

The Consumer Advocate

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February 1, 2019

Via Courier

Board of Commissions of Public Utilities
120 Torbay Road, P.O. Box 2140
St. John's, NL A1A 5B2

**Attention: G. Cheryl Blundon, Director of
Corporate Services / Board Secretary**

Dear Ms. Blundon:

RE: Newfoundland and Labrador Hydro - 2017 General Rate Application

Further to the above-captioned, enclosed please find the original and thirteen (13) copies of the Consumer Advocate's Written Submissions dated February 1, 2019.

Yours truly,



Stephen Fitzgerald
Counsel for the Consumer Advocate

Encl.
/bb

cc **Newfoundland & Labrador Hydro**
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IN THE MATTER OF

the *Electrical Power Control Act, 1994*
SNL 1994, Chapter E-5.1 (the “*EPCA*”)
and the *Public Utilities Act, RSNL 1990*,
Chapter P-47 (the “*Act*”), as amended; and

IN THE MATTER OF a General Rate
Application by Newfoundland and Labrador
Hydro to establish customer electricity rates
for 2018 and 2019; and

To: The Board of Commissioners of Public Utilities (the “Board”)

**CONSUMER ADVOCATE’S
WRITTEN SUBMISSIONS**

FEBRUARY 1, 2019

Dennis Browne, Q.C.

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1 **BACKGROUND**

2

3 On the 28th of July, 2017 Newfoundland and Labrador Hydro (“Hydro”) filed a General Rate
4 Application (“GRA”) with the Public Utilities Board (the “Board”) to establish customer
5 electricity rates for 2018 and 2019.

6

7 By its Procedural Order No. 30(2017) Amended dated the 26th of September, 2017 the Board
8 granted Intervenor status to those parties named in Schedule “A” thereto, including the
9 Consumer Advocate.

10

11 Several revisions to Hydro’s Application were subsequently submitted to the Board on
12 September 8, 2017; October 16, 2017; October 27, 2017, and November 11, 2017.

13

14 On January 4, 2018, the Consumer Advocate filed an Application to delay Hydro’s Application
15 until certain additional information was filed by Hydro.

16

17 By Order P.U. 2(2018) dated the 26th of January, 2018, the Board made the following Order
18 relating to the Consumer Advocate’s Application:

19

20 *IT IS THEREFORE ORDERED THAT:*

21

22 1. *Hydro shall file forecast 2018 and 2019 revenue requirements and cost of service*
23 *studies based on the expected supply scenario, setting out the basis and support for the*
24 *forecasts and assumptions used and including information related to customer rates and*
25 *the updated fuel price forecast, in accordance with the findings of the Board in this Order.*

26

27 Pursuant to Order P.U. 2(2018), Hydro filed additional Cost of Service information on the 23rd
28 of March, 2018, based on its expected supply scenario (the “Expected Supply Scenario”) for the
29 test years 2018 and 2019.

30

31 Following this, and upon consideration of the Pre-Filed Evidence filed by Hydro, a Settlement
32 Agreement of some of the issues set forth in Hydro’s Application was entered into between
33 Hydro and the Intervenor on the 11th of April, 2018.

34

35 Public hearings commenced in relation to Hydro’s GRA on the 16th of April, 2018, until the
36 public hearing was adjourned on the 26th of April, 2018.

1 Following this, a second Supplementary Settlement Agreement was reached between Hydro and
2 the Intervenor dated the 16th of July, 2018, after which time the public hearings resumed on the
3 remaining unresolved issues, which hearings were held between the dates of July 16 and August
4 16, 2018.

5
6 By its correspondence to Hydro and the Intervenor dated November 26, 2018, the Board advised
7 as follows:

8
9 *On October 26, 2018 Hydro filed, as directed by the Board, an update reflecting both the*
10 *revised forecast of off-island purchases and the updated fuel price forecast along with*
11 *the revised customer rate projections for 2019 for each customer class. The Board also*
12 *directed Hydro to file a revision to its 2017 GRA to update Part B, Hydro Proposals.*

13
14 *On November 7, 2018 Hydro completed its filing of undertakings agreed to in the hearing*
15 *process. On November 19, 2018, in response to IC-NLH-002 in the 2018 Cost Deferral*
16 *and Interim Rates Application, Hydro stated that it considers the parties final submissions*
17 *to be the only outstanding item to bring the GRA to completion.*

18 19 **THE CONSUMER ADVOCATE'S POSITION**

20 21 **(a) Labour Costs**

22
23 The Consumer Advocate is of the view that labour costs is one of the primary issues remaining
24 outstanding, as most of the other issues of the 2017 GRA have already been settled.

