"** means the amount of Power averaged over each consecutive period of fifteen minutes duration, commencing on the hour and ending each fifteen minute period thereafter and measured by a demand meter of a type approved for revenue metering by the appropriate department of the Government of Canada;

(e) **"Electricity"** includes Power and Energy;

(f) **"Energy"** means the amount of electricity delivered in a given period of time and measured in kilowatt hours;

(g) **"Firm Energy"** means the Energy associated with the Firm Power;

(h) **"Firm Power"** means, except as varied by paragraph 3.02(a) and subject to Clause 3.03, the Demand normally associated with the Amount of Power on Order;

(i) **"Hydro Delivery Points"** means the load side of the 66,000/4160 volt transformer at the Customer's premises at its Duck Pond mine site, or at such other location or locations that Hydro and the customer mutually agree in writing;

(j) **"Interconnection Contribution Agreement"** means that agreement between Hydro and the Customer entered into on the 21st day of March 2005 and as filed with the Board, which sets out the terms and conditions upon which Hydro constructed a transmission interconnection on behalf of the Customer including provisions for the repayment of those costs;

(k) **"Interruptible Demand"** means, that part of a Customer's Demand which exceeds its Power on Order, which may be interrupted, in whole or in part, at the discretion of Hydro, and which is supplied to the Customer in accordance with Clause 5.01;

(l) **"Interruptible Energy"** means the Energy associated with Interruptible Demand determined as that Energy taken in each fifteen-minute interval in which Interruptible Demand is taken and it shall be deemed that in such cases Firm Energy is taken at 100 per cent load factor;

(m) **"Maximum Demand"** means the greatest amount of Power during the appropriate Month or part of a Month, as the case may be, averaged over each consecutive period of fifteen minutes duration commencing on the hour and ending each fifteen minute period thereafter, and measured by a demand meter of a type approved for revenue metering by the appropriate department of the Government of Canada;

(n) **"Month"** means a calendar month;

(o) **"Non-Firm Energy"** means Energy associated with Interruptible Demand;

(p) **"Power"** means the amount of electrical power delivered at any time and measured in kilowatts;

(q) **"Province"** means the the Province of Newfoundland and Labrador;

(r) **"Rate Schedules"** means the schedules of rates that are approved by the Board for the sale and purchase of Power and Energy;

(s) **"Secondary Energy"** means that Energy Hydro is willing to sell, according to Clause 4.01, at a rate approved by the Board and which, if not sold, would be surplus to its needs and likely to result in spillage at one or more of Hydro's hydraulic generating stations;

(t) **"Specifically Assigned Charge"** means the payment made by the Customer in each Month, calculated according to a method approved by the Board, for the use of Specifically Assigned Plant;

(u) **"Specifically Assigned Plant"** means that equipment and those facilities which are owned by Hydro and used to serve the Customer only;

1.02 Hydro and the Customer agree that they are bound by this Agreement and by the agreements and covenants contained in the Rates Schedules. In the event of a conflict between this Agreement and the Rates Schedules, the Rates Schedules shall have priority.

1.03 In this Agreement all references to dollar amounts and all references to any other money amounts are, unless specifically otherwise provided, expressed in terms of coin or currency of Canada which at the time of payment or determination shall be legal tender herein for the payment of public and private debts.

1.04 Words in this Agreement importing the singular number shall include the plural and vice versa and words importing the masculine gender shall include the feminine and neuter genders.

1.05 Where a word is defined anywhere in this Agreement, other parts of speech and tenses of the same word have corresponding meanings.

1.06 Wherever in this Agreement a number of days is prescribed for any purpose, the days shall be reckoned exclusively of the first and inclusively of the last.

1.07 The headings of all the articles are inserted for convenience of reference only and shall not affect the construction or interpretation of this Agreement.

1.08 Any reference in this Agreement to an Article, a Clause, a subclause or a paragraph shall, unless the context otherwise specifically requires, be taken as a reference to an article, a clause, a subclause or a paragraph of this Agreement.

1.09 This Agreement may be executed in two or more counterparts, each of which when so executed shall be deemed to be an original, but all of such counterparts together shall constitute one and the same instrument.

