

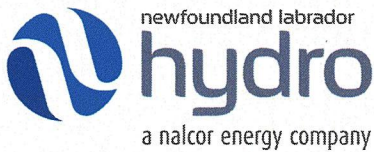
1 Q. **NLH Evidence, Section 5.2, page 5.3**

2 Please provide copies of a) Hydro’s proposal to delay the cost of service  
3 methodology hearing until after the 2017 GRA, and b) the letter dated September 9,  
4 2016 by which the Board approved it.

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7 A. Please see LAB-NLH-017, Attachment 1 for Hydro’s correspondence to the Board  
8 outlining Hydro’s proposal to delay the Cost of Service Methodology Review, as  
9 submitted on July 28, 2016, and LAB-NLH-017, Attachment 2 for the Board’s reply  
10 dated - Cost of Service Methodology Review - Board's Response, dated September  
11 9, 2016.



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July 28, 2016

The Board of Commissioners of Public Utilities  
Prince Charles Building  
120 Torbay Road, P.O. Box 21040  
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**Attention: Ms. Cheryl Blundon**  
**Director Corporate Services & Board Secretary**

Dear Ms. Blundon:

**Re: Cost of Service Methodology Review**

**A. Background**

The completion of the Muskrat Falls Project (including the Muskrat Falls generation, Labrador Island Link (LIL) and the Labrador Transmission Assets (LTA)) will result in a major change in the source of supply of electricity to the Island. For many years, load growth on the Island Interconnected System has been supplied by the Holyrood Thermal Generating Station (Holyrood). Upon the full commissioning of the Muskrat Falls Project (MF Project), supply cost payments will commence under the Transmission Funding Agreement and Muskrat Falls Power Purchase Agreement, and Holyrood, as a generating station, will be phased-out.

Because of the material change in the forecast supply cost mix with the commissioning of the MF Project, Hydro proposed in its Amended 2013 General Rate Application (GRA) to conduct a Cost of Service Methodology review prior to its next GRA. The Settlement Agreements to the 2013 GRA required Hydro to file a Cost of Service Methodology Review Report with the Board of Commissioners of Public Utilities (the Board) by March 31, 2016.

The scope of the Cost of Service Methodology Review, as stated in the Supplemental Settlement Agreement to the Amended 2013 GRA dated September 28, 2015, is as follows:

*The Cost of Service Methodology Review to be completed in 2016 will include a review of: (i) all matters related to the functionalization, classification and allocation of transmission and generation assets and power purchases (including the determination whether assets are specifically assigned and the allocation of costs to specifically assigned assets) and (ii) the approach to CDM cost allocation and recovery.*

The Parties also agreed that the generation credit agreement between Hydro and Corner Brook Pulp and Paper Limited (CBPP), which was approved on a pilot basis by the Board in Order No. P.U. 4(2012), will be reviewed in the cost of service generic hearing.

#### **B. Timing of Review**

Hydro is required to file its next GRA at the end of the first quarter in 2017 based on a 2018 Test Year. To ensure that rates provide reasonable cost recovery beyond one year, Hydro may need to include two test years in its next GRA application. In conducting the Cost of Service Methodology Review report filed with the Board on March 31, 2016, Hydro assumed that supply costs from the MF Project would be reflected in the 2019 costs for the full year. However, Hydro is not required to pay the costs of the MF Project until the entire project is commissioned (i.e., generation and transmission assets are fully commissioned).

In June 2016, Hydro was advised that the MF Project is behind schedule and that full commissioning is not expected until 2020. The delay of commissioning of the MF Project until 2020 removes the requirement for the costs of the MF Project to be recovered in 2018 or 2019 through Hydro's 2017 GRA filing.

It is anticipated that the delay in the MF Project schedule will require Hydro to file an application in 2019 to provide the opportunity to recover the supply costs resulting from the commissioning of the MF Project. Therefore, Hydro believes a cost of service methodology hearing can be held in early 2018 to provide an opportunity to reflect methodology changes in Hydro's 2019 filing to recover costs related to the MF Project.

Hydro remains committed to filing a General Rate Application no later than March 31, 2017 in accordance with the Settlement Agreement.

#### **C. Power Availability in Advance of MF Commissioning**

The availability of the LIL and the Maritime Link (ML) in advance of generation being available from the MF Project will provide the opportunity to purchase energy to reduce Holyrood production. The contract terms for using LIL in advance of any generation being available from MF are currently under review. Some additional costs will be incurred by Hydro to utilize LIL and ML to access lower cost supply costs.