25
26 In its Order on the Amended 2013 GRA (P.U. 49(2016), page 45, lines 4 to 13), the Board states:

27
28 *“While the management of Hydro has the discretion to determine its organizational*
29 *structure, wage levels and the number of FTEs, only those costs which are demonstrated*
30 *to be reasonable and necessary in the provision of least cost reliable service can be*
31 *recovered from customers. The Board does not accept that the proposed 2015 salaries*
32 *and benefits costs are reasonable and necessary in the circumstances. To account for*
33 *wage increases and levels of FTEs which have not been justified to be reasonable and*
34 *necessary the Board will disallow a portion of these costs. The Board notes that wage*
35 *increases were associated with approximately \$20.0 million of the increase in salaries.*
36 *Aside from the rise in salaries, the increasing level of FTEs is associated with another*
37 *approximate \$8.0 million increase. The Board believes that a disallowance of \$4.0 million*
38 *of the proposed 2015 salaries and benefits costs is reasonable in the circumstances.”*
39

1 In the 2017 Application (Revision 3, Footnote 72, page 3.34), Hydro states “*In 2017, operating*
2 *costs return to normalized levels*”. Hydro goes on to say “*In 2016, a plan to reorganize Hydro*
3 *was announced which resulted in the creation of a dedicated and separate executive team for*
4 *Hydro and established separate support functions for Hydro. Hydro’s 2017 Forecast operating*
5 *costs reflect the outcome of these changes. Operating costs in 2017 are forecast to be \$10.4*
6 *million higher than 2016 actual costs. The primary drivers of the increase are labour costs of*
7 *\$4.0 million, other operating costs of \$3.3 million, including consulting, insurance, and other*
8 *costs, as well as an increase of \$2.4 million in cost allocations associated with Information*
9 *Systems and other costs*”.

10
11 An up-to-date compilation of Hydro’s labour costs in recent years is provided in PUB-NLH-187.
12 The following submission is based on information in Attachment 1 of this RFI response, which
13 is appended hereto for ease of reference (see: Appendix “A” – PUB-NLH-187).

- 14
- 15 • In the Amended 2013 GRA Hydro proposed \$75,611,000 for labour costs (exclusive of
16 “Employee Future Benefits” and “Overtime”) for the 2015 test year. The Board approved
17 \$69,978,000, \$5,633,000 less than proposed by Hydro.
 - 18
 - 19 • Actual labour costs in 2016 and 2017 were less than that approved by the Board for 2015,
20 by \$5,497,000 and \$1,650,000, respectively. As discussed above, Hydro states that
21 operating costs returned to normalized levels in 2017.
 - 22
 - 23 • In the 2018 test year, Hydro has proposed \$73,906,000 for labour, an increase of
24 \$5,578,000 over 2017 actual, and \$2,192,000 over 2018 actual (based on 11 months of
25 actual costs and 1 month of forecast costs).
 - 26
 - 27 • As discussed above, Hydro reorganized in 2016. A main driver of this reorganization was
28 presumably to improve efficiency. However, Hydro has proposed \$75,224,000 for labour
29 costs in the 2019 test year, about \$6.9 million more than 2017 actual labour costs when
30 Hydro states that operating costs returned to normal.
 - 31
 - 32 • Hydro is now budgeting for labour costs of \$73,897,000 for 2019 which allows for
33 vacancy allowance adjustment to account for the additional 15 FTEs agreed to in the 2017
34 GRA Settlement Agreement filed with the Board on April 16, 2018. This is \$1,327,000
35 less than proposed or the 2019 test year.
 - 36

37 It is difficult to know just how much money Hydro needs for labour because we are unable to
38 determine if Hydro has reasonable labour productivity. Actual labour costs in recent years

1 provide an indication of cost control. Based on this measure, Hydro is proposing roughly \$3.5
2 million more for labour than actual costs in 2018, an increase of 4.9%, and \$6.9 million more
3 than actual labour costs in 2017 when according to Hydro operating costs returned to normalized
4 levels. This represents an unreasonable increase at a time when Hydro's evidence was that rates
5 are forecast to double with the Muskrat Falls project coming on line. Consumers expect Hydro
6 to cut costs wherever possible under these circumstances and labour represents an area over
7 which Hydro has a measure of control.

