



Grant Thornton

An instinct for growth™

Board of Commissioners of Public Utilities Newfoundland Power Inc.

2016 - 2017 General Rate Application
Financial Consultants Compliance Application Report

Contents

	Page
Introduction and Scope	1
Observation and Findings – General Rate Order	2
Revenue Requirements	2
Average Rate Base and Rate of Return on Average Rate Base	5
Conclusion	6
Rate Stabilization Adjustment/Municipal Tax Adjustment	7
Conclusions – Rate Stabilization Adjustment/Municipal Tax Adjustment	9

1 Introduction and Scope

2
3 On June 17, 2016, Newfoundland Power Inc. (“the Company”) (“Newfoundland Power”) submitted
4 an *Application Filed in Compliance with Order No. P.U. 18 (2016)* (“the Compliance Application”) to the
5 Board of Commissioners of Public Utilities (“the Board”) with respect to its 2016 - 2017 General
6 Rate Application (the “GRA” or “Application”). The Compliance Application reflects the orders
7 included in Board Order No. P.U. 18 (2016) that was issued by the Board on June 8, 2016.
8

9 Grant Thornton LLP (“Grant Thornton”) has undertaken a review of the Compliance Application
10 focusing on the changes to Newfoundland Power’s 2016 and 2017 test years’ forecast revenue
11 requirement, forecast average rate base and forecast rate of return on average rate base. The review
12 also included the 2016 rate stabilization adjustment (the “RSA”) and municipal tax adjustment (the
13 “MTA”) to be incorporated in customer electricity rates. In conducting our review, we have
14 performed the following procedures:
15

- 16 • reviewed the Compliance Application, including the exhibits thereto containing certain
17 Finance and Accounting Schedules, to assess whether the orders contained in P.U.18 (2016)
18 are appropriately reflected in the Compliance Application;
- 19 • reviewed and agreed the Finance and Accounting schedules to supporting information
20 provided by the Company where appropriate;
- 21 • made enquiries and obtained additional documentation, where appropriate, to support the
22 revisions to 2016 and 2017 forecast revenue requirement, forecast average rate base and
23 forecast rate of return on average rate base;
- 24 • confirmed the calculation, found in Schedule 2, of the RSA of (1.110) cents/kWh;
- 25 • confirmed the calculation, found in Schedule 2, of the MTA of 1.02526 cents/kWh;
- 26 • ensured the calculations included in Schedule 2 are in accordance with Board Orders P.U. 18
27 (2004), P.U. 6 (2008), P.U. 18 (2015) and P.U. 18 (2016);
- 28 • ensured the new RSP rates for the Fuel Rider and the March 31st RSP balance of
29 \$(77,890,345) effective July 1, 2016, which was filed by Newfoundland and Labrador Hydro
30 on June 3, 2016 and approved in P.U. 21 (2016) are incorporated into the calculation of the
31 RSA and MTA;
- 32 • ensured the RSA incorporates the transfers from the Energy Supply Cost Variance Reserve,
33 the Conservation and Demand Management Cost Deferral Account, the disposition of the
34 Optional Seasonal Rate Revenue and Cost Recovery Account, the Wholesale Flow-Through
35 Cost Recovery, and the Weather Normalization Balance Recovery which were approved by
36 the Board in P.U. 32 (2007), P.U. 13 (2013), P.U. 10 (2016), P.U. 18 (2015), and P.U. 13
37 (2013), respectively.
- 38 • ensured the Company’s schedule of rates, tolls and charges as set out in Schedule 2 Appendix
39 D incorporates the base rate changes approved in P.U. 18 (2016) and the proposed RSA and
40 MTA adjustments included in the Compliance Application;
- 41 • verified the calculation of the proposed rates necessary to meet the forecast revenue
42 requirement in the 2016 and 2017 test years as set out in the Compliance Application.
43

44 The procedures undertaken in the course of our financial analysis do not constitute an audit of the
45 Company’s financial information and consequently, we do not express an audit opinion on the
46 financial information.
47

1 Observations and Findings – General Rate Order

2 *Revenue Requirement*

3
4
5
6
7
8
9

As a result of P.U. 18 (2016), the forecast revenue requirements from rates for the 2016 and 2017 test years included in the Company's Compliance Application are calculated to be \$665,114,000 and \$671,005,000 respectively, which are a decrease of \$4,046,000 and \$9,416,000 respectively from those proposed by the Company in its Application filed March 8, 2016. The breakdown of these changes is as follows:

Change in 2016 Test Year Revenue Requirement	<u>2016</u>
(000's)	
Revenue Requirement from rates, per Application	<u>\$ 669,160</u>
(Decrease) Increase in 2016 Test Year Revenue Requirement	
Return on Common Equity	(4,815) ¹
Power Supply Cost	(172) ²
Operating Costs	(284) ³
Amortization of Deferred Cost Recoveries	3,192 ⁴
Income Taxes	<u>(1,967) ⁵</u>
Total decrease in Revenue Requirement	<u>(4,046)</u>
Revenue Requirement from rates, per Compliance Application	<u>\$ 665,114</u>

10 Note 1: Return on rate base has decreased by \$4,815,000 as a result of the change in return on equity from 9.5% to 8.5%.

