

June 8, 2015

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 & Gentlemen:

Re: 2016 Deferred Cost Recovery Application (the "Application")

A. The Application

Newfoundland Power is currently required to file its next general rate application ("GRA") by October 16, 2015.¹ The Application seeks to defer the filing of Newfoundland Power's next GRA to June 1, 2016. To enable this, the Application also seeks 2016 deferred cost recovery of approximately \$4 million.

These are Newfoundland Power's submissions on the Application.

B. The Hydro and Newfoundland Power GRAs

Regulatory Perspective

The relief sought in the Application is justified by the current regulatory agenda before the Board, particularly the current GRA of Newfoundland and Labrador Hydro ("Hydro") and its related applications and issues (collectively, the "Hydro GRA").²

The Board clearly has the power to control its own processes. The circumstances giving rise to the Application effectively require the Board to establish hearing priorities within a time constrained regulatory calendar. In determining those priorities, the Board is obliged to consider, and balance, the interests of the utilities and the utilities' customers. Approval of the

¹ See Order No. P.U. 15 (2015).

² To date, the additional applications and issues include a number of applications for interim rate relief, deferred cost recovery and interim intervenor costs. Further applications related to the Hydro GRA will include a proposal for refund of Hydro rate stabilization plan ("RSP") balances which accrued over the 7 year period ending in 2013. In addition, Phase II of the *Board's Investigation into Supply Issues and Power Outages on the Island Interconnected System*, which is an extraordinary proceeding in its own right, is expected to continue throughout the remaining schedule of Hydro's GRA.



relief requested in the Application will ensure that Newfoundland Power has the opportunity to earn a fair and reasonable return in 2016 while ensuring the orderly establishment of reasonable rates for consumers. This would be consistent with the provisions of the *Public Utilities Act* and the *Electrical Power Control Act, 1994* and the majority opinion of the Court of Appeal which observed:

“...in choosing to exercise a particular power within the Board’s jurisdiction, the Board must always be mindful whether, in so acting, it will be furthering the objectives and policies of the legislation and doing so in a manner that amounts to a reasonable balance of the competing interests involved.”³

The Regulatory Calendar

The evidence before the Board indicates that the Hydro GRA is extraordinary in the size, scope and complexity of issues raised. These issues include proposed Hydro revenue requirements increases of \$231 million for 2015, review of the prudence of over \$210 million of Hydro expenditures and resolving the longstanding mismatch of Hydro’s costs and rates which has resulted in a current RSP credit balance of \$294 million. Issues relating to Hydro supply reliability and proposed changes in cost of service are also prominent in Hydro’s GRA.⁴

The evidence contains a summary of data related to Hydro’s GRA and Hydro’s first GRA which was filed in 2001. This evidence is reproduced below:⁵

Comparative Hydro GRA Data

	1st GRA	Current GRA
Filing Date	May 31, 2001	July 30, 2013
Registered Intervenors	5	11
RFIs	Over 1,000	Over 2,100
Months to Hearing	4 months	25 months
Start of Public Hearings	September 24, 2001	September 9, 2015
Days of Public Hearing	61	-
Conclusion of Public Hearings	January 29, 2002	-

³ Stated Case, paragraph 144.

⁴ See the response to Request for Information NLH-NP-062.

⁵ See the response to Request for Information NLH-NP-062, page 3, Table 1.



Based upon the array of issues presented in the Hydro GRA and this comparative data, it was Newfoundland Power's evidence that:

“The extraordinary size and scope of issues raised in Hydro's current GRA, together with the proceedings to date, indicate that public hearings for Hydro's current GRA will likely take several months. There is no reason to expect that public hearings on Hydro's current GRA will conclude in less than the 4 months it took for them to conclude on Hydro's 1st GRA. In fact, proceedings to date on Hydro's current GRA indicate that public hearings on Hydro's current GRA will likely take longer than on Hydro's 1st GRA.”⁶

This evidence is consistent with the Board's findings in January 2015 that:

“As a result of the filing of the amended general rate application on November 10, 2014 it is likely that the proceeding, which began with the filing of the original general rate application on July 30, 2013, will not conclude until late 2015 *at the earliest.*” (emphasis added)⁷

The impact of Hydro's GRA on a Newfoundland Power GRA filed on October 16, 2015 was assessed in evidence:

“In Newfoundland Power's next GRA, it is expected, at a minimum, that there will be RFIs submitted by Board staff, the Consumer Advocate, and Hydro. Board staff, the Consumer Advocate, and Hydro are all active participants in Hydro's current GRA. Given the uncertainty associated with the length of public hearings required on Hydro's GRA, it is reasonable to expect that parties interested in Newfoundland Power's next GRA and also participating in Hydro's current GRA will require additional time to interrogate Newfoundland Power's GRA.