ARTICLE 2
AMOUNT OF FIRM POWER

2.01 Subject to this Agreement, Hydro agrees to deliver to the Customer and the Customer agrees to purchase from Hydro the Amount of Power on Order.

2.02 Subject to Clause 2.06, the Customer shall declare to Hydro in writing, not later than October 1 of each calendar year, its Amount of Power on Order for the following calendar year. Such declarations may provide for an Amount of Power on Order to apply throughout the calendar year, or may provide for one or more successive increases at specified times during the calendar year, but subject to Clause 2.05, may not provide for a decrease other than a decrease to take effect on January 1st of that following calendar year. The Amount of Power on Order shall in no event be greater than 15,000 kilowatts.

2.03 Hydro will supply all future Power requirements requested by the Customer additional to the 15,000 kilowatts provided, however, that the Customer's requests for such additional Power be made upon adequate notice in order that Hydro may make suitable extensions or additions to its system.

2.04 If Hydro cannot fully comply with a declaration of Amount of Power on Order made in accordance with Article 2.02 it will, as soon as practicable and in any event not later than November 1 of the year in which the declaration was made, advise the Customer of the extent to which it can comply. If more than one industrial customer requests an increase in their Amount of Power on Order and Hydro cannot in its judgment provide enough Power to satisfy all of the timely requests it has received, Hydro will offer additional Amounts of Power on Order to the industrial customers who made those requests in such amounts as are prorated in accordance to the quantity of additional Amounts of Power on Order in the timely requests it has received from those customers.

2.05 If the Customer obtains a new source of electric generation such that it can decrease or eliminate the amount of Power it requires from Hydro, then, provided the Customer gives Hydro thirty-six Month's written notice of the reduction, the Customer may reduce or eliminate its Amount of Power on Order and its Billing Demand effective on the date that the new generation is to go into service as indicated in that written notice.

2.06 For the calendar years 2005 and 2006, the Customer shall declare the Amount of Power on Order for the following Month by giving written notice to that effect to Hydro's Energy Control Center not later than noon of the last working day of each Month. Such declarations shall provide for an Amount of Power on Order that shall apply throughout the following Month. The Amount of Power on Order shall in no event be greater than 15,000 kilowatts. In the event that the Customer does not declare an Amount of Power on Order for any Month pursuant to this clause, the Billing Demand for Firm Power for that Month shall be the Customer's Maximum Demand in that Month.

ARTICLE 3
PURCHASE AND SALE OF POWER AND ENERGY

3.01 The sale and purchase of Power and Energy shall be at such prices and upon such terms and conditions as are set out in the Rate Schedules and this Agreement.

3.02 Subject to Clauses 2.05 and 2.06 and Article 10, the Customer's Billing Demands, which shall each be charged at the applicable rates as approved by the Board, shall comprise the following:

(a) the Billing Demand for Firm Power, which in each Month shall be either

(i) the Amount of Power on Order,

(ii) the lesser of 75% of the Amount of Power on Order for the prior calendar year and, the Amount of Power on Order for the prior calendar year less 20,000 kW,

or

(iii) the Maximum Demand taken up to that time in that calendar year less any Interruptible Demand, if applicable,

whichever is greatest; and

(b) the maximum Interruptible Demand for that Month.

3.03 Notwithstanding that the Billing Demand for Firm Power shall have, by operation of Clause 3.02, exceeded the Power on Order declared for that calendar year in accordance with Article 2, Hydro is not obliged to provide any amount of Power in excess of the Power on Order.

3.04 Notwithstanding anything to the contrary herein, the Customer shall pay in each Month its Specifically Assigned Charge, applicable Demand charges, and Energy charges. Its Energy charges shall comprise its Firm Energy and Non-Firm Energy taken in that Month. The Customer shall also pay any amounts due under the Interconnection Contribution Agreement.

ARTICLE 4
SECONDARY ENERGY

4.01 If Hydro has surplus Energy capability and the Customer desires to purchase it, and provided that appropriate metering is in place, Hydro will deliver Secondary Energy to the Customer for use in its electric boilers. The quantity and availability of Secondary Energy shall be determined by Hydro in its sole discretion, however, once declared to be available, Secondary Energy shall remain available for a period of not less than 72 hours. The rate to be paid for Secondary Energy shall be determined by the Board.

