NP-CA-017 **Reference: *Comments on Newfoundland Power's 2022 Capital Budget Application*, Elenchus Research Associates Inc., August 13, 2021, page 29, lines 13-19.**

"NP's economic analysis appears to quantify the reduction in its payments to NLH based on the implicit assumption that the costs that will have to be recovered by NLH from its other domestic customers will not be impacted. However, under the more realistic assumption that NLH's cost are mostly fixed and export revenue will not increase significantly when sales to NP decline, a portion of NP's reduced payments to NLH will be offset by an increase in the costs that NLH will recover from its in-province customers."

QUESTION: **Please provide the basis for the statement that "NP's economic analysis appears to quantify the reduction in its payments to NLH based on the implicit assumption that the costs that will have to be recovered by NLH from its other domestic customers will not be impacted." In the response please indicate whether Hydro's Marginal Cost Study Update - 2018 Summary Report was reviewed to understand the basis for the estimates provided of the marginal energy costs and avoided capacity costs provided in report 1.2 Sandy Brook Plant Penstock Replacement: Appendix A Sandy Brook Plant Economic Evaluation.**

RESPONSE: The question is correct in pointing out that NP's economic analysis does not "quantify the reduction in its payments to NLH based on the implicit assumption that the costs that will have to be recovered by NLH from its other domestic customers will not be impacted." In fact, the Sandy Brook Plant Economic Evaluation provides no quantification of the reduction in the payments to NLH. Elenchus did not scrutinize NLH's Marginal Cost Study Update - 2018 Summary Report.

The comment contained in the Elenchus evidence needs to be restated. In the view of Elenchus, NP has provided no support for the assumed marginal cost projections relied on in the Sandy Point economic analysis.

- For the years to 2029, NP has used NLH's marginal cost projections.[15]

- For the years 2020 to 2042, the "marginal cost projections are escalated based on Conference Board of Canada GDP deflator, long term projection dated December 5, 2019 without explanation or justification. Given the uncertainties with respect to the evolution of

[15] 2022 CBA, PDF page 232, Note 1.

the electricity sector in the coming decades, the assumption that electricity avoided cost will escalate in line with the economic wide GDP deflator appears to be speculative.[16]

- The escalation of the avoided cost from 2042 to 2071 is not identified in the Major Inputs and Assumptions identified at PDF page 239. Assuming NP has extrapolated the trendline, the escalated avoided costs become increasingly speculative over the years.

Elenchus further notes that the Sandy Brook Plant Economic Evaluation, Attachment C (page 231 of 523 in pdf file) indicates that the avoided costs are intended to reflect opportunity cost/value of sales to the northeastern US. To date, sales revenues have averaged far less than the avoided cost values used.

Elenchus accepts the conventional wisdom that in the long run (beyond 10 years) the value of power will be constrained by the marginal cost of new supply. The value of new supply will be driven by the trend in costs, which as discussed in the response to NP-CA-009 is expected to decline rapidly. Based on the views of industry experts cited in that response, it is at least credible, if not likely, that the differential between the GDP price deflator for Canada and the marginal cost of new supply will be in excess of 3%. Under this credible scenario, the committed costs of the Sandy Brook project face a high risk of being in excess of the future value of power. Similarly, the cost of other committed sources of supply will exceed the cost of new supply in the 2030's to the 2060's. It is this disconnect between the cost of present day long term committed power supplies and long term alternate supplies that supports the Elenchus concern that committing to long term supply options at this time may result in uneconomic bypass of other currently embedded (i.e., sunk cost) resources.

[16] 2022 CBA, PDF page 232, Note 2.