11
12
13 Note 2: Power supply costs decreased by \$172,000. The Company has indicated that primarily due to a domestic rate
14 increase of 3.8% (includes a 2% increase in HST) included in the Compliance Application versus 3.1%, there will
15 be a decrease in forecast energy sales of 1.7 GWh's as a result of elasticity effects, therefore purchased power
16 requirements have decreased.

17
18 Note 3: Operating costs recoveries decreased by \$284,000. \$200,000 of this decrease is the result of a change in the
19 approved hearing costs to \$1.0 million amortized over 30 months commencing July 1, 2016 versus proposed
20 deferred hearing costs of \$1.2 million amortized over 36 months for the complete year in the original application.
21

	Application	Compliance Application	Change
Hearing costs	\$ 1,200,000	\$ 1,000,000	\$(200,000)
2016 amortization	<u>(400,000)</u>	<u>(200,000)</u>	<u>(200,000)</u>
Deferral	<u>\$ 800,000</u>	<u>\$ 800,000</u>	<u>\$ -</u>
Revenue requirement impact	<u>\$ 400,000</u>	<u>\$ 200,000</u>	<u>\$ (200,000)</u>

22
23
24
25
26
27
28
29
30 \$84,000 of the decrease is a result of a change in Short-Term Incentive ("STI") amounts reflecting approved
31 reductions of 50% of the Company's proposals in the original application:
32

	Application	Compliance Application	Change
STI costs	<u>\$ 168,000</u>	<u>\$ 84,000</u>	<u>\$ (84,000)</u>
Revenue requirement impact	<u>\$ 168,000</u>	<u>\$ 84,000</u>	<u>\$ (84,000)</u>

Note 4: Amortization of deferred cost recoveries has increased by \$3,192,000. This is the result of a change in the 2016 revenue shortfall due to a reduction in return on equity to 8.5% which has shifted the balance from a shortfall to a surplus.

	Application	Compliance Application	Change
Total revenue (shortfall) surplus	\$ (1,410,000)	\$ 2,580,000	\$3,990,000
2016 amortization	<u>282,000</u>	<u>(516,000)</u>	<u>(798,000)</u>
Revenue requirement impact	<u>\$ (1,128,000)</u>	<u>\$ 2,064,000</u>	<u>\$ 3,192,000</u>

Note 5: Income taxes have decreased by \$1,967,000. This is primarily due to the lower forecast return on common equity.

Change in 2017 Test Year Revenue Requirement

(000's)

	<u>2017</u>
Revenue Requirement from rates, per Application	<u>\$ 680,421</u>
(Decrease) Increase in 2017 Test Year Revenue Requirement	
Return on Common Equity	(5,099) ¹
Power Supply Cost	(571) ²
Operating Cost	(86) ³
Amortization of deferred cost recoveries	(1,596) ⁴
Income Taxes	<u>(2,064) ⁵</u>
Total decrease in Revenue Requirement	<u>(9,416)</u>

Revenue Requirement from rates, per Compliance Application

\$ 671,005

Note 1: Return on rate base has decreased by \$5,099,000 as a result of the change in return on equity from 9.5% to 8.5%.

Note 2: Power supply costs decreased by \$571,000. The Company has indicated that primarily due to a domestic rate increase of 3.8% (includes a 2% increase in HST) included in the Compliance Application versus 3.1%, there will be a decrease in forecast energy sales of 5.6 GWh's as a result of elasticity effects, therefore purchased power requirements have decreased.

Note 3: Operating costs recoveries decreased by \$86,000 as a result of a change in Short-Term Investive ("STI") amounts reflecting approved reductions of 50% of the Company's proposals in the original application:

	Application	Compliance Application	Change
STI costs	<u>\$ 172,000</u>	<u>\$ 86,000</u>	<u>\$ (86,000)</u>
Revenue requirement impact	<u>\$ 172,000</u>	<u>\$ 86,000</u>	<u>\$ (86,000)</u>

Note 4: Amortization of deferred cost recoveries has decreased by \$1,596,000. This is the result of a change in the 2016 revenue shortfall due to a reduction in return on equity to 8.5% which has shifted the balance from a shortfall to a surplus.