ARTICLE 5
INTERRUPTIBLE DEMAND

5.01 The Customer may in any Month take an amount of Interruptible Demand and Energy in addition to the Amount of Power of Order which shall be billed at the Non-Firm Demand and Energy rates approved by the Board. Provided the Amount of Power on Order is equal to or greater than 20,000 kW, the amount of Interruptible Demand and Energy available shall be the greater of 10% of the Amount of Power on Order and 5,000 kW. If the Amount of Power on Order is less than 20,000 kW, the Amount of Interruptible Demand and Energy available shall be 25% of the Amount of Power on Order. If Hydro is willing and able to serve the Customer's Interruptible Demand, then the following shall apply:

(a) The Customer shall, if practicable, make a prior request for, or otherwise as soon as practicable notify Hydro of its requirement, specifying the amount and duration of its Interruptible Demand requirements. Such request or notification may be made by telephone and confirmed by facsimile transmission to Hydro's officials at its Energy Control Centre, who shall advise the Customer if such Interruptible Power will be made available.

(b) If serving the Customer's Interruptible Demand would result in Hydro generating from, or increasing or prolonging generation from a standby or emergency energy source, then Hydro will so advise the Customer. If the Customer wishes to purchase

Interruptible Demand and Energy at such a time or times, that Power and Energy shall be charged for as calculated by the method or formula approved by the Board.

(c) Notwithstanding anything contrary herein, if service of the Interruptible Demand is disrupted by Hydro or is curtailed by the Customer as a decision to reject the more expensive standby or emergency energy source (which for the purposes of this clause shall be deemed to be a reduction of Hydro of Interruptible Demand), the Billing Demand for Interruptible Power for the Month shall be determined as follows:

(i) If there is a total interruption of Interruptible Demand and Interruptible Energy by Hydro for a whole Month, the Customer shall not be required to make any payment for Interruptible Demand and Energy that Month.

(ii) If there is a total interruption of Interruptible Demand for part of a Month, the Billing Demand for that Interruptible Demand for that Month shall be reduced by a number of kilowatts bearing the same ratio to that Billing Demand as the number of hours during which the interruption occurs bears to the total number of hours in that Month.

(iii)If Hydro requires a reduction of Interruptible Demand for a whole Month, then, the reduced Billing Demand for Interruptible Demand for that Month shall be substituted for the Billing Demand for Interruptible Demand for the same Month, when determining the price of Power and Energy for that Month.

(iv)If Hydro requires the reduction of Interruptible Demand for part of a Month, then, subject to subparagraph (v) of this paragraph 5.01(c), there shall, when determining the price of Interruptible Power and Energy for the Months in which the reduction occurs, be substituted for the Billing Demand for Interruptible Demand for that Month, the number of kilowatts obtained by adding

(a) the reduced Billing Demand for Interruptible Demand for the part of the month during which the reduction was made, averaged over the whole of that Month;

to

(b) the Billing Demand for Interruptible Demand for the part of the Month during which no reduction was made, averaged over the whole of that Month.

(v) In any case arising under subparagraph (iii) or subparagraph (iv) of this paragraph 5.01(c), where a reduction of Interruptible Demand is made for a whole Month or part thereof and the Maximum Demand for Interruptible Demand over that same period is greater than the reduced Billing Demand for Interruptible Demand for that same period, then, instead of that reduced Billing Demand, that Maximum Demand for such period shall be substituted for the Billing Demand for Interruptible Demand for that period when determining the price of Power and Energy for the Month in which the reduction occurs, but, if in any period during which a reduction occurs, the Maximum Demand for Interruptible Demand is less than the reduced Billing Demand for Interruptible Demand, no account shall be taken of that Maximum Demand.

ARTICLE 6
CHARACTERISTICS OF POWER SERVICE AND POINTS OF DELIVERY

6.01 The Power and Energy to be supplied under this Agreement will be delivered to the Customer at three (3) phase alternating current having a normal frequency of sixty (60) cycles and at a voltage of approximately 69,000 volts and delivery will be made at the Hydro Delivery Points.