This additional time requirement will, in turn, extend the overall length of time and costs associated with a Newfoundland Power GRA filed on October 16, 2015. As time is extended, the requirement for additional information and processes (including updates of costs and results of operations by Newfoundland Power) has the potential to even further extend the time associated with the review of a Newfoundland Power GRA filed on October 16, 2015.

⁶ See the response to Request for Information NLH-NP-062, page 3, lines 13-18.

⁷ See Order No. P.U. 1 (2015), page 3, lines 23-25. Order No. P.U. 1 (2015) was issued *prior* to the Board's decision to review the prudence of over \$210 million of Hydro's expenditures as part of Hydro's GRA; the establishment of the current schedule for Hydro's GRA which indicates public hearings will commence on September 9, 2015; and the delivery of the decision of the Court of Appeal which, in effect, determined that the RSP refund mandated by OC2013-089 must be made to the customers who paid into the RSP.



These potential conflicts and series of delays raises the risk that a Newfoundland Power GRA filed on October 16, 2015 will not result in a final order of the Board on 2016 costs until late in 2016, or possibly 2017.”⁸

The evidence relating to the extraordinary nature of Hydro’s GRA and the foreseeable consequences of Hydro’s GRA on the regulatory calendar is not in dispute.

C. Relief Requested Consistent with Regulatory Practice & Principles

Relief Requested

The 2016 deferred cost recovery of \$4 million proposed in the Application represents the additional cost of financing forecast 2016 capital expenditures required to provide service to customers. These expenditures will not be incurred without prior Board approval pursuant to Section 41 of the *Public Utilities Act*. So, they can be expected to be prudent. The expenditures were not expected to be covered by current customer rates, so their recovery would be reasonable and appropriate.⁹

In the evidence, the amount of this additional cost is shown to be calculated in a manner consistent with the Board’s existing practice for the annual regulation of Newfoundland Power’s forecast returns on rate base for years that are not test years.¹⁰

Regulatory Practice

The Board has approved 5 cost recovery deferrals for Newfoundland Power since 2005. Each of the prior applications effectively allowed Newfoundland Power an opportunity to earn a just and reasonable return which it would not have had without filing a GRA.¹¹

The Board has used a variety of means to assess and determine the appropriateness of Newfoundland Power cost deferrals in advance of approving them. These have included use of values that have been tested in the previous test year.¹² However, the Board has allowed

⁸ See the response to Request for Information NLH-NP-062, page 4, lines 17-34. A delay until 2017 in a final order of the Board on 2016 costs is not consistent with prospective regulation (see the response to Request for Information PUB-NP-006). See also the response to Request for Information PUB-NP-002 which outlines how extended GRA schedules result in higher regulatory costs.

⁹ See the response to Request for Information PUB-NP-001, page 4, lines 29 *et. seq.*

¹⁰ See *2016 Deferred Cost Recovery: Evidence*, page 5, line 24 to page 10, line 27. The appropriateness of the methodology used to calculate the \$4 million proposed deferred cost recovery has not been disputed. The use of an 8.80% cost of equity is opposed by the Consumer Advocate and is further addressed at pages 6-7 of these submissions.

¹¹ See the response to Request for Information PUB-NP-001, page 1, lines 35-38.

¹² See Order Nos. P.U. 40 (2005), P.U. 39 (2006), P.U. 30 (2010) and P.U. 22 (2011), where the deferred cost recoveries were justified on the basis of the expiration of depreciation and other amortizations which were approved in a prior GRA.



deferred cost recovery for Newfoundland Power without full testing of forecast costs on a number of occasions.¹³

The array of circumstances in which the Board has approved deferred cost recovery simply indicates the versatility of this form of regulatory relief. However, in all deferred cost recovery applications, the Board has been satisfied that the deferred cost recovery proposed was appropriate and necessary in the particular circumstances of the application before it.¹⁴

In 2006, Hydro filed a GRA prior to the filing of an expected Newfoundland Power GRA that same year. The scheduling issues raised by having 2 GRAs outstanding at the same time were resolved in Order No. P.U. 39 (2006) when the Board approved 2007 deferred cost recovery of \$7.6 million for Newfoundland Power. This amount included increased depreciation expense related to conclusion of a depreciation true up and increased *forecast* replacement energy costs not reflected in Newfoundland Power customer rates at that time.¹⁵

The Board's approval of the proposed 2016 deferred cost recovery of approximately \$4 million would be consistent with the Board's past determinations on similar Newfoundland Power applications.