	Application	Compliance Application	Change
Opening (shortfall) surplus	\$ (1,128,000)	\$ 2,064,000	\$3,192,000
2017 amortization	<u>564,000</u>	<u>(1,032,000)</u>	<u>(1,596,000)</u>
Unamortized (shortfall) surplus	<u>\$ (564,000)</u>	<u>\$ 1,032,000</u>	<u>\$ (1,596,000)</u>
Revenue requirement impact	<u>\$ 564,000</u>	<u>\$ (1,032,000)</u>	<u>\$ (1,596,000)</u>

Note 5: Income taxes have decreased by \$2,064,000. This is primarily due to the lower forecast return on common equity.

1 **We have reviewed the forecast revenue requirement included in the Compliance Application**
2 **and obtained appropriate evidence to support the revisions as a result of P.U. 18 (2016).**

3

4

Average Rate Base and Rate of Return on Average Rate Base

2016 forecast average rate base included in the Compliance Application decreased by \$1,008,000 compared to the Application that was filed on March 8, 2016 (\$1,061,342,000 in the Application versus \$1,060,334,000 in the Compliance Application). 2017 forecast average rate base included in the Compliance Application decreased by \$1,622,000 compared to the Application that was filed on March 8, 2016 (\$1,106,324,000 in the Application versus \$1,104,702,000 in the Compliance Application). The decreases in the forecast average rate base and the decrease in the return on common equity from 9.5% to 8.5% resulted in a decrease in the forecast rate of return on average rate base for 2016 from 7.66%, in the Application, to 7.21% in a range of 7.03% to 7.39% in the Compliance Application and for 2017 from 7.64%, in the Application, to 7.19% in a range of 7.01% to 7.37% in the Compliance Application.

The decrease in forecast average rate base was due to the following:

Change in 2016 Forecast Average Rate Base

(000's)

	<u>2016</u>
Decrease in Cost Recovery Deferral - Regulatory Amortization	\$ (1,133) ¹
Increase in Cash Working Capital Allowance	<u>125</u> ²
	<u>\$ (1,008)</u>

Change in 2017 Forecast Average Rate Base

(000's)

	<u>2017</u>
Increase in Cost Recovery Deferral - Regulatory Amortization	\$ (1,700) ¹
Increase in Cash Working Capital Allowance	<u>78</u> ²
	<u>\$ (1,622)</u>

Note 1: Decrease in 2016 Revenue Shortfall to Revenue Surplus due to reductions in ratemaking return on equity from 9.5% to 8.5%.

Note 2: Increase in cash working capital allowance due primarily to forecasted HST increases from 13% to 15%.

1 ***Conclusion***

2
3 Based on our review of the Compliance Application and the completion of the procedures described
4 in the scope of our report, we present the following findings for the Board's consideration:

- 5
6 • the revised forecast 2016 and 2017 test year revenue requirement to be recovered from electrical
7 rates, of \$665,114,000 and \$671,005,000 respectively, appropriately incorporates the impact of
8 the orders included in P.U. 18 (2016);
9
10 • the revised forecast 2016 and 2017 average rate base of \$1,060,334,000 and \$1,104,702,000,
11 respectively, appropriately incorporates the impact of the orders included in P.U. 18 (2016);
12
13 • the proposed revised rates of return on average rate base of 7.21% and 7.19% for 2016 and 2017,
14 respectively, appropriately incorporate the impact of the orders included in P.U. 18 (2016)
15
16 • the forecast revenue requirement from rates, as proposed by the Company is calculated based
17 upon the proposed Schedule of Rates, Tolls and Charges effective July 1, 2016, which is located
18 in Schedule 2 Appendix E of the 2016-2017 GRA Compliance Application.
19

1 ***Rate Stabilization Adjustment / Municipal Tax Adjustment***

2

3 We have completed our review of the Company's Compliance Application filed on June 17, 2016
4 requesting approval of: the RSA and MTA to be applied to electricity rates for the period July 1, 2016
5 to June 30, 2017 pursuant to Section 71 of the Public Utilities Act and approval of the schedule of
6 rates, tolls, and charges incorporating the RSA and MTA adjustments. The scope of our review is
7 detailed on Page 1.

8 Based on our review we present the following comments and findings with respect to the Company's
9 Compliance Application.