6.02 Hydro will exercise its best endeavours to limit variation from the normal frequency and voltage to tolerable values.

ARTICLE 7
POWER FACTOR

7.01 The Customer agrees to take and use the Power contracted for in this Agreement at a power factor of not less than ninety percent (90%) lagging at the point of delivery specified in this Agreement.

7.02 Should the power factor be consistently less than ninety percent (90%) lagging, the Customer, upon written notification from Hydro, agrees to install suitable corrective equipment to bring the power factor to a minimum of ninety percent (90%) lagging.

7.03 If the Customer should install static condensers to correct the lagging power factor, the equipment shall be so installed that it can be completely disconnected at the request of Hydro.

ARTICLE 8
METERING

8.01 The metering equipment and meters to register the amount of Demand and Energy to be taken by the Customer under this Agreement shall be furnished by Hydro and if required to be located on the Customer's premises will be installed by Hydro in a suitable place satisfactory to Hydro and provided by the Customer, and in such manner as to register accurately the total amount of Demand and Energy taken by the Customer under this Agreement.

8.02 If the metering is installed on the low voltage side of transformers that are Specifically Assigned Plant or owned by the Customer, an appropriate adjustment will be made to account for losses in the transformers.

8.03 The Customer shall have the right, at its own expense, to install, equip and maintain check meters adjacent to the meters of Hydro.

8.04 Authorized employees of Hydro shall have the right of access to all such meters at all reasonable times for the purpose of reading, inspecting, testing, repairing or replacing them. Should any meter fail to register accurately, Hydro may charge for the Demand and Energy supplied during the period when the registration was inaccurate, either,

(a) on the basis of the amount of Demand and Energy charged for

(i) during the corresponding term immediately succeeding or preceding the period of alleged inaccurate registration, or

(ii) during the corresponding term in the previous calendar year; or

(b) on the basis of the amount of Demand and Energy supplied as established by available evidence,

whichever basis appears most fair and accurate.

ARTICLE 9
LIABILITY FOR SERVICE

9.01 Subject to the provisions of the Rate Schedules and this Agreement, the Power and Energy herein contracted for will be made available for use by the Customer

during twenty-four (24) hours on each and every day of the term of this Agreement.

9.02 The obligation of Hydro to furnish Power and Energy under this Agreement is expressly subject to all accidents or causes that may occur at any time and affect the generation or transmission of such Power and Energy, and in any such event, but subject to Clause 9.03, Hydro shall have the right in its discretion to reduce or, if necessary, to interrupt the supply of Power and Energy under this Agreement.

9.03 Hydro agrees to take all reasonable precautions to prevent any reduction or interruption of the supply of Power and Energy or any variation in the frequency or voltage of such supply, and whenever any such reduction, interruption or variation occurs, Hydro shall use all reasonable diligence to restore its service promptly.

9.04 (1) Subject to Clause 9.04(2) hereof, Hydro shall be liable for and in respect of only that direct loss or damage to the physical property of the Customer caused by any negligent act or omission of Hydro its servants or agents. Customer agrees that for the purpose of this Clause 9.04, "direct loss or damage to the physical property of the Customer" shall not be construed to include damages for inconvenience, mental anguish, loss of profits, loss of earnings or any other indirect or consequential damages or losses.

9.04 (2) Hydro's liability under subclause 9.04(1) applies only when the direct loss or damage to the Customer arising from a single occurrence exceeds the sum of $100,000.00. In no event shall the liability of Hydro exceed the sum of $1,000,000.00 for any single occurrence.

9.04 (3) Customer further agrees that any damages to which it may be entitled pursuant to clause 9.04(1) shall be reduced to reflect the extent to which such losses or damages could reasonably have been reduced if the Customer had taken reasonable protective measures.

9.05 Hydro shall have the right, temporarily to interrupt its service hereunder in order to maintain or make necessary changes to its system, but, except in cases of emergency or accident, the service shall be interrupted only at such time or times as will be least inconvenient to the Customer, and Hydro shall use all reasonable diligence to complete promptly such repairs or necessary changes.