Regulatory Principles

Prospective Ratemaking and Intergenerational Equity: The prospective nature of regulation in Newfoundland and Labrador is well established. If Newfoundland Power filed its next GRA on October 16, 2015 the Board, in the current circumstances, might practically determine Newfoundland Power's 2016 costs in late 2016 or 2017. This is not consistent with prospective ratemaking.¹⁶ On the other hand, the Board's approval of the proposed 2016 deferred cost recovery of approximately \$4 million would be consistent with prospective ratemaking.

The principle of intergenerational equity provides that customers in a particular period should pay the costs necessary to provide service in *that* period. The Board's application of this principle has recognized it is not absolute. In the context of Hydro's GRA, the Board's approval of the proposed 2016 deferred cost recovery of approximately \$4 million would be consistent with the Board's past application of this principle.¹⁷

Regulatory Lag and Delayed Cost Recovery: Hydro's costs account for almost 2/3rd of the rates charged by Newfoundland Power to its customers. Hydro's GRA was first filed with the Board in July of 2013. The \$294 million credit balance in Hydro's RSP reflects money collected from customers since 2007. A further \$124 million in 2014 and 2015 costs are proposed to be

¹³ See the response to Request for Information PUB-NP-007.

¹⁴ See the response to Request for Information PUB-NP-001 for a detailed description of Newfoundland Power cost deferral applications that have been approved by the Board.

¹⁵ See the response to Request for Information PUB-NP-001.

¹⁶ See the response to Request for Information PUB-NP-006.

¹⁷ See the response to Request for Information PUB-NP-006.



recovered in future Hydro rates. These 2 items reflect some of the consequences of regulatory lag and delayed cost recovery associated with Hydro's GRA. The regulatory lag associated with Hydro's GRA has had, and is continuing to have, a material impact on Newfoundland Power's customers. Any regulatory lag and delayed cost recovery associated with the proposed 2016 deferred cost recovery of approximately \$4 million for Newfoundland Power is immaterial by comparison.¹⁸

A Newfoundland Power GRA filed on October 16, 2015 prior to conclusion of Hydro's GRA will only further obscure the relationship between costs and customer rates on the Island interconnected system. It could also add to the regulatory lag associated with Hydro's GRA. The Board's approval of the relief requested in the Application will facilitate an orderly reinstatement of customer rates that reasonably reflect costs on the Island interconnected system.

Regulatory Cost Efficiency: Longer regulatory proceedings, including GRAs, will tend to increase the cost associated with regulatory process. A Newfoundland Power GRA running concurrently with the existing Hydro GRA can be expected to increase the length and cost of both proceedings.¹⁹

It is not disputed that the relief sought in the Application is consistent with overall regulatory cost efficiency.

D. Intervenor Submissions

Consumer Advocate

The primary position of the Consumer Advocate is that "The entire application rests on the untested assumption that the rate of return on common equity of 8.80% that was previously approved for 2013, 2014, and 2015 test years remains appropriate for 2016."²⁰

The Consumer Advocate's submission refers to the response to Request for Information PUB-NP-004 to highlight the "...most recently allowed return..." of 8.30% approved on March 23, 2015 by the Alberta Utilities Commission for 2013-2015.²¹ It appears the Consumer Advocate has overlooked Newfoundland Power's 1st Revision to the response to Request for Information PUB-NP-004. This revision shows that on May 26, 2015, the Regie de l'energie Quebec decided to maintain the return on equity of 8.90% established in 2012 for Gaz Metro for 2016 and 2017.²²

¹⁸ See the response to Request for Information PUB-NP-003.

¹⁹ See the response to Request for Information PUB-NP-002 for a description of how a Newfoundland Power GRA, filed in 2015, will contribute to more extended regulatory processes and increased costs.

²⁰ See the Submission of the Consumer Advocate, page 2, lines 26-28.

