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Attn: Maureen Greene, Q.C.
Vice-President Human Resources,
General Counsel & Corporate Secretary

DATE: May 20, 2003

PAGES SENT INCLUDING COVER: 4 PLEASE CALL IF ANY OMISSIONS AND ASK FOR: Michelle: (709) 737-5819

Re: Hydro's 2004 Capital Budget Application

Please see attached letter in response to the Application of Abitibi Consolidated, Corner Brook Pulp & Paper Limited and North Atlantic Refining Limited filed on May 15, 2003.

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May 20, 2003

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 & Labrador Hydro's ("Hydro") 2004 Capital Budget Application

This will respond to the Application of Abitibi Consolidated Inc. (Grand Falls), Abitibi Consolidated Inc. (Stephenville), Corner Brook Pulp & Paper Limited and North Atlantic Refining Limited in this matter, dated May 15, 2003 (the "Motion").

The Motion essentially relates to the scheduling of a hearing into Hydro's 2004 Capital Budget Application dated March 28, 2003 (the "Application"). The essential submission in the Motion concerning this issue is that the Application should be heard as part of the hearing of a General Rate Application that Hydro has been ordered to file by the end of 2003 (the "GRA").

It is Newfoundland Power's position that combining the hearing of the Application with the GRA is not appropriate.

A. The Issue

It should first be observed that the issues and evidence that will be considered by the Board in the Application and in the GRA are fairly distinct. The Application is essentially an application under s.41 of the *Public Utilities Act*. The hearing will principally focus upon engineering evidence justifying the capital projects necessary to meet Hydro's obligation to provide service to its customers. The GRA is essentially an application under s.80 of the *Public Utilities Act*. The hearing will principally focus upon evidence regarding operating costs and Hydro's return on rate base. Typically, GRAs also deal with cost of service and rate design issues.

B. Experience

While it has been Newfoundland Power's experience that an earlier review and approval of its capital budgets facilitates the orderly, efficient and cost effective implementation of capital projects, recent experience suggests that the combining of a capital budget hearing with the hearing of a GRA may have the opposite effect. Hydro's 2001 general rate application was filed on May 31, 2001. Hydro's 2002 capital budget application was included as part of Hydro's 2001 general rate application. This resulted in a delay of the approval of parts of Hydro's 2002 capital budget until the issuance of Order No. P.U. 7 (2002-2003) in June 2002.

In 2002, in preparing its response to a Consumer Advocate's application to combine the hearing of its 2003 capital budget application with Newfoundland Power's 2003 GRA, the Company surveyed the practice in other jurisdictions. The survey revealed that there was no established practice requiring a utility to seek approval of its capital budget as a part of its general rate application.¹

C. Regulatory Policy

To fulfill its statutory obligation to provide electrical service to its customers, a public utility must make capital expenditures throughout the course of the year. Section 41 of the *Public Utilities Act* requires that a public utility obtain the prior approval from the Board for those expenditures. Without approval of a reasonable capital budget in advance, Hydro could be in a position where it could not lawfully fulfill its obligation to provide service on a timely basis. This reasoning underpins Newfoundland Power's position that the Board is obliged by the terms of the *Public Utilities Act* to approve a public utility's reasonable capital expenditures for an ensuing year *in advance*.

The *Electrical Power Control Act, 1994* sets out the policy of the province regarding electrical power. Section 3(b) provides, in part, as follows:

- (b) all sources and facilities for the production, transmission and distribution of power in the province should be managed and operated in a manner
 - (i) that would result in the most efficient production, transmission and distribution of power,
 - (ii) that would result in consumers in the province having equitable access to an adequate supply of power,

¹ A review of National Energy Board, Ontario Energy Board and British Columbia Utilities Commission practices indicates that no established practice exists whereby utility capital budgets are reviewed as part of general rate applications.

- (iii) that would result in power being delivered to consumers in the province at the lowest possible cost consistent with reliable service,..."

Newfoundland Power believes that this policy requires that a reasonable capital budget be approved by the Board in advance of the year of expenditure. This enables the expenditure of capital in an orderly, efficient and cost effective manner which helps achieve the policy objectives set out above.

By Order No. P.U. 7 (2002-2003), the Board ordered Hydro to file the GRA by December 31, 2003. While it appears that Hydro may file earlier than the deadline contained in the order, it is nevertheless quite possible that the GRA will not be fully heard and decided until early 2004.


Approval of a capital budget during the year of expenditure places a utility in an untenable position with respect to the orderly, efficient and cost effective implementation of its capital expenditures for that year. Such a course of action is effectively contrary to the policy objectives of ss.3(b)(i) through (iii) of the *Electrical Power Control Act, 1994*.

D. Conclusion

The hearing of the Application ought to be conducted within a timeframe that will yield an order of the Board approving reasonable capital expenditures proposed by Hydro for 2004 prior to 2004. Given the possibility that the GRA will not be fully heard and decided until some time in 2004, hearing the Application as part of the GRA, as proposed in the Motion, is not a reasonable course of action for the Board to undertake.

We trust the foregoing and enclosed are found to be in order, however, if you have any questions, feel free to contact the undersigned.

Yours very truly,



Gerard M. Hayes
Senior Counsel

Enclosures

- c. Maureen P. Greene, Q.C.
Janet M. Henley Andrews, Q.C.
Joseph S. Hutchings, Q.C.