ARTICLE 10
REDUCED BILLING DEMAND

10.01 If at any time during the term of this Agreement the operation of the works of either party is suspended in whole or in part by reason of war, rebellion, civil disturbance, strikes, serious epidemics, fire or other fortuitous event, then, such

party will not be liable to the other party to purchase or, as the case may be, to supply Power and Energy hereunder until the cause of such suspension has been removed and in every such event, the party whose operations are so suspended shall use all reasonable diligence to remove the cause of the suspension.

10.02 (1) For the purposes of this Clause 10.02 the expression "reduced Billing Demand" means the number of kilowatts to which the Billing Demand is reduced in any of the circumstances referred to in subclauses (2) or (3) of this Clause 10.02.

(2) If the Customer is prevented from taking an amount of Power because of a suspension of its operations due to a reason listed in Clause 10.01, and any such interruption or reduction lasts for one hour or longer, then Hydro shall, on the request of the Customer, allow a proportionate reduction of the Billing Demand as calculated pursuant to subclauses (4) through (9) of this Clause 10.02, provided however that, except for reduced Billing Demands that occur pursuant to paragraphs 10.02(4)(b) or (c), in no such case shall the Billing Demand be reduced below 0.85 of the Amount of Power on Order unless Hydro is unable to deliver Power and Energy in accordance with this Agreement.

(3) If the supply of Power and Energy by Hydro is interrupted or reduced for any of the reasons referred to in Clause 9.02, 9.05 or 10.01, and any such interruption or reduction lasts for one hour or longer, then Hydro shall, on the request of the Customer, allow a proportionate reduction of the payment as calculated pursuant to subclauses (4) through (9) of this Clause 10.02.

(4) For those times when the Customer is prevented from taking an amount of Power because the Customer's mining or milling operations are suspended or curtailed due to a strike by the employees of the Customer, the Customer's Billing Demand shall be calculated as follows:

(a) for the first 15 days of the strike and for that portion of the strike which exceeds 120 days, the Billing Demand shall be determined in the manner set out in subclauses (5) to (9) of this clause 10.02;

(b) for those whole Months during the period that commences following the first 15 days of the strike and ends not later than 120 days after the strike began, the reduced Billing Demand shall be the Customer's Maximum Demand (less any applicable Compensation Demand), in those Months;

(c) for those part Months that comprise periods that include;

(i) a period that commences following the first 15 days of the strike and ends not later than 120 days after the strike began,

together with one or both of

(ii) a period when the Customer is not affected by a strike or other suspension of its operations due to a reason listed in Clause 10.01,

and

(iii) a period where a strike has continued in excess of 120 days, or where the Customer is affected by any other suspension of its operations due to a reason listed in Clause 10.01,

the Customer's Billing Demand shall be determined by adding

(iv) the Maximum Demand for the part of the Month described in subparagraph (i) averaged over the whole of the Month,

(v) the greater of the Maximum Demand for Firm Power and the Amount of Power on Order for the part of the Month described in subparagraph (ii), if any, averaged over the whole of the Month

and

(vi) the reduced Billing Demand applicable to the period described in subparagraph (iii) averaged over the whole of the Month.

(5) If there is a total interruption of the supply of Power and Energy by Hydro for a whole Month, the Customer shall not be required to make any payment for that Month.

(6) If there is a total interruption of Power for part of a Month, the Billing Demand for that Month shall be reduced by a number of kilowatts bearing the same ratio to that Billing Demand as the number of hours during which the interruption occurs bears to the total number of hours in that Month.

(7) If the reduction of Power is made for a whole Month, then, subject to clause (9) of this Clause 10.02, the reduced Billing Demand for that Month shall be substituted for the Billing Demand for the same Month, when determining the price of Power and Energy for that Month.

(8) If the reduction of Power is made for part of a Month, then, subject to subclause (9) of this Clause 10.02, there shall, when determining the price of Power and Energy for the Months in which the reduction occurs, be substituted for the Billing Demand for that Month, the number of kilowatts obtained by adding

(a) the reduced Billing Demand for the part of the month during which the reduction was made, averaged over the whole of that Month;

to

(b) the Billing Demand for the part of the Month during which no reduction was made, averaged over the whole of that Month.

