<u>Larry B. Brockman</u>

(Re: Pages 7-19 - marginal cost)

Q. In light of the response to NP-124 NLH, which indicates that although energy may initially drive the need to add new generation, the need for additional capacity to meet increased system demand will occur shortly thereafter, does NP agree that demand as well as energy is a relevant consideration for Hydro in developing marginal cost based rates? If no, why, and when are demand-related marginal cost signals appropriate for Hydro?

A. Yes. Newfoundland Power believes that both demand and energy are relevant in the development of marginal costs. The short-run marginal cost of energy from Holyrood is currently known. However, the long-run incremental costs of demand are uncertain, and as estimated in Hydro's evidence, will occur further in the future.

Hydro has not provided a long-run marginal cost study that would clearly indicate the incremental costs of demand. In the Sample Rate, Hydro is using an embedded demand cost from its cost of service study to provide a marginal demand cost signal. The $84 annual cost per kW used in the Sample Rate is sending an inconsistent demand price signal given that Hydro, at the same time, is not renewing the Interruptible B contract at a cost of $28.20 per kW.