Also, during the construction of the MF facilities, power and energy will be produced between the period when the first generating unit is available to reliably generate power until full commissioning of the MF plant. Contractually, this energy is termed as the "Commissioning Period Block". MF Corporation will make such power and energy available to Hydro during this commissioning period at no cost. The Muskrat Falls Power Purchase Agreement provides Hydro the option to pay for the Commissioning Period Block based on its own terms with these payments applied as a contribution to reduce the development capital costs. Hydro's preference for utilization of Commissioning Period Block will be reflected in its rate implementation plan to be provided to the Board.

Hydro anticipates it will achieve savings relative to the Holyrood fuel costs reflected in current customer rates as a result of the ability to access other supply sources prior to full commissioning of the MF Project. Hydro is currently reviewing the potential for supply cost savings from access to (i) LIL and the ML prior to the provision of Muskrat Falls generation and (ii) the availability of the Commissioning Period Block. The potential for supply cost savings is an element in an ongoing review with respect to developing a rate implementation plan for recovery of the costs of the MF Project assets.

**D. Cost of Service Approach for 2017 GRA Filing**

The scope of the Cost of Service Methodology Review also included several items not related to the completion of the MF Project. These included:

- (i) the generation credit agreement between Hydro and CBPP, which was approved on a pilot basis by the Board in Order No. P.U. 4(2012); and
- (ii) the determination whether assets are specifically assigned and the allocation of costs to specifically assigned assets) and the approach to CDM cost allocation and recovery.

Hydro will use the CA Energy review on these matters and present recommendations in its 2017 GRA filing. Hydro also plans to engage in discussions with the Parties to the 2013 GRA Settlement Agreement to attempt to achieve agreement on these matters in advance of its GRA filing.

With the delay of the inclusion of MF Project costs in Hydro's cost of service, Hydro's 2017 GRA filing will materially reflect the existing cost of service methodology, subject to the 2013 GRA Final Order.

Should you have any questions, please contact the undersigned.

Yours truly,

**NEWFOUNDLAND AND LABRADOR HYDRO**



Tracey L. Pennell  
Senior Counsel, Regulatory

TLP/bs

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2016-09-09

Ms. Tracey Pennell  
Senior Counsel  
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Dear Ms. Pennell:

**Re: Newfoundland and Labrador Hydro's Proposal to reschedule Cost of Service Methodology Review – Board's Response**

On July 28, 2016 the Board received correspondence from Newfoundland and Labrador Hydro ("Hydro") proposing to delay the cost of service review which had been planned for 2016. As a part of the settlement agreement in Hydro's General Rate application the parties had agreed that Hydro would file a cost of service methodology review report by March 31, 2016. Hydro filed the report as required but now asks that the cost of service review be delayed, stating:

*It is anticipated that the delay in the MF Project schedule will require Hydro to file an application in 2019 to provide the opportunity to recover the supply costs resulting from the commissioning of the MF Project. Therefore Hydro believes a cost of service methodology hearing can be held in early 2018 to provide an opportunity to reflect methodology changes in Hydro's 2019 filing to recover costs related the MF Project.*

The Board received comments from several of the parties in Hydro's general rate application in relation to Hydro's correspondence, all suggesting that it is reasonable to delay the cost of service review in the circumstances. The Consumer Advocate did not take issue with the proposed delay but suggested that Hydro be directed to file a plan in relation to regulatory activities associated with cost of service and electricity rates for the next few years. Newfoundland Power agreed that the proposed deferral is reasonable but suggested that, given the uncertainties, it would be premature to establish a timeline for the review. Corner Brook Pulp and Paper Limited and NARL Refining Limited Partnership also agreed with deferral of the review and that it would be impractical to establish a timeline at this stage. Vale Newfoundland and Labrador Limited had no objection to the delay so long as a final decision on the methodology for calculating specially assigned charges is not delayed.

The Board acknowledges that there are cost of service issues that will need to be addressed as part of Hydro's next general rate application, including issues related to the methodology for calculating specifically assigned charges. The Board believes that these issues can be addressed in the usual course apart from the full cost of service methodology review which will be required prior to inclusion of Muskrat Falls project costs in Hydro's cost of service. In terms of the timing of the cost of service methodology review, the Board agrees it is premature to establish at plan at this time but to ensure that the review proceeds in an orderly fashion Hydro should advise as to its plans for the review when it files its next general rate application.

If you have any questions, please do not hesitate to contact the Board.

Yours truly,



Cheryl Blundon  
Board Secretary

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