(9) In any case arising under subclause (7) or subclause (8) of this Clause 10.02, where a reduction of Power is made for a whole Month or part thereof and the Maximum Demand for that same period is greater than the reduced Billing Demand for that same period, then, instead of the reduced Billing Demand, the Maximum Demand for such period shall be substituted for the Billing Demand for that period when determining the price of Power and Energy for the Month in which the reduction occurs, but, if in any period during which a reduction occurs, the Maximum Demand is less than the reduced Billing Demand no account shall be taken of that Maximum Demand.

(10) Where a Billing Demand, a reduced Billing Demand or a Maximum Demand for a part of a Month is to be averaged for the whole of that Month in accordance with subclause (8) of this Clause 10.02, the averaging shall be done by dividing the Billing Demand, the reduced Billing Demand or the Maximum Demand, as the case may be, by the total number of hours in the whole of that Month and multiplying the result by the number of hours to which the Billing Demand, the reduced Billing Demand or the Maximum Demand relates.

(11) In addition to the reductions in Billing Demand that may be made in accordance with this Article 10, Hydro may, in its sole judgment and discretion, make other Billing Demand adjustments from time to time to

decrease the Customer's bill to reflect unusual or unanticipated conditions or to facilitate the testing of equipment or processes by the Customer.

ARTICLE 11
CONSTRUCTION OR INSTALLATION OF TRANSMISSION LINES OR APPARATUS

11.01 For the consideration aforesaid, the Customer hereby grants to Hydro the right to construct transmission lines and accessory apparatus on locations approved by the Customer on, under or over the property of the Customer for the purpose of serving the Customer and the other customers of Hydro, together with the right of access to the property of the Customer at all times for the construction of such lines and apparatus and for the repair, maintenance and removal thereof, provided that nothing in this clause shall entitle Hydro to construct transmission lines and accessory apparatus on or over the Customer's property if such transmission lines are not directly connected with the Customer's premises or some part thereof.

11.02 The Customer shall not erect any building, structure or object on or over any right-of-way referred to in Clause 11.01 without the written approval of Hydro, but subject to that limitation the Customer shall be entitled to make fair and reasonable use of all lands subjected to the said right-of-way.

11.03 Any changes that the Customer may request Hydro to make in the location of any lines or apparatus constructed pursuant to Clause 11.01 shall be made by Hydro, but the Customer shall bear the expense of any such changes to the extent that such lines or apparatus supply Power to the Customer.

11.04 All transmission lines and apparatus of Hydro furnished and installed by it on the Customer's premises shall remain the property of Hydro, and Hydro shall be entitled to remove such transmission lines and apparatus on the expiry or termination of this Agreement.

11.05 For the purpose of using the power service of Hydro, the Customer shall install properly designed and suitable apparatus in accordance with good engineering practice, and shall at all times operate and maintain such apparatus so as to avoid causing any undue disturbance on the system of Hydro, and so that the current shall be approximately equal on all three of its phases.

11.06 If, at any time, the unbalance in current between any two of its phases is, in the judgment of Hydro, excessive to a degree that the power supply system of Hydro

and/or the electrical equipment of any other customer of Hydro is adversely affected, then it shall be the responsibility of the Customer to take such reasonable remedial measures as may be necessary to reduce the unbalance to an acceptable value.

11.07 If, at any time during the term of this Agreement, Hydro desires to improve the continuity of power service to any of its customers, Hydro and the Customer will co-operate and use their best endeavours to carry out the improvements either by changes to existing equipment or additions to the original installations of either Hydro or the Customer.

11.08 The Customer shall not proceed with the construction of or major alterations of its equipment or structures associated with any terminal substation at which Power and Energy is being delivered until Hydro is satisfied that the proposals for such construction or alteration are in accordance with good engineering practice and the laws and regulations of the Province, provided that any examination of the Customer's proposals by Hydro shall not render Hydro responsible in any way for the construction or alteration proposed, even if electrical connection is made by Hydro, whether or not any changes suggested by Hydro shall have been made by the Customer.

