NEWFOUNDLAND AND LABRADOR
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

AN ORDER OF THE BOARD

NO. P. U. 32(2008)

IN THE MATTER OF the *Electrical Power Control Act*, RSNL 1994, Chapter E-5.1 (the "*EPCA*") and the *Public Utilities Act*, RSNL 1990, Chapter P-47 (the "*Act*") as amended, and their subordinate regulations;

AND

IN THE MATTER OF an application by Newfoundland and Labrador Hydro ("Hydro") for approval to extend the amortization period for deferral of Major Extraordinary Repairs, pursuant to Sections 69, 78 and 80 of the *Act*.

Application

On September 4, 2008 Hydro filed an application with the Board for approval, effective January 1, 2008, to extend from five to seven years the amortization of expenditures associated with two projects at the Holyrood Thermal Generating Station, the Asbestos Abatement Plan and repairs to the Unit 2 Boiler (the "Application").

On October 8, 2008 the Board sent information requests to Hydro in relation to the Application. Hydro responded to these information requests on October 30, 2008. Further information requests were sent to Hydro on November 6, 2008. Hydro responded to the further requests on November 14, 2008. Further information requests were sent to Hydro on November 21, 2008. Hydro responded to these information requests on November 27, 2008, with the exception of PUB-NLH-26 which Hydro undertook to answer on December 1, 2008. Hydro provided a response to PUB-NLH-26 on December 5, 2008.

No submission in relation to the Application was received from the Consumer Advocate or Newfoundland Power, both having been copied with all correspondence. The Industrial Customers wrote the Board on September 11, 2008 to advise that the Industrial Customers would not be submitting any comments specific to the Application.

Decision

In the Application Hydro seeks the Board's approval to extend the amortization period in relation to deferred expenditures associated with the 2005-2007 Asbestos Abatement Plan as well as the 2006 repairs to the Unit 2 Boiler. Hydro proposes that these expenditures be amortized over seven years rather than five years. At the same time that the Application was filed, Hydro filed a separate application for approval to defer the costs of a 2007 repair to the Unit 2 Turbine at the Holyrood Thermal Generating Station over a seven-year period.

Hydro estimates that the annual amortization associated with the three expenditures based on a five-year period is $2.9 million. Hydro points out that this is $1 million more than was set up in the 2007 Test Year for amortization of extraordinary repairs. Hydro argues that this difference would result in a negative impact on regulated earnings and proposes to extend the amortization from five to seven years to levelize the amount of amortization recognized in each year.

The Board notes that Hydro's application to amortize the expenditures in relation to the 2007 Unit 2 Turbine repairs was denied in Order No. P. U. 31(2008). If the amount of the annual amortization relating to these repairs is removed from Hydro's projections the estimated remaining annual amortization, based on a five-year period, would be $2.7 million rather than $2.9 million.

In relation to the Asbestos Abatement Plan, in Order No. P. U. 2(2005) the Board approved Hydro's proposal to treat the Asbestos Abatement Plan as a Major Extraordinary Repair with the actual costs for each year of the three-year work plan deferred over a five-year period. The total expenses were estimated at the time of the application to be $8.7 million plus financing for a total cost of $10.4 million. Now that the work has been completed Hydro reports that the actual costs for the whole project were much higher than originally estimated with total costs of $11.3 million, plus financing.

The Board in Order No. P. U. 2(2005) and in Order No. P. U. 44(2006) determined that it was appropriate to treat the expenditures as Major Extraordinary Repairs to be deferred over a five-year period. This is extraordinary treatment which is only appropriate in special circumstances. Generally Accepted Accounting Principles (GAAP) require that operating costs be recognized as expenses in the fiscal year in which they are incurred unless an alternative treatment is approved by Board. The Board has in the past allowed the deferral of the cost for a Major Extraordinary Repair if it meets the minimum threshold of $500,000 and if taking it into income in the year in which it is incurred would cause a rate shock or a shock in the utility's earnings. It has generally been accepted that a reasonable amortization period for a Major Extraordinary Repair is three to five years. This addresses inter-generational equity issues and generally coincides with the usual periods between general rate applications. There are circumstances where a longer period would be appropriate; for example where the amount is so large that amortizing it over three to five years would not avoid rate shock or a shock to the utility's earnings.

The Board must decide whether it is appropriate in the circumstances to extend the amortization period already established by the Board. Hydro argues that the amount of the difference between the annual amortization based on a five-year period and the amount included in the 2007 Test Year for amortizations would cause a negative impact on Hydro's earnings. Based on the information filed by Hydro the annual amount amortized on a five-year basis is $2.7 million. The amount included in the 2007 Test Year is $1.9 million. The Board notes that both the five-year amortization period and the amount to be deferred were approved by the Board in Order Nos. P. U. 2(2005) and P. U. 44 (2006) as proposed by Hydro in the original applications. As well the amount included in the 2007 Test Year in relation to the amortization of major extraordinary repairs was part of the Revenue Requirement proposed by Hydro as part of the Settlement Agreement which was filed by Hydro in late 2006 and accepted by the Board in Order No. P. U. 8 (2007).

Hydro suggests that it is now appropriate to extend the amortization period on the basis that taking the difference into income would result in a negative impact on regulated earnings. The Board notes that Hydro now estimates its earnings for 2008 to be $9.7 million (PUB-NLH-4) using the five-year amortization period and excluding any amounts in relation to the Unit 2 Turbine repair costs. Hydro also provided a 2009 operating budget where it estimates that Net Regulated Operating Income for

2009 will be $7.8 million (PUB-NLH-26). In the Board's view the forecast earnings for 2008 and 2009 are not out of line with the projected 2007 Test Year earnings of $8.0 million (PUB-NLH-3). The Board is not satisfied that taking the expenditures associated with a five-year deferral into account in 2008 and 2009 would cause a shock to Hydro's earnings in that year. While the expense is now forecast to be higher than estimated in the 2007 Test Year Hydro has not shown that the difference would cause a shock to either rates or earnings. There is nothing on the record to demonstrate that this increase in forecast expense should be given special treatment different than other changes to revenues and expenses. The onus is on Hydro to establish that it is appropriate to extend the previously ordered amortization period from five to seven years. Based on the information provided by Hydro the Board is not satisfied that it is appropriate in the circumstances to extend the amortization period.

IT IS THEREFORE ORDERED THAT:

1. The Application is denied.

2. Hydro shall pay the expenses of the Board incurred in connection with this Application.

DATED at St. John's, Newfoundland and Labrador, this 18th day of December 2008.

Andrew Wells
Chair & Chief Executive Officer

Darlene Whalen, P.Eng.
Vice-Chair

Dwanda Newman, LL.B.
Commissioner

G. Cheryl Blundon
Board Secretary