8
9 While it may be difficult to know if Hydro has reasonable labour productivity, Liberty
10 Consulting Group is in a good position to make such a determination. Liberty has been
11 significantly involved with Hydro for a number of years now, starting with the inquiry into the
12 2013 and 2014 outages, and now with the reference relating to Muskrat Falls rate mitigation.
13 Liberty states in its interim report dated December 31, 2018 (page 7):

14
15 *"We did not encounter a strong Hydro focus on work execution productivity. Work*
16 *planning and management is dispersed, its systems and methods are not as strong as we*
17 *have seen elsewhere, productivity metrics are not robust, work measurement and data*
18 *analysis do not appear to be "central" elements of cost management, and accountability*
19 *for productive performance is not well-placed. The Hydro organization is large enough*
20 *to make this issue matter - - each two percent improvement in productivity (a modest*
21 *assumption here) has a value well in excess of \$1 million per year."*

22
23 This statement by Liberty is clear-cut. If the Board passes through the proposed 2019 labour cost
24 of \$75,224,000 Hydro will have little incentive to improve "*work execution productivity*". The
25 problem is exacerbated when one considers that Hydro's return on equity is set equal to that of
26 Newfoundland Power owing to OC2009-063. Hydro has very little incentive to improve
27 efficiency and performance.

28
29 The Board states in P.U. 49(2016) (page 45): "*While the management of Hydro has the discretion*
30 *to determine its organizational structure, wage levels and the number of FTEs, only those costs*
31 *which are demonstrated to be reasonable and necessary in the provision of least cost reliable*
32 *service can be recovered from customers."* The Consumer Advocate does not accept that
33 Hydro's proposed 2018 and 2019 labour costs are reasonable and necessary in the circumstances.

34
35 Based on all of the foregoing and lacking timelines upon which to base a cap, the Consumer
36 Advocate recommends that the Board freeze Hydro's labour costs at levels approved at the
37 Amended 2013 GRA for the 2015 test year at \$69,978,000. This is about \$1.65 million more
38 than 2017 actual levels when Hydro's operating costs returned to normalized levels. It would

1 reduce the 2018 and 2019 test year revenue requirements by \$3.928 million (5.3% of proposed
2 levels)) and \$5.246 million (7.0% of proposed levels), respectively.

3
4 **(b) Off-Island Purchases**

5
6 The Consumer Advocate is also of the view that the off-island purchases issue remains
7 outstanding.

8
9 As noted earlier, only those costs which are demonstrated to be reasonable and necessary in the
10 provision of least cost reliable service can be recovered from customers. The Consumer
11 Advocate submits that the costs of off-island purchases that are included in the 2019 test year do
12 not meet this standard.

13
14 Hydro appears to believe that by establishing the Revised Energy Supply Cost Variance Deferral
15 Account customers will be left unharmed. However, the cost of service should reflect Hydro's
16 best forecast of costs, and at this point, the costs associated with the off-island purchases do not
17 appear to do so.

18
19 Responses to CA-NLH-008 (2018 Cost Deferral and Interim Rates Application) and PUB-NLH-
20 176 (2017 General Rate Application) show the various forecasts of off-island purchases in GWh
21 for the 2019 test year since the March 2018 filing:

22

<i>Source</i>	<i>March 2018 Filing</i>	<i>July 2018 Filing</i>	<i>October 2018 Filing</i>	<i>PUB-NLH-176 Filed January 11, 2019</i>
Recapture Energy	919	920	667	637
Other Off-Island Purchases	41	96	49	49
Total	960	1016	716	686

23
24 As can be seen, over the past 10 months the forecast of off-island purchases for the 2019 test
25 year has decreased dramatically from a high of 1016 GWh to the current forecast level of 686
26 GWh. While increases in the Labrador load forecast have reduced the amount of recall energy
27 available to the Island, it is not clear why purchases from other sources have remained basically
28 the same. What happened to "Fill-the-LIL"? Admittedly, purchases from other sources are not
29 as lucrative as purchases of recall energy, but should there not be an increase in purchase from
30 other sources to make up the loss of purchases of recall energy?

1 We are unable to quantify the benefits of off-island purchases because we still do not have
2 information pertaining to Nalcor Energy Marketing's (NEM's) purchase strategy or the review
3 process for NEM sales/purchases. In CA-NLH-340 Hydro says it will file a report with the Board
4 on NEM's 2018 activities by the end of the 1st quarter 2019.

5
6 The projected net savings in 2019 from off-island purchases are now reduced by \$4.7 million
7 (PUB-NLH-176). This implies that if the cost of service is not updated in the compliance filing,
8 the balance in the Revised Energy Supply Cost Variance Deferral Account will show a
9 significant amount owing by consumers. Any strategy that defers expenses to the period when
10 Muskrat Falls is coming on line is not particularly favourable to consumers.