²¹ Refer to the table provided on page 8, lines 5-6 and lines 10-11 of the Submission of the Consumer Advocate.

²² See the response to Request for Information PUB-NP-004, 1st Revision, Table 1.



Newfoundland Power's current cost recovery, including its allowed return on equity, was approved by the Board in April 2013.²³ In the current circumstances, deferring the next full review of the Company's costs, including the cost of capital, to a Newfoundland Power GRA to be filed June 1, 2016 is justified.

The Consumer Advocate has indicated that "Four of the five precedents cited by NP simply passed through accounting costs in amounts that related directly to previous Board Orders."²⁴ This too appears mistaken. In Order No. P.U. 39 (2006), the Board permitted deferred cost recovery of forecast replacement energy costs related to the 2007 refurbishment of Newfoundland Power's Rattling Brook hydroelectric plant. In Newfoundland Power's view, replacement energy costs are not an "accounting" cost.

Hydro

Hydro's submission raises 2 principal issues. One relates to the Board's approval of the deferral on an interim basis. The other relates to forecast uncertainty.

The Issue of "Interim" Deferral: Hydro stated in its submission that Newfoundland Power's "...Deferred Cost Recovery should be approved for deferral, however only on an interim basis."²⁵

Newfoundland Power *has not applied for* approval on an interim basis.

Newfoundland Power presumes Hydro is proposing an approval similar to that granted in Order No. P.U. 58 (2014) which, in effect, permitted the creation of a deferral account to segregate an amount but left the determination of recovery, if any, of that amount to a later date. The decision in Order No P.U. 58 (2014) was the clear result of the lateness of Hydro's request for deferred recovery:

"Normally this relief is granted where there has been some opportunity for review of the proposals made and the evidence filed. However, as a result of Hydro's approach to the management of its general rate application, including the late filing of the application seeking interim relief, there is no reasonable opportunity at this time to assess the evidence filed in support of Hydro proposals and determine the possible impacts and relevant considerations... While Hydro's proposals raise issues which, as a result of the late filing of the application, cannot be properly addressed at this time, the Board finds that approval in 2014 of a deferral account to segregate an amount associated with the 2014 revenue requirement is necessary to ensure that the Board retains jurisdiction with respect to Hydro's 2014 revenue requirement. Given the extraordinary circumstances, the Board will grant approval to establish a deferral

²³ See Order No. P.U. 13 (2013), page 59.

²⁴ See page 11, lines 20-21 of the Submission of the Consumer Advocate.

²⁵ See page 7 of the Submission of Hydro.



account in relation to Hydro's proposed 2014 revenue requirement.” (emphasis added)²⁶

The Board went on further to state:

“While it is possible that the Board will, after a full review, grant approval for Hydro to recover all or part of the \$45.9 million, *there is no certainty at this time of any recovery.*” (emphasis added)²⁷

To avoid encountering these inconsistencies and difficulties, the Application seeking 2016 deferred cost recovery of approximately \$4 million was filed by Newfoundland Power on *April 15, 2015*. This timing permits adequate opportunity for review of the proposal and the evidence filed in support of it.²⁸ It also provides Newfoundland Power with the flexibility to respond to the Board’s determination.

In Order No. P.U. 39 (2006), the Board approved 2007 deferred cost recovery of \$7.6 million for Newfoundland Power at the time a Hydro GRA was outstanding. In responding to the Consumer Advocate’s submission that the Board should offset prior approved cost deferrals in a subsequent process, the Board observed:

“The Board sets electricity rates on a prospective basis using forecast costs for a test year or years. This is consistent with accepted regulatory principles and established practice and in line with the Board’s mandating legislation. Section 3(a)(ii) of the *EPCA* directs the Board to establish rates wherever practicable based on forecast costs for the supply of power for 1 or more years. Section 80(4) permits the Board to use estimates of the rate base and the revenues and expenses of a public utility when setting rates. The prospective nature of rate setting was also recognized by the Supreme Court in the Stated Case...

“Consistent with regulatory practice and in the interests of a predictable and fair regulatory framework that accepts the necessity and practicality of prospective regulation the Board will not make the offset proposed by the Consumer Advocate.” (emphasis added)²⁹

Hydro’s submission on this matter is not consistent with longstanding regulatory practice of the Board. The 2016 deferred cost recovery of approximately \$4 million proposed in the Application is consistent with longstanding regulatory practice of the Board.