10 **March 31, 2016 Rate Stabilization Account**

11 Our procedures with regards to the balance in the Rate Stabilization Account of \$7,308,075 as of
12 March 31, 2016 focused on the Energy Supply Cost Variance Reserve, the Conservation and
13 Demand Management Cost Deferral Account, the disposition of the Optional Seasonal Rate
14 Revenue and Cost Recovery Account, the Wholesale Flow-Through Cost Recovery, and the Weather
15 Normalization Balance Recovery which were approved by the Board in P.U. 32 (2007), P.U. 13
16 (2013), P.U. 10 (2016), P.U. 18 (2015), and P.U. 13 (2013), respectively.

17 There is no balance in the Pension Expense Variance Deferral Account or OPEB's Variance
18 Deferral Account in 2016 as there is no variance in 2016 actual cost from the 2016 Test Year.

19 Energy Supply Cost Variance Reserve

20 We confirm that the Energy Supply Cost Variance Reserve of \$3,599,515 that was transferred as a
21 charge to the Rate Stabilization Account on December 31, 2015 is calculated in accordance with the
22 methodology approved by the Board in P.U. 32 (2007).

23 Conservation and Demand Management Cost Deferral Account

24 We can confirm that the 2015 Conservation and Demand Management Amortization of \$1,711,951
25 was transferred in 2016 as a charge to the Rate Stabilization Account that is calculated in accordance
26 with the methodology approved by the Board in P.U. 13 (2013).

27 Optional Seasonal Rate Revenue and Cost Recovery Account

28 The 2015 balance in the Optional Seasonal Rate Revenue and Cost Recovery Account of \$69,298
29 was transferred as a charge to the Rate Stabilization Account as approved in P.U. 10 (2016).

30 Wholesale Flow-Through Cost Recovery

31 We confirm that the Wholesale Flow-Through Cost Recovery amount of \$521,000 that was
32 transferred as a credit to the Rate Stabilization Account on December 31, 2015 is calculated in
33 accordance with the methodology approved by the Board in P.U. 18 (2015).

34

1 Weather Normalization Balance Recovery

2 We confirm that the 2015 pre-tax balance of the Weather Normalization Balance Recovery of
3 \$6,212,027 that was transferred as a charge to the Rate Stabilization Account is calculated in
4 accordance with the methodology approved by the Board in P.U. 13 (2013). Newfoundland Power's
5 Weather Normalization Balance Reserve of \$6,212,027 (\$4,410,537 after tax) was approved in P.U.
6 11 (2016).

7 **2016 Rate Stabilization and Municipal Tax Adjustments**

8 Our procedures were focused on ensuring the methodology and calculations relating to the RSA and
9 the MTA were in compliance with P.U. 18 (2015), P.U. 6 (2008) and P.U. 18 (2004). More
10 specifically, our procedures with respect to confirming the Company's calculations in Schedule 2
11 included agreeing the various components to source data such as P.U. 21 (2016) approving on an
12 interim basis Newfoundland and Labrador Hydro's application for RSP rates to be charged to the
13 Company, and supporting documents provided by the Company relating to this Application.

1 ***Conclusions – Rate Stabilization Adjustment/Municipal Tax Adjustment***

2 Based upon the results of our procedures we can advise that we did not note any discrepancies in the
3 calculations or methodology and therefore:

4 • Confirm that the Company’s calculation in Schedule 2 of the Compliance Application, which
5 represents the Rate Stabilization Adjustment effective July 1, 2016, is appropriate and is in
6 accordance with P.U. 6 (2008). The “recovery adjustment factor” will be (1.087) cents per kWh
7 and the “fuel rider adjustment factor” will be (0.023) cents per kWh for a total Rate Stabilization
8 Adjustment of (1.110) cents per kWh.

9 • Confirm that the Company’s calculation in Schedule 2 of the Compliance Application, which
10 represents the Municipal Tax Adjustment effective July 1, 2016, is appropriate and is in
11 accordance with P.U. 18 (2004). The “municipal tax adjustment factor” will be 1.02526 to be
12 used in billing customers for the period July 1, 2016 to June 30, 2017.

13 **Schedule 2 – Rates, Tolls and Charges incorporating the RSA and MTA Adjustments**

14 We can confirm that the Company’s schedule of rates as set out in Schedule 2 of the Compliance
15 Application incorporates the base rates arrived at in this Application and the 2016 RSA and MTA
16 adjustments included in this Application.

17 

18 St. John’s, Canada
19 June 24, 2016

Chartered Professional Accountants