

"Strike While the Iron is Hot"
or
"Waves Come and Go"

Current State of Play

Performance

- High quality private sector CEO, Jim Hankinson, has created a positive direction for NB Power from a financial point of view – 96/97 net of (\$87mm) has increased to a 99/00 net of \$17mm (but what was that \$450mm anyway?)
- Annual debt reduction has gone from \$53mm to \$233mm over the same period
- Out of Province sales went from \$182mm to \$330mm
- Point Lepreau has had improving performance
- However - employee numbers have not changed for the last 5 years (2500)
- Rate increases of approximately 3% per year are closing the gap with some of the regional comparisons, but residential rates continue to be the lowest in the region (but industrial rates?)
- Fuel oil is up significantly, but no increase in electricity rates

Perception

- Things seem OK at present but what is going on under the water
- Government and Management of NB Power don't appear to be on the same page (last rate increase, Lepreau feasibility study, CEO lawsuit)
- What is the future of the current CEO?
- Public had been involved in development of thought on future structure of the electricity industry but things have moved behind closed doors
- Who is making the decisions on Lepreau refurbishment and refiring of Coleson Cove – these are major capital decisions which have significant implications for the future ownership and the financial health of NB Power and for the Province

- Privatization still seems too complicated - witness the problems which have arisen this summer in other jurisdictions

But let's look back...

We can only see where we are going by where we have been. The development of thought on deregulation and privatization of NB Power in the Province of New Brunswick has been largely influenced by outside factors.

The Build

- Worldwide phenomenon of deregulation and privatization of power systems
 - o USA, UK, Australia, New Zealand,
- High valuations paid for existing franchises and assets ('window of opportunity?')
 - o Particularly in the Northeast corridor

Against this background in New Brunswick:

- NB Power was about to begin swimming upstream
 - o For the three fiscal years leading up to 97/98, NB Power had lost \$212 million, made up through the release of historic reserves totaling \$226million (and those reserves were now largely gone)
- Frank McKenna lead the Province with a strong hand on the tiller for 10 years, including some significant steps to outsource Government activities to the Private sector
- Time was ripe to look at privatization
- Under Premier Ray Frenette, the Government released their Discussion Paper – *Electricity in New Brunswick Beyond 2000* and announced the terms of reference for a Special Task Force, Co-chaired by Donald Savoie and me to 'identify options' for the future of electricity in New Brunswick
- July 1998 – the Task Force released "*Electricity in New Brunswick and Options for its future*"
 - o Reading between the lines, there was a distinct 'it is broke' and a suggestion that we should look at new approaches
- November 1998 Select Committee on Energy commences work on electricity

- March 1999 – Premier Camille Theriault in his State of the Province address comments that regardless of the outcome of the Select Committee, NB Power will continue to be owned by New Brunswick
- May 1999 – Select Committee report favours continued ownership of NB Power by the Government but with a move to wholesale competition – it also recommends a functional split of NB Power into three units
- June 1999 – Bernard Lord's Conservative Government elected to office – including Finance Minister Norm Betts – recently described in the Press as '...a man with strong opinions on the virtues of privatization'
- August 1999 – Mactaquac meeting orchestrated by the Government to solicit input from customers, electricity professionals, special interest groups
- Then the music stopped

The Transition

- What happened?
- Government preoccupied with '200 Days of Change' - not the least of which was 'unprivatizing' the toll highway
- Fall 1999 - Question as to which of Minister Betts (Finance and clear understanding of the NB Power issues) or Minister Volpe (Natural Resources and Energy) would lead the charge on NB Power
- Nov 18 1999 - Grant Thornton Report – Under direction of Minister Betts
 - "high priority be given to a reassessment of the governance structure between Government, the Board, and management of NB Power"
- Nov 24 – Minister Volpe says "Everything on the Table for NB Power"
- March 2000 Bangor Daily News
 - "Citing a regional glut of electricity, the primary contractor for the decommissioning of Main Yankee has chosen to waive its option to build and operate a gas-fired generating plant at the site....Under its agreement with Maine Yankee, Stone & Webster had until next September to exercise its option to re-power the

plant. The plan was to build an 800-megawatt station powered by natural gas and sell the output to the New England power pool....In explaining his company's decision to opt out, Moody said there are more than enough generating plants ready to go on line than the market can bear. New England's average demand is about 22,000 megawatts and there are more than 27,000 megawatts available in the New England queue. 'Its obvious to many in the industry,' Moody said, 'that there are going to be some failures among the new plants waiting to go on line. There is just too much supply right now.'

