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January 9, 2019

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

**Attention: Ms. Cheryl Blundon**  
**Director Corporate Services & Board Secretary**

Dear Ms. Blundon:

**Re: Rate Mitigation Options and Impacts Review**

This correspondence constitutes the response of Nalcor Energy and its Subsidiaries ("Nalcor") with respect to:

1. the Synapse Energy Economics Inc. ("Synapse") Report released January 2, 2019, entitled *Phase 1 Findings on Muskrat Falls Project Rate Mitigation* (the "Synapse Report"); and
2. the Liberty Consulting Group ("Liberty") Report released January 2, 2019, entitled *Final Report on Phase One of Muskrat Falls Project Potential Rate Mitigation Opportunities* (the "Liberty Report").

In recognition that the Muskrat Falls Project would result in a significant increase in rates for electricity customers in the Province, options to manage rate impacts have been a focus for Nalcor for a number of years. Further, since 2017, Nalcor has been an active participant in the Rate Mitigation Committee, sponsored by the Department of Natural Resources. The findings in both the Synapse and Liberty Reports are largely in line with the work Nalcor has performed to date on mitigation of rates for customers.

Nalcor was pleased to assist Liberty, Synapse and Board staff in conducting their work in Phase 1 and looks forward to continuing working with the Board and its consultants through Phase 2.

#### **SYNAPSE REPORT**

Overall, Nalcor agrees that the proposals in the Synapse Report, if realized, can provide substantial mitigation through load growth and the deferral of future capital investments. This is particularly so if the "high scenarios" as outlined by Synapse are achieved. As noted by Synapse, "several aggressive policy initiatives to promote

*electrification, cost-effective CDM initiatives and increased export sales*” will be required to meet that high scenario potential. Synapse’s Phase 2 analysis may affect planning assumptions and thus impact future capital costs. Such analysis should therefore be completed in consideration of the ongoing *Reliability and Resource Adequacy Assessment*, as filed with the Board by Newfoundland and Labrador Hydro (“Hydro”) on November 16, 2018, which will provide guidance on the future system parameters for the Newfoundland and Labrador Interconnected System.

Nalcor acknowledges and supports Synapse’s proposals for further investigation in Phase 2 of this review, particularly in respect of:

1. **Electrification.** Nalcor has identified electrification opportunities in areas similar to those as identified by Synapse. In combination with careful management of peak load and resource availability, Nalcor agrees that increased electrification has potential and should be further examined. Nalcor is willing to work with Synapse to conduct the required studies to increase confidence in the Synapse assumptions for use in evaluation of the potential benefits and costs of an electrification program.
2. **Export Sales.** Nalcor agrees that maximizing potential of export sales during higher value periods is a worthwhile objective. Following interconnection with the North American transmission grid, Hydro and Nalcor Energy Marketing commenced a pilot project to assess optimization of hydraulic resources through “ponding” opportunities (i.e., purchase and import of low cost energy from off-island sources and the export and sale of an offsetting amount of energy at another time when market prices are higher relative to the timing of the imported energy). Supporting increased opportunity imports and export sales through market optimization and ponding should be further analyzed as part of Phase 2.
3. **Conservation and Demand Management (“CDM”).** Nalcor supports bolstering CDM efforts to optimize required capacity. Hydro and Newfoundland Power have cooperated previously on CDM programs and Nalcor looks forward to further analysis of CDM programming opportunities the two companies can undertake to ensure reliable service at least cost, while creating opportunities for increased export sales.
4. **Load Forecasting.** Synapse noted that Hydro has considered several future price and load scenarios and found Hydro’s load forecast process to be reasonable. Nalcor agrees that the effect of price changes on customer load should be analyzed in Phase 2 and supports further efforts to analyze price elasticity as a component of load forecasting efforts.

Finally, Nalcor supports an exploration of rate design issues (including time of use rates) as proposed by Synapse to be part of Phase 2.

