

1 Q. (Reference 2017 GRA Volume I, page 5.6) It is stated (lines 11 to 13) “*reflecting the*
2 *forecast savings from pre-commissioning off-island purchases in the 2018 and 2019*
3 *Test Year revenue requirements is anticipated to keep rates flat or potentially*
4 *reduce rates slightly.*” Based on this expected future and the Alberta interim rates
5 test identified below, should the Board approve Hydro’s proposed interim rates for
6 January 1, 2018? Specifically, does Hydro’s application pass the Alberta interim
7 rates test? The Alberta interim rates test includes two parts with the first part
8 relating to quantum and need for the rate increase and the second part relating to
9 the general public interest.

10

11 Part One

- 12 i. Is the identified revenue deficiency probable and material?
13 ii. Can all or some portion of any contentious items be excluded from the
14 amount collected?
15 iii. Is the increase required to preserve the financial integrity of the applicant or
16 to avoid financial hardship to the applicant?
17 iv. Can the applicant continue safe utility operations without the interim
18 adjustment?

19

20 Part Two

- 21 i. Do the interim rates promote rate stability and ease rate shock?
22 ii. Do the interim adjustments help maintain intergenerational equity?
23 iii. Can interim rate increases be avoided through the use of carrying costs?
24 iv. Are the interim rate increases required to provide appropriate price signals
25 to customers?
26 v. Is it appropriate to apply the interim rider on an across-the-board basis?

1 A. As noted in the question, the Alberta Utilities Commission (AUC) has established a
2 two-part test applicable to interim rate applications. It is Hydro's opinion that its
3 request for interim rates for 2018 meets the requirements of this test.

4

5 As explained in Hydro's response to CA-NLH-042, there is material uncertainty in
6 Hydro's fuel/supply costs to be incurred in 2018 and 2019 as a result of the planned
7 interconnection to the North American grid. There is currently no mechanism in
8 place to deal with supply cost variability that will result from off-island supply.

9 Therefore, in determining its Test Year revenue requirements, Hydro has proposed
10 to set aside the net savings from off-island purchases that are achieved during the
11 pre-commissioning period in a deferral account and use those savings to help
12 mitigate the increase in rates required to provide recovery of the Muskrat Falls
13 Project costs. Under Hydro's proposal, the potential savings will not be available to
14 offset Hydro's cost increases in 2018.

15

16 **Part I: Quantum and Need**

17 (i) Is the identified revenue deficiency probable and material?

18 Yes. As noted in Hydro's Application, the continuation of existing 2015 Test Year
19 rates for 2018 would result in a 2018 net loss for Hydro and a return on rate base
20 below the lower end of the approved range of return on rate base of 6.41%
21 (midpoint of 6.61%).¹ Please see Schedule 4-III page 1 of 1 in Hydro's 2017 General
22 Rate Application.

23

24 The continuation of 2015 Test Year base rates in 2018 will result in a revenue
25 deficiency which is both probable and material. Even with the most recent lower

¹ Hydro's 2015 rate of return on rate base of 6.61% was approved by the Board in P.U. 22(2017).

1 fuel price forecast taken into consideration, customer rates to provide full recovery
2 of 2019 forecast costs would need to be implemented by April 2018 to avoid a 2018
3 revenue deficiency.² Given the hearing is not proposed to start until January 30,
4 2018, final customer rates will not be implemented until later in 2018 and may not
5 be implemented until January 1, 2019.³

6
7 (ii) Can all or some portion of any contentious items be excluded from the amount
8 collected?

9 Hydro's proposal for 2018 interim rates reflects recovery of only 70% of the
10 increased costs relative to the approved 2015 Test Year; this approach has
11 effectively excluded 30% of the cost increases from Hydro's proposed interim rates.

12
13 If upon final testing of 2018 costs, the Board determines that 2018 cost adjustments
14 are required, then these amounts would be applied to reduce the 2018 net income
15 deficiency to be recovered through customer rates in future years. Hydro's
16 proposed approach ensures; (i) customers do not pay rates in 2018 that exceed the
17 approved cost of providing service in 2018, and (ii) the amount of 2018 costs to be
18 recovered from customers in future years is minimized.

19
20 (iii) Is the increase required to preserve the financial integrity of the applicant or to
21 avoid financial hardship to the applicant?

22 Yes. As discussed in response (i), the continuation of existing 2015 Test Year rates
23 for 2018 would result in a 2018 net loss for Hydro and a return on rate base below
24 the lower end of the approved range of return on rate base of 6.41%.

² Refer to Hydro's response to NP-NLH-098 and NP-NLH-104.

