

Ms. Cheryl Blundon  
Director of Corporate Services and Board Secretary  
Board of Commissioners of Public Utilities  
120 Torbay Road  
P.O. Box 21040  
St. John's, NL  
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Dear Ms. Blundon:

We are writing to comment on the recently released interim report by the Liberty Consulting Group on supply issues and power outages. We believe this is a good forensic piece of work, focusing principally on maintenance and management practices. The analysis reveals a deep seated problem in our electrical system which calls not only for improved vigilance and better training but also a shift in the corporate culture. The confluence of errors and faults demands remedial action at all levels, along with robust oversight by the Public Utilities Board.

The response by the CEO of Nalcor and NL Hydro is further cause for concern.

"Martin said it (the Liberty Consulting Group Interim Report) does not provide any evidence that an act or omission of by Hydro caused the power problems." (The Telegram, April 26, 2014)

In the same article he also said that when he assumed his present role over seven years ago: "The age of the assets and the asset management processes and the work that was being poured into them for their age was not enough, not acceptable."

Is Mr. Martin saying that, during his watch, the situation has improved?

Our reading of the Liberty Consulting group report does not support his assertion that no act or omission of Hydro caused the power outages and rolling blackouts in January. And it demonstrates that his stewardship of our Hydro assets is not what we have a right to expect from the President and CEO of Newfoundland and Labrador Hydro. It also brings into question the capacity of the management team properly to manage the Muskrat Falls project.

What were the acts or omissions of Hydro identified in the Liberty Consulting Interim Report which lead to the conclusion of the report "that there exists a continuing and unacceptable high risk of of supply-related emergencies until Muskrat Falls and the Labrador-Island Link come into service." (The reliability of the post Muskrat Falls system will be the subject of the fall report by Liberty and the subsequent PUB hearings.)

1. Hydro's planning averages winter conditions. "Given the very large percentage of customers using electric heat, this approach does not give sufficient emphasis to the extreme loads that winter conditions can produce."

2. Hydro seeks to make its generation available by December 1 in each year. "The goal is to complete required maintenance and repairs by the time each winter season begins." The report notes that: "Hydro has not, however, met that goal."
3. With respect to the asset management processes of Hydro the report concluded that the results of those processes during the outages of 2014 and 2013 "call into question the effectiveness of the process."
4. Hydro "has deferred some maintenance, including equipment that failed, required by its established cycles."
5. Hydro's asset management did not take into account the age of equipment. "We found Hydro's maintenance standards more appropriate for a system comprising equipment of "younger" vintage than characterizes Hydro's infrastructure."
6. The report describes the supply planning decisions of Hydro as one "elected to operate close to the edge, which raises the risk of adverse outcomes. In summary, we found that Hydro's practices vis-a-vis reliability standards did influence the supply conditions that contributed to the January 2014 interruptions, indirectly through a culture more tolerant of rotating outages and directly through the long-established reserve criteria and how the company has implemented them."
7. With respect to the Hardwoods CT outage the report concluded: "Failure to require the presence of personnel critical to getting the unit back on line, even recognizing the holiday season, created avoidable risk."
8. The Stephenville CT unit derating (reducing capacity by half) was caused by worn insulating blankets. The report states: "The failure to deal with the blankets, first during the 20-month outage and second with a delayed procurement process, did not demonstrate sufficient concern with respect to the December 1 deadline, and became a contributor to the outage events of 2014."

The Liberty Consulting Group will prepare a final report which will be submitted in the fall to "support general conclusions about the overall effectiveness of management and operations of systems, equipment, and activities necessary for ensuring safe, reliable, and continuous service."

We suspect that report will not be kind to the management of Hydro given what is contained in the Interim Report.

We hope that the next report will also focus on what can be done to improve corporate governance and management of Hydro and will focus on two concerns which we have:

The first is the composition of the Board of Hydro and its parent company, Nalcor. Do the boards have the right mix of expertise and experience to properly supervise management? Should the CEO be a member of the Boards?