### **LIBERTY REPORT**

The Liberty Report identified four general areas for Phase 2 review. Liberty also noted preliminary dollar range impacts to ultimately reduce ratepayer costs (listed below in order of greatest impact). While the potential impacts will be further analyzed in Phase 2, Nalcor agrees with these proposed general areas of analysis for Phase 2 and offers the following comments:

1. **Changes to Muskrat Falls Project (“MFP”) Financing Structure and Allocation of MFP Dividends.** As Liberty noted, this area of review has the greatest potential for rate mitigation - *“dwarfing other alternatives in magnitude”*. Liberty acknowledged Nalcor’s existing analysis of a broad range of options in this area developed through the Rate Mitigation Committee. Note that changes impacting the Muskrat Falls debt financing structure require agreement between the existing financing parties (i.e., Nalcor, the Province and the Government of Canada).
2. **Other Nalcor Dividends.** In respect of the calculation and distribution of various dividends from Nalcor activities (e.g., export sales, Hydro’s return on equity, etc.), opportunities for adjustments in this area have been the subject of analysis by Nalcor. Nalcor awaits Liberty’s analysis on this issue and the Board’s review of the appropriate distribution of such dividends.
3. **Organizational Design.** The organizational structure of Nalcor and Hydro has been the subject of review both internally and externally, including by Liberty. Nalcor’s current organizational structure, implemented in 2016, reflects identified priorities: (a) to ensure successful completion of the Muskrat Falls Project; (b) to prepare the provincial electricity system for integration of Muskrat Falls power; and (c) to have clear separation of (and focus on) the regulated business from the remaining unregulated business operations while continuing its commitment to providing safe, reliable electricity to Hydro’s customers.

As a result, Nalcor has organized its electricity operations into regulated and non-regulated segments. On the regulated side, the structure provides a dedicated focus on its regulated electricity operations and a single executive leadership for this division to ensure the provision of reliable service to Hydro customers. With respect to non-regulated electricity operations, this structure allows for separate focus on completion of the Muskrat Falls Project and utilizing existing and future non-regulated assets to maximize value for the Province. Nalcor is committed to provide clarity on its organizational design during Phase 2.

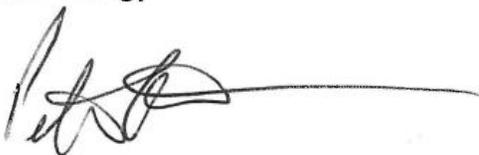
**4. Cost Measures.**

- a) Nalcor welcomes further assessment of Nalcor's operations to determine where efficiencies may be found, whether internal or in conjunction with Newfoundland Power. Cost savings in relation to increasing efficiencies in Nalcor's internal operations should be balanced with the need to maintain reliable service to customers.
- b) As noted by Liberty, any cost savings in relation to Nalcor's generation assets should be balanced with the need to maintain reliable service to customers.
- c) In respect to Liberty's benchmarking of Nalcor's plants against chosen panels of similar sized plants in other jurisdictions, Nalcor has not seen sufficient detail to date on these panels to comment as to whether the benchmarks or metrics used are appropriate. Nalcor looks forward to a further review of Liberty's supporting data in this area (and an opportunity for comment) as part of an analysis of operating and maintenance ("O&M") costs in Phase 2.
- d) In respect of the Water Power Rental Fee paid to the Province, Nalcor awaits Liberty's further analysis and the Board's review of this issue.

In summary, as noted by both consultants, time constraints did not permit a full discussion of certain items as a part of Phase 1. Nalcor observes that (a) some of the assumptions used by Synapse and (b) some of the metrics and calculations employed by Liberty (particularly in respect of FTE allocation, O&M costs and Nalcor operations) will benefit from further discussion with Nalcor representatives as part of Phase 2. Overall, Nalcor has found both the Synapse and Liberty Reports to be informative and generally supportive of the extensive analysis undertaken by Nalcor to date in respect of rate mitigation options. We look forward to working with Liberty, Synapse, the Board and others as part of Phase 2.

Yours truly,

**Nalcor Energy**

A handwritten signature in black ink, appearing to read 'Peter Hickman', followed by a long horizontal line extending to the right.

Peter Hickman  
VP General Counsel & Corporate Secretary