³ Refer to Hydro's response to PUB-NLH-003.

1 The approval of the proposed interim increase in base rates will reduce financial
2 uncertainty for 2018 and reduce Hydro’s borrowing costs.

3

4 (iv) Can the applicant continue safe utility operations without the interim
5 adjustment?

6 Yes. While Hydro is committed to the delivery of safe, reliable, least-cost power, it is
7 not appropriate, in Hydro’s view, to continue with uncertainty with respect to cost
8 recovery.

9

10 **Part II: Public Interest Factors**

11 (i) Will the interim rates promote rate stability and ease rate shock?

12 Yes. The proposed interim rates avoids materially higher rates in 2019 when final
13 rates are implemented. In addition, delayed implementation of rates from Hydro’s
14 2017 General Rate Application would further increase the 2018 revenue deficiency
15 to be recovered from customers. Not only would this add to the above noted rate
16 increases, it further compounds the issue of intergenerational equity, discussed in
17 Part II(ii).

18

19 (ii) Will the interim adjustments help to maintain intergenerational equity?

20 Yes. Approval of interim rates in 2018 to increase Hydro’s base rate revenues will
21 help maintain intergenerational equity. If increased interim base rates are not
22 implemented, there is a substantial risk that customers’ rates for 2018 will not
23 reflect the costs associated with the service provided in that period. In this
24 circumstance, 2015 base rates will be in place for much and potentially all of 2018.
25 Rates charged to customers in 2018 will not accurately reflect the costs associated
26 with the service provided in that period. Denial of Hydro’s proposal to implement
27 increased interim base rates in 2018 will further increase the 2018 revenue

1 deficiency and place an increased cost burden on future customers to fund recovery
2 of costs incurred in previous years.

3

4 (iii) Can interim rate increases be avoided through the use of carrying costs?

5 This is not a reasonable approach in the current circumstances. Carrying costs do
6 not address the underlying problem, namely the existence of a significant net
7 income deficiency that must be recovered from customers because customer base
8 rates for 2018 do not recover the forecast 2018 revenue requirement.

9

10 There is an opportunity to minimize the required increase in customer rates and
11 provide additional base rate revenue to Hydro by adjusting the fuel rider early in
12 2018 to reflect the reduced fuel price, and simultaneously implement a base rate
13 increase. This approach would use revenues from existing billings to offset Hydro's
14 2018 revenue deficiency.

15

16 (iv) Are the interim rate increases required to provide appropriate price signals to
17 customers?

18 Yes. As stated in Hydro's evidence, the cost to provide reliable service is increasing.
19 Hydro is forecast to invest \$370 million in capital assets in 2017 and \$206 million in
20 2018. Current customer rates based on the 2015 Test Year do not reflect this
21 increased cost of providing service to customers.

22

23 (v) Is it appropriate to apply the Distribution interim rate increase on an across the
24 board basis?

25 No. Hydro believes the interim increases to be implemented should be 70% of the
26 forecast required increase for each class of customers. However, Hydro is proposing

1 interim rate increase to Labrador Interconnected customers on an across the board
2 basis.

3

4 Rate changes to customers of Newfoundland Power will be determined in
5 accordance with Board-approved rate design for Newfoundland Power customers.

6

7 Conclusion

8 Hydro submits that its proposal for 2018 interim rates meets the two-part test
9 originally established by the AUC for consideration of interim rate adjustments.

10 Hydro has shown that the net income deficiency for 2018 is both probable and
11 material. Approval of the proposed interim rates will provide an approximate 70%
12 recovery of the increased cost of service relative to the approved 2015 Test Year.

13

14 Hydro does not believe it is appropriate to make further adjustments to reduce the
15 level of recovery in 2018 interim rates. If upon final testing of 2018 costs, the Board
16 determines that 2018 cost adjustments are required, then these amounts would be
17 applied to reduce the 2018 net income deficiency to be recovered through
18 customer rates in future years.

19

20 Approval of increased base rates on an interim basis will add rate stability for 2018
21 and help mitigate intergenerational equity concerns caused by delayed rate
22 implementation. Delayed implementation of increased base rates will further
23 increase the 2018 revenue deficiency proposed for recovery from customers upon
24 establishment of final customer rates.

25

26 Hydro believes that approval of its increased base rates in 2018 on an interim basis
27 provides a reasonable balance of the interests of both the utility and its customers.

- 1 With the material decrease in the fuel price forecast for 2018, there is currently an
- 2 opportunity to provide interim rate relief for Hydro without requiring a material
- 3 increase in customer rates.