²⁶ Order No. P.U. 58 (2014), pages 7, line 41 to page 8, line 39.

²⁷ Order No. P.U. 58 (2014), page 9, lines 3-5.

²⁸ See the response to Request for Information NLH-NP-074 for a full explanation of Newfoundland Power’s view of Order No. P.U. 58 (2014) including the uncertainty it creates.

²⁹ See Order No. P.U. 39 (2006), page 6, lines 21-27 and page 7, lines 1-3.



Forecast Uncertainty: Hydro indicated in its submission that “...NP’s application contains substantial uncertainty as to a just and reasonable deferred cost amount.” This is incorrect.

The 2016 deferred cost recovery of approximately \$4 million proposed in the Application represents the additional cost for Newfoundland Power to finance the increased 2016 rate base resulting from 2016 capital expenditures required to provide service to customers. The amount is determined in accordance with regulatory practice.³⁰ This is the *only* additional cost that is proposed to be recovered from customers in 2016 which will not have been specifically approved by the Board following Newfoundland Power’s last GRA.³¹

If the Board approves the 2016 deferred cost recovery of \$4 million, then Newfoundland Power’s 2016 customer rates will continue to reflect the tested values approved by the Board in Newfoundland Power’s last GRA.³²

Newfoundland Power observes that variability is inherent in any forecast. This, to use the words of the Board, is a “...necessity and practicality of prospective regulation...”. The forecast evidence filed in support of the Application is consistent in quality and detail with that routinely relied on by the Board for regulatory decision making.³³

E. Conclusion

The extraordinary nature of Hydro’s GRA and the foreseeable consequences of Hydro’s GRA on the regulatory calendar are the primary justification for the relief sought in the Application. To respond to the reality of the current regulatory agenda, the Application seeks approval for (i) the filing of Newfoundland Power’s next GRA by June 1, 2016 and (ii) the 2016 deferred cost recovery of approximately \$4 million.

The amount of the proposed deferral is calculated in a manner consistent with existing Board practice for regulating Newfoundland Power’s returns. The Board’s approval of the proposed 2016 deferred cost recovery would be consistent with the Board’s past determinations on Newfoundland Power deferral applications. This includes Order No. P.U. 39 (2006) which arose from circumstances substantially similar to the present. Similarly, the Board’s approval of the relief requested in the Application would be consistent with its application of regulatory principles. These include the principles of prospective ratemaking, intergenerational equity, the minimization of regulatory lag, the timely recovery of costs and regulatory efficiency.

³⁰ In the Application, the amount of this additional cost is calculated in a manner consistent with the Board’s existing practice for the annual regulation of Newfoundland Power’s forecast returns on rate base for years that are not test years. See *2016 Deferred Cost Recovery*, Evidence, page 5, line 24 to page 10, line 27.

³¹ See the response to Request for Information PUB-NP-007.

³² This is shown in Exhibit 5 to the evidence filed in support of the Application.

³³ See, for example, the forecast evidence in support of Newfoundland Power’s application to establish a 2015 rate of return on rate base which was approved by the Board in Order No. P.U. 51 (2014). Also see the response to Request for Information NLH-NP-053.



Neither the Consumer Advocate nor Hydro appear to dispute either the extraordinary nature of the Hydro GRA or the foreseeable consequences which would result from Newfoundland Power's filing a GRA by October 16, 2015. Both, however, oppose or seek modifications to the relief sought in the Application. Their proposals are not consistent with Board practice and regulatory principles.

In Order No. P.U. 32 (2007), the Board considered how it was to implement the regulatory policy framework contained in the *Electrical Power Control Act, 1994* and the *Public Utilities Act*.³⁴ There, the Board observed:

"The real challenge for the Board, in keeping with its legislative mandate, is to balance oftentimes competing objectives within the regulatory environment to ensure a set of sound and reasoned decisions serving the interests of both customer and utility alike."

Newfoundland Power submits that, in the current circumstances, the appropriate balance favors the Board's approval of the relief sought in the Application.

RESPECTFULLY SUBMITTED,



Peter Alteen, QC
Vice President,
Regulation & Planning

Enclosures

c. Geoffrey Young
Newfoundland and Labrador Hydro

Thomas Johnson, QC
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³⁴ See the response to Request for Information NLH-NP-018.

