

DELIVERED BY HAND

April 7, 2017

Board of Commissioners
of Public Utilities
P.O. Box 21040
120 Torbay Road
St. John's, NL A1A 5B2

Attention: G. Cheryl Blundon
Director of Corporate Services
and Board Secretary

Ladies and Gentlemen:

**Re: Newfoundland and Labrador Hydro – Amended 2013 General Rate Application –
Compliance Application – Order No P.U. 49 (2016) – Comments**

A. Background

In Order No. P.U. 49 (2016) (the “GRA Order”), the Board of Commissioners of Public Utilities (the “Board”) made a number of determinations on proposals contained in, and matters arising from Newfoundland and Labrador Hydro’s (“Hydro”) Amended 2013 General Rate Application (the “GRA”). On January 27, 2017, Hydro filed an application in compliance with that GRA Order (the “Compliance Application”).

The Compliance Application requests, amongst other things, that the Board approve a Schedule of Rates, Rules and Regulations effective April 1, 2017. Hydro’s evidence filed in support of the application (“Hydro’s Evidence”) shows a 2.3% increase in the Utility rate charged to Newfoundland Power Inc. (“Newfoundland Power” or the “Company”). The rate increase consists of (i) a 0.5% base rate decrease in compliance with the GRA Order and (ii) an effective 2.8% increase as a result of an updated fuel rider.¹ The overall customer rate impact to Newfoundland Power’s customers is estimated by Hydro to be a 1.5% increase.

On February 20, 2017, Hydro filed an application with the Board proposing a delay in the filing of Hydro’s next GRA from March 31, 2017 to July 31, 2017. The request was, in part, to delay the effective date of the rate change from April 1, 2017 to July 1, 2017 to correspond with the annual rate adjustment related to Hydro’s Rate Stabilization Plan (“RSP”).² On March 16, 2017, the Board approved Hydro’s proposal.³

¹ See Hydro’s Evidence, Exhibit 4, Appendix B. 2.3% total increase - (0.5%) base rate decrease = 2.8% increase.

² See Hydro’s February 20, 2017 application, paragraph 8 on page 3.

³ See Order No. P.U. 8 (2017).

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On March 15, 2017, the Board's financial consultant, Grant Thornton, filed a report on Hydro's Compliance Application (the "Grant Thornton Report"). Grant Thornton noted a number of issues with the Compliance Application.

On March 16, 2017, the Board requested comments from the parties on the Compliance Application. Newfoundland Power's comments follow and are separated into (i) costs to be included in Hydro's rates, and (ii) issues arising from the implementation of rates on July 1, 2017.

B. Comments Regarding Costs

Summary

Hydro's Compliance Application includes costs which do not reflect determinations of the Board in the GRA Order.

These costs include (i) \$0.4 million in depreciation costs associated with \$146 million in disallowed 2014 test year capital expenditure which are not correctly excluded from the 2014 and 2015 revenue deficiency calculations, (ii) inclusion of the 2014 revenue deficiency in rate base for rate setting purposes which inappropriately increases 2015 revenue requirements by approximately \$1.3 million, and (iii) a \$60,000 error which inaccurately increases costs allocated for recovery from Newfoundland Power's customers.

Each of these items are detailed below.

2014 Capital Expenditures

Hydro has indicated that depreciation associated with the disallowed \$146 million in 2014 test year capital expenditure is \$0.4 million. This amount has not been deducted from the calculation of the 2014 revenue deficiency. Hydro justifies its failure to deduct the depreciation costs on the basis that "...this reduction in depreciation was offset by assets that went into service earlier in the year and/or have lower service lives than originally budgeted."⁴

Disallowance of a capital cost should exclude from revenue requirement those costs directly associated with the disallowed capital cost, including depreciation costs. This requires (i) the reduction of \$0.4 million in depreciation associated with the disallowed \$146 million 2014 test year capital expenditure from Hydro's 2014 revenue deficiency calculation and (ii) a reduction of depreciation associated with disallowed capital expenditures from Hydro's 2015 revenue deficiency calculation.

The 2014 Revenue Deficiency

In the Compliance Application, Hydro includes a cost deferral in the amount of the 2014 revenue deficiency of \$38.1 million in the calculation of 2014 test year rate base (the "2014 Cost Deferral"). The 2014 Cost Deferral is included in the calculation of average rate base for the purposes of

⁴ See the response to Request for Information NP-NLH-003.

determining 2014, 2015 and 2016 revenue deficiencies as well as for rate setting purposes.⁵ Including the 2014 Cost Deferral in the calculation of test year rates is, in Newfoundland Power's submission, inappropriate.

The amount included in Hydro's 2015 average rate base for rate setting purposes is \$19.1 million, or 50% of the \$38.1 million. Hydro's evidence is that this is because the 2014 Cost Deferral was "...paid out of the RSP..." in the 2015 test year for rate setting purposes.⁶ This evidence implies that Hydro achieves recovery of the 2014 Cost Deferral via surpluses created by rerunning of the RSP as directed by the GRA Order.