The second issue is whether the position of CEO of Hydro should be a full-time position. We understand that the present incumbent spends approximately 10% of his time managing Hydro. We note that Newfoundland Power has a full-time CEO. To what extent did the part-time nature of the position contribute to the reliability issues which we experienced this January? What are the skill sets necessary for the position of CEO of Hydro? Should the incumbent have experience in running a hydro company?

We believe it is important that the next report from the Liberty Group address other resource options on the demand side. This includes conservation and demand side management. These options will likely be less costly than building additional generating capacity. Our utilities have not pursued aggressive demand side management and, indeed, there is little incentive for them to do so. The initiative needs to come from an agency outside of the utilities and it should provide a mechanism whereby ratepayers can invest in home retrofits and alternative power sources without having to incur incremental cost. The conservation agency should be linked with the utilities in such a way that energy savings can be applied to the capital costs, after which there would be a permanent reduction in electric usage.

We also expect that the next report will focus on the reliability of the system, upon interconnection, and the need for additional power, both base power and emergency power, on the Avalon Peninsula. Power reliability is inversely related to the distance between the source and the customer, and that is certainly true for our province, particularly when the line passes through alpine conditions and beneath the iceberg-scoured sea bottom of the Strait of Belle Isle.

The present plan calls for Holyrood to be decommissioned in 2021. We question whether this will be consistent with reliable power and whether reliance upon Nova Scotia for emergency power is adequate. Nalcor has maintained that the Maritime Link with Nova Scotia will provide sufficient access to emergency power and that we will not need to depend upon Holyrood for generation. The reality is that adverse weather conditions tend to influence both provinces concurrently and weather systems have been known to cause serious disruptions to our main transmission lines which could impede access to power from Nova Scotia. The next Liberty report may call for a fundamental reassessment of our base and emergency requirements and may call into question the alleged cost difference between the Interconnected and the Isolated Island options.

With the creation of Nalcor Energy we have witnessed the growth of a crown corporation which combines the worst features of both public and private enterprise. Nalcor has been given greater authority than Newfoundland and Labrador Hydro ever had. It has become a drain on the public Treasury, where NL Hydro once contributed dividends to the Treasury. It has operated as a law unto itself. Its CEO has higher visibility and, apparently more authority, than the Premier, or any Cabinet Minister. It is out of control. Retrogressive amendments to the Electrical Power Control Act, which were passed under the cover of the 2012 Christmas rush and which prohibited other companies from generating power or from using Nalcor's transmission lines to import power from other sources, enhanced its egregious powers and placing our Province out of step with the rest of the Continent, where growing competition is the order of the day.

We need a strong PUB to protect the public interest. The present Liberty Report on the supply outages may be a watershed event in the evolution of regulatory oversight in NL, one which will animate our citizens to demand greater public accountability, through the PUB. The revelations of the present report strongly suggest the need for a reassessment of the role of, and, indeed, the need for, Nalcor, including the prospect of placing it under full PUB oversight, along with NL Hydro. When Newfoundland Power became part of Fortis Inc. the PUB demanded oversight and forensic scrutiny over inter-corporate transactions with other Fortis-owned companies. The Fortis solution, where Newfoundland Power is regulated but not Fortis, is not an adequate solution in this instance, where Nalcor exercises such a pervasive influence, with the ability to make massive capital investments and to control the future of electrical power rates.

There is growing evidence in our Province and elsewhere that crown corporations such as Nalcor, with strong political links, demand a rebalancing of their relationship with the citizens who own but do not control them. Part of this rebalancing is a full audit by the Auditor General of the management failures which allowed this concatenation of problems to occur. A recommendation to Government for such an audit should be made by the Board, on a priority basis, following the submission by the final report of the Liberty Report.

Yours truly,

Ronald Penney

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David Vardy

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