ARTICLE 12
RESPONSIBILITY FOR DAMAGES

12.01 Beyond the point of delivery, the Customer shall indemnify and hold Hydro harmless with respect to any and all claims that may be made for injuries or damages to persons or property caused in any manner by electric current or by the presence or use on the Customer's premises of electric circuits or apparatus, whether owned by Hydro or by the Customer, unless and to the extent that such injuries or damages are caused by negligence on the part of the employees of Hydro.

12.02 Up to the point of delivery, Hydro shall indemnify and hold the Customer harmless with respect to any and all claims that may be made for injuries or damages to persons or property caused in any manner by electric current or by the presence or use on the Customer's premises of electric circuits or apparatus owned by Hydro and resulting from or arising out of the negligence of Hydro's employees or other persons for whom Hydro would in law be liable, unless and to the extent that such injuries or damages are caused by negligence on the part of the employees of the Customer.

12.03 If any of the transmission lines or apparatus installed by Hydro on the Customer's premises should be destroyed or damaged by the negligence of the Customer, its servants or agents, the Customer shall reimburse Hydro for the cost of their replacement or repair.

ARTICLE 13
PAYMENT OF ACCOUNTS AND NOTICE OF CLAIMS OF CUSTOMER

13.01 Hydro will render its accounts monthly and the Customer shall, within twenty (20) days after the date of rendering any such account, make payment in lawful money of Canada at the office of Hydro in St. John's, Newfoundland, or in such other place in the said Province as Hydro may designate, without deduction for any claim or counterclaim which the Customer may have to claim to have against Hydro arising under this Agreement or otherwise.

13.02 All amounts in arrears after the expiration of the period of twenty (20) days referred to in Clause 13.01 shall bear interest at the rate of one and one-half (1-1/2%) percent per Month.

13.03 If the Customer is in default for more than thirty (30) days in paying any amount due Hydro under this Agreement, then, without prejudice to its other recourses and without liability therefor, Hydro shall, upon ten (10) days written notice to the Customer of its intention so to do, be entitled to suspend the supply of Power and Energy to the Customer until the said amount is paid, and if the supply is so suspended, the Customer shall not be relieved of its obligations under this Agreement.

13.04 The Customer and Hydro will submit to the other in writing every claim or counterclaim which each may have or claim to have against the other arising under this Agreement within sixty days of the day upon which the Customer or Hydro has knowledge of the event giving rise to such a claim.

13.05 The Customer and Hydro shall be deemed to have waived all rights for the recovery of any claim or counterclaim that has not been submitted to the other party pursuant to and in accordance with Clause 13.04.

ARTICLE 14
ARBITRATION

14.01 If a settlement of any claim made by the Customer in accordance with Clause 13.04 is not agreed to by both parties, the matters in dispute shall be submitted, within three months from the time the claim was submitted, for decision to a board of arbitrators consisting of three members, one to be named by each party

to this Agreement and the third to be named by the two arbitrators so chosen, and the decision of any two members of the board of arbitrators shall be final and binding upon both parties.

14.02 The charges of the third member of a board of arbitrators who shall be the chairman of that board, shall be borne by the losing party, and the parties shall bear the costs or charges of their own appointees. Any arbitration hearing commenced under this Article shall be held in St. John's or such other place as the parties mutually agree.

14.03 If the two appointees of the parties are unable to agree upon the third arbitrator or chairman, the chairman shall be appointed upon application of either party to the Trial Division of the Supreme Court of Newfoundland and Labrador or a judge of that Division.

14.04 The period of delay for appointment by the parties to this Agreement of their respective nominees shall be seven days after notification by the other party to this Agreement of its nominee, and the period for agreement by the two nominees on the chairman shall be ten days.

14.05 The provisions of the Arbitration Act, Chapter A - 14 of the Revised Statutes of Newfoundland and Labrador, 1990, as now or hereafter amended shall apply to any arbitration held pursuant to this Article 14.

ARTICLE 15
MODIFICATION OR TERMINATION OF AGREEMENT

15.01 Except, where otherwise specifically provided in this Agreement and only to the extent so provided, all previous communications between the parties to this Agreement, either oral or written, with reference to the subject matter of this Agreement, are hereby abrogated and this Agreement shall constitute the sole and complete agreement of the parties hereto in respect of the matters herein set forth.