From a ratemaking perspective, the conceptual purpose of the 2015 test year is to establish Hydro's reasonable costs on a *forward-looking basis*.⁷ By the end of 2016, the 2014 revenue deficiency is more than offset by revenue surpluses in 2015 and 2016 for the purposes of setting customer rates.⁸ In fact, Hydro's evidence shows that the base rate revenues billed to Newfoundland Power were in excess of the revenue deficiencies as of the then-anticipated implementation date of April 1, 2017.⁹

The evidence is clear that at the point that new rates are implemented on July 1, 2017, Hydro will no longer be funding the 2014 Cost Deferral. For this reason, it is not appropriate to include the 2014 Cost Deferral in Hydro's 2015 average rate base for the purpose of determining customer rates. Excluding it reduces the 2015 test year revenue requirement for rate setting purposes by approximately \$1.3 million.¹⁰

Cost Allocation

In Hydro's Evidence there is a difference between the regulated average equity shown in the 2014 finance schedules compared to the regulated average equity shown in the 2014 cost of service study.¹¹ Hydro indicates that this error causes an allocation variance in the cost of service study of \$60,000; however, it has no impact on total revenue requirement.¹²

Although the error does not affect total revenue requirement, the Grant Thornton Report indicates that correcting the error would result in a net decrease to the Newfoundland Power revenue

⁵ See the response to Request for Information NP-NLH-004.

⁶ See the response to Request for Information NP-NLH-004.

⁷ For example, in the GRA Order, the Board approved Hydro's proposal to reflect the full-year impact of 2014 delayed in-service assets in its 2015 test year average rate base for the purpose of setting rates beginning in 2016. See the GRA Order, page 63, *et. seq.*

⁸ See Hydro's Evidence, Exhibit 3, page 19, Table 13. This would exclude the net impacts associated with re-computing the RSP for 2015 and 2016 of \$76.4 million and a 2016 cost deferral associated with 2015 and 2016 supply costs of \$38.8 million.

⁹ See Hydro's Evidence, Exhibit 3, page 19, Table 13, *et seq.*

¹⁰ \$19.1 million x 2015 test year rate of return on rate base of 6.61% (see Hydro's Evidence, Exhibit 2, page 35, Table 29) = approximately \$1.3 million.

¹¹ See Hydro's Evidence, Exhibit 2, Appendix A, page A-4, line 30 and Exhibit 10, page 2, line 15.

¹² See the response to Request for Information NP-NLH-009.

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requirement of \$60,000 and an offsetting increase to the Labrador interconnected revenue requirement of approximately the same.¹³

Newfoundland Power submits that Hydro should be required to rectify this error in its calculation of rates to be implemented on July 1, 2017.

C. Comments Regarding July 1, 2017 Rate Implementation

Revised Hydro Compliance Application

The Compliance Application reflects a proposed rate implementation date of April 1, 2017. Subsequent to its filing, Hydro indicated a proposed rate implementation date of July 1, 2017 was preferable.¹⁴

Before the Board can approve final rates arising out of the GRA, a revised Hydro compliance application reflecting a July 1, 2017 implementation date will be required.

2017 Revenue Deficiency Calculations

The Compliance Application indicates a 2017 revenue deficiency of \$5.1 million based on a rate implementation date of April 1, 2017. Hydro's evidence indicates that the amount of the 2017 revenue deficiency is reduced by \$2.9 million to \$2.2 million if rate implementation is deferred to July 1, 2017.¹⁵

Newfoundland Power submits that final July 1, 2017 Hydro rates should reflect the lower 2017 revenue deficiency.

2017 RSP Operation

Implementation of final rates arising out of the GRA will coincide with the annual July 1, 2017 rate adjustment related to the operation of the RSP. Currently, it is Newfoundland Power's expectation that the July 1, 2017 customer rate impacts from RSP operation will be significant. Hydro has indicated it will provide details concerning the July 1, 2017 RSP operation on the 10th working day of April.¹⁶

When that information is before the Board, the combined impact of Hydro's GRA and the RSP on July 1, 2017 rate implementation can be assessed.

¹³ See the Grant Thornton Report, page 36, lines 17 – 28.

¹⁴ See Order No. P.U. 8 (2017).

¹⁵ See the response to Request for Information NP-NLH-010.

¹⁶ See the response to Request for Information NP-NLH-011. Newfoundland Power submits these details should reflect the most current exchange rate information as indicated in the Grant Thornton Report.

The Segregated Load Variation Balance

The segregated load variation balance in the RSP owing to Newfoundland Power's customers was approximately \$49 million as of December 31, 2016.¹⁷ Hydro has implied in the Compliance Application that this balance might be available to fund Hydro's recovery of deferred 2015 and 2016 supply costs of \$38.7 million.¹⁸ There is currently no application or evidence before the Board regarding Hydro's recovery of these costs.

In the absence of an appropriate record, the Company observes that any Board consideration of the application of RSP credit balances existing in favour of Newfoundland Power's customers to Hydro's costs would be premature.

D. Concluding

We trust the foregoing is helpful to the Board.

If you have any questions regarding the enclosed, please contact the undersigned at your convenience.

Yours very truly,



Peter Alteen, QC
Vice President,
Regulation & Planning

c. Tracey Pennell
Newfoundland and Labrador Hydro

Paul Coxworthy
Stewart McKelvey

Yvonne Jones, MP
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Larry Bartlett
Teck Resources Ltd.

¹⁷ See Hydro's Evidence, Exhibit 3, Table 3. This table also shows the hydraulic component of the RSP having a credit balance owing to customers of approximately \$21 million as of December 31, 2016.

¹⁸ See Hydro's Evidence, Exhibit 3, page 24, *et seq.*