- Spring 2000 - Minister Volpe announces activation of Energy Secretariat reporting to him to prepare a final Energy Policy by Fall 2000
- July 2000 - Leaked TD Securities report urging sale of NB Power – and at the same time, Nova Scotia Power expresses interest in acquisition
- 'Summer of Discontent' in deregulating jurisdictions – well covered in the press:
 - August - National Post – 'Alberta government to go ahead with power auction despite criticism'
 - New York Times – 'Feeling Powerless In a World Of Greater Choice – Consumers Grow More Anxious As They Are Cut Loose In Electricity's New Free Market'
 - Enron – Jeff Skilling, President, 'Summer Power Market Woes To Widen Deregulation Gulf' – 'These developments haven't done much for the reputation of electric deregulation in states that have thus far sat on the sidelines'
 - Globe& Mail – 'Ontario stuck with ugly Non Utility Generation contracts as deregulation hopes fade'
 - Daily Gleaner – 'Energy deregulation has too many unknowns'
 - Daily Gleaner – 'Future of NB Liquor - No privatization plans'
- Privatization wave passed
 - Change in Government

- "Window of opportunity" for premium generating asset sales in Northeast corridor closed as private sector fills the pipe
- Financial position of NB Power was improving (but what about that \$450mm?)
- Deregulation hits execution hiccups in New York, California, Alberta, Ontario during the summer of 2000

The Way Forward

- Imminently awaiting Energy Policy in New Brunswick – Key to way forward
- Decisions on refurbishment at Point Lepreau and Coleson Cove being made behind closed doors - significant implications for the future of the utility
- Don't swim upstream
 - we need to accept realities of the Government, marketplace and electorate sentiment
 - everybody has the same desire: make NB Power responsive to public market pressures to make it more competitive
- Must ensure that our actions or lack of action does not impede our ability to maximize out of province sales – this may be increasingly important when we actively permit co-generation

THOUGHTS

Co-Generation

- While it is possible through an Order-in-Council, no direction or precedent exists within the Province
- Provides real competitive pressure on NB Power
- Exit fee / stranded cost structure, and backup charges must not serve as a mechanism to thwart bona fide co-gen development
- Work needs to be done to strike the right balance

Competitive Position Review Board

- Ontario Government's white paper "Direction For Change" November 1997 stated that:
 - o "Ontario Hydro's problems have continued over a number of years, and are in large part due to the fact that the corporation is a monopoly, and has not been subject to the discipline of the marketplace."

- Concluding that competition would be introduced while Government ownership of Ontario Hydro would be maintained, they said:
 - o "The Government, on behalf of taxpayers, would insist that prudent assumptions are used in investment planning and budgeting, and that tough performance targets are met"

- If we can't privatize and put public market pressure on the enterprise, let's create a body that will do so: Competitive Position Review Board

- Purpose would be to mimic the public market pressures on a non-public company

- Provide resource to the Board to enable it to:
 - Identify comparable utility companies

 - Hire investment bank analyst/consultant to provide a template for public market indicia (kilowatts per employee, revenue per employee, financial targets – perhaps with pro forma financial statements with appropriate capital structures, etc.)

 - Set a plan for NB Power to move towards such goals over a 3 year time frame

 - Make the targets and the process dynamic

 - Provide a variable bonus pool to the CPRB which it would allocate to management based on achievement of goals

- Let's give incentive to management

- Objective is to mimic public market pressures on NB Power to have the benefits of public ownership (costs of capital and tax status) but the performance pressures of the public market
- As we stated in our Task Force Report:
 - "History tells us that governments have not been very successful at reforming their agencies or enterprises from within. Efficiency drives or campaigns only bring at best limited success and this only during the actual period of pressure."
 - An independent, qualified, resource CPRB may provide the necessary backbone
 - Longer term, if the privatization pendulum swings back, NB Power would be much closer to a form which could result in a quick and successful transfer to the private market

NB Power

- NB Power must be part of the solution
- Reticence is counter-productive