Q. Exhibit RDG-2 relating to the report on the treatment of NP generation:

a. How is embedded generation (i.e., generation embedded in a distribution system) treated in cost of service/rate design in other jurisdictions?

b. What lessons have been learned on the treatment of embedded generation in competitive electricity markets?

c. Page 15 of the report includes an alternative where Hydro would purchase NP thermal generation. Was an alternative considered where instead of purchasing the thermal generation assets, Hydro would purchase the power from NP thermal generation assets while the assets would remain under the ownership of NP; i.e., similar to purchases from IPPs?

d. On page 14 it is stated that "uncertainty as to the Board's desire to introduce marginal cost principles in the costing process" is a disadvantage. Why is this considered a disadvantage, and how does it relate to the design standards listed on page 5?

A. Exhibit RDG-2 relating to the report on the treatment of NP generation:

a. In other jurisdictions that Mr. Greneman is familiar with, customer-owned generation is generally run to serve the customer's own load or for backup purposes and therefore is not included in the utility's cost to serve. However, if there is a system emergency, the utility may request that the customer ensure that its generation is running. In

return for providing support during system emergency, the customer can receive credit under a special contract that recognizes the emergency value of the backup generation or by means of a load management type of incentive. In order to encourage alternative generation resources, such as wind and solar, embedded generation less than a nominal threshold level, e.g., 75 kW, is typically addressed through net metering.

b. There is not currently standard treatment for embedded generation except as noted in (a), above, when a unit is of a nominal size such that it is treated through net metering. In a competitive electricity market where the utility also has an obligation for the supply of power to customers, the value of embedded generation may increase or decrease in relation to competitive locational market prices. If the utility is a distribution-only utility, the value of embedded generation to the utility would be dependent on the ability of the generation to provide necessary service to the delivery system. Embedded or distributed generation in the competitive market is under investigation in some jurisdictions to understand its appropriate treatment by regulated distribution entities (e.g., need for standby rates) and within the competitive market. As noted above, net metering is still in place in many jurisdictions for smaller facilities.

c. Yes, this alternative was considered. Table 6 in the Treatment of NP Generation report provides sufficient alternatives for the eventual value that might be negotiated as part of the contract discussions.

d. In an embedded cost environment, fully-allocated cost of service is the standard to assess the degree to which revenue requirement is

equitably apportioned among customer classes. The avoided cost alternative was listed as a potential disadvantage with respect to uncertainty of acceptance by the Board of marginal cost principles in the costing process. With respect to the design standards on page 5, the introduction of marginal cost principles in embedded costing relates to equitability among customer classes, relationship to cost causation and practical implications.