11
12 In summary, the Consumer Advocate submits that the off-island purchases accounted for the
13 2019 test year does not represent the best forecast of costs to serve customers. In this regard, the
14 Consumer Advocate recommends that an Order on the 2017 GRA should be delayed at least
15 until the parties to this undertaking have had the opportunity to review the report on NEM's 2018
16 sales/purchase activities scheduled for filing by the end of the 1st quarter 2019 and make
17 submissions in reference to the same.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 1st day of February, 2019.


for

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Consumer Advocate

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**PUB-NLH-187
2017 General Rate Application**

Page 1 of 1

- 1 Q. **2018 Cost Deferral and Interim Rates Evidence - Revision 2, November 14, 2018**
2 Provide a revised Schedule 3-IX of Operating Costs from the 2017 Amended General
3 Rate Application including 2017 Actuals and the most current forecast for 2018 and
4 2019, including actuals to the latest month available. In the response provide
5 explanations of significant variances between the 2018 Test Year in the existing
6 schedule compared to the most current forecast for 2018 Operating Costs, as well
7 as the differences between the 2019 Test Year and the revised 2019 Operating
8 Costs forecast.
9
10
11 A. Please refer to PUB-NLH-187, Attachment 1.

Newfoundland and Labrador Hydro
Total Operating Expenses by Cost Type
\$ thousands

	2015 TY	2015 GRA Order	2015			2018 Test Year	2018 Forecast ⁽¹⁾	18 TY vs 18 FCST	2019 Test Year	2019 Budget	19 TY vs 19 FCST	
			Approved TY	2015 Actual	2016 Actual							2017 Actual
Labour related costs	75,611	(5,633)	69,978	73,287	64,481	68,328	73,906	71,714	2,192 ⁽²⁾	75,224	73,897	1,327 ⁽⁷⁾
Employee future benefits	8,371	-	8,371	6,690	6,902	6,282	6,489	6,819	(331)	6,705	6,705	-
Overtime	4,906	-	4,906	10,589	6,164	6,972	4,874	6,304	(1,430) ⁽³⁾	4,901	4,901	-
Total Labour	88,888	(5,633)	83,255	90,566	77,547	81,582	85,269	84,837	431	86,830	85,503	1,327
System Equipment and Maintenance	26,825	(41)	26,784	31,927	25,048	25,791	26,228	23,477	2,751	26,796	26,796	-
Other												
Office supplies and expenses	2,804	-	2,804	2,762	2,249	2,118	2,516	2,285	231	2,520	2,520	-
Professional services	9,494	(540)	8,954	14,408	6,662	6,142	9,112	8,238	874 ⁽⁴⁾	8,825	8,825	-
Insurance	2,607	-	2,607	2,508	2,530	3,175	3,345	3,233	112	3,425	3,425	-
Equipment rentals	3,066	-	3,066	4,218	4,197	3,817	3,749	3,831	(82)	3,746	3,746	-
Travel	3,717	(500)	3,217	3,250	1,984	2,412	2,757	2,631	127	2,759	2,759	-
Miscellaneous expenses	5,654	-	5,654	5,789	4,974	5,447	5,784	5,425	359	5,867	5,867	-
Building rental and maintenance	1,217	-	1,217	1,497	1,109	1,164	1,100	935	165	1,100	1,100	-
Transportation	2,245	-	2,245	1,649	856	1,009	1,164	1,958	(794) ⁽⁵⁾	1,274	1,274	-
Customer costs	118	-	118	253	126	86	118	200	(83)	118	118	-
Total Other	30,922	(1,040)	29,882	36,334	24,687	25,370	29,645	28,736	909	29,634	29,634	-
Cost Allocations	(7,066)	(118)	(7,184)	(7,906)	(3,370)	(2,530)	1,235	(84)	1,320 ⁽⁶⁾	2,073	(968)	3,041 ⁽⁸⁾
Total operating costs	139,569	(6,832)	132,737	150,921	123,912	130,213	142,377	136,966	5,411	145,333	140,965	4,368

Notes:

(1) Actuals are provided up to the end of November 2018.

(2) Decrease in labour related costs is primarily due to FTE vacancy, variations in salaries from the 2018 TY budget, higher utilization of resources on capital work and a reduction in fringe benefits.

(3) Increase in overtime costs is primarily a result of operational support requirements and variations in maintenance schedules.

(4) Decrease in professional services is primarily due to changes in scope and activity.

(5) Increase in vehicle fleet costs is a result of lower capitalization.

(6) Decrease in Cost Allocations is primarily due to variations in the intercompany admin fees and a lower allocation of Business System costs as a result of project delays. The 2018 forecasted Business System costs were agreed to be deferred in the 2017 GRA Settlement Agreement filed with the Board on April 16, 2018. However, as Hydro has not yet received a final Board Order the Business System costs have not been deferred in Hydro's forecast.

(7) Vacancy allowance increased to reflect an additional 15 FTEs as per the 2017 GRA Settlement Agreement filed with the Board April 16, 2018.

(8) 2019 forecast adjusted to reflect the Deferral of the Business System Fee, as outlined in the 2017 GRA Settlement Agreement filed with the Board April 16, 2018.