15.02 At any time during the currency of this Agreement, the Customer may terminate it by giving to Hydro two years previous notice in writing of its intention so to do.

15.03 Any amendment, change or modification of this Agreement shall be binding upon the parties hereto or either of them only if such amendment, change or modification is in writing and is executed by each of the parties to this Agreement

by its duly authorized officers or agents and in accordance with its regulations or by-laws.

15.04 Subject to Article 10, if the Customer voluntarily or forcibly abandons its operations, commits an act of bankruptcy or liquidates its assets, then, there shall, forthwith, become due and payable to Hydro by the Customer, as stipulated and liquidated damages without burden or proof thereof, a lump sum equal to:

(a) 0.85 of its then current Billing Demand for Firm Power, at the Firm Power Demand charge, multiplied by 24

plus

(b) any remaining amounts payable pursuant to Article 3 of the Interconnection Contribution Agreement.

ARTICLE 16
SUCCESSORS AND ASSIGNS

16.01 This Agreement shall be binding upon and enure to the benefit of the parties hereto and their respective successors and assigns, but it shall not be assignable by the Customer without the written consent of Hydro.

ARTICLE 17
GOVERNING LAW AND FORUM

17.01 This Agreement shall be governed by and interpreted in accordance with the laws of the Province, and every action or other proceeding arising hereunder shall be determined exclusively by a court of competent jurisdiction in the Province, subject to the right of appeal to the Supreme Court of Canada where such appeal lies.

ARTICLE 18
ADDRESS FOR SERVICE

18.01 Subject to Clauses 18.02 and 18.03, any notice, request or other instrument which is required or permitted to be given, made or served under this Agreement by either of the parties hereto, except for notices or requests pertaining to Interruptible Demand or Secondary Energy, shall be given, made or served in writing and shall be deemed to be properly given, made or served if personally

delivered, or sent by prepaid telegram or facsimile transmission, or mailed by prepaid registered post, addressed, if service is to be made

(a) on Hydro, to

The Corporate Secretary
Newfoundland and Labrador Hydro
Hydro Place
P.O. Box 12400
St. John's, Newfoundland
CANADA. A1B 4K7
FAX: (709) 737-1782
or

(b) on the Customer, to

Aur Resources Inc.
Suite 2501
1 Adelaide Street E
Toronto, Ontario
Canada, M5C 2V9
Attn: Corporate Secretary
FAX: (416)367-0427

18.02 Any notice, request or other instrument given, made or served as provided in Clause 18.01 shall be deemed to have been received by the party hereto to which it is addressed, if personally served on the date of delivery, or if mailed three days after the time of its being so mailed, or if sent by prepaid telegram or facsimile transmission, one day after the date of sending.

18.03 Except for notices for Interruptible Demand or Secondary Energy, whenever this Agreement requires a notice to be given or a request to be made on a Sunday or legal holiday, such notice or request may be given or made on the first business day occurring thereafter, and, whenever in this Agreement the time within which any right will lapse or expire shall terminate on a Sunday or legal holiday, such time will continue to run until the next succeeding business day. Notices or requests pertaining to Interruptible Demand or Secondary Energy may be given and received by and to the appropriate nominees of the respective parties by voice or electronic communication provided that it is confirmed in writing and transmitted or delivered by facsimile, courier or mail as soon as practicable.

18.04 Either of the parties hereto may change the address to which a notice, request or other instrument may be sent to it by giving to the other party to this Agreement

notice of such change, and thereafter, every notice, request or other instrument shall be delivered or mailed in the manner prescribed in Clause 18.01 to such party at the new address.

IN WITNESS WHEREOF Newfoundland and Labrador Hydro and the Customer has each executed this Agreement by causing it to be executed in accordance with its by-laws or regulations and by its duly authorized officers or agents, the day and year first above written.

THE CORPORATE SEAL of **Newfoundland and Labrador Hydro** was hereunder affixed in the presence of:

Witness

Vice President, Regulated Operations

Assistant Corporate Secretary

DULY EXECUTED by **Aur Resources Inc.** in accordance with its Regulations or By-Laws in the presence of:

Witness