

1 **Q. Please explain the relationship between Purchased Power Expense and Total**
2 **Revenue from Rates. In the response, please explain why in NP's five year actual**
3 **average power purchases as a percentage of total revenue was 64.55% and in the**
4 **2016 forecast of this application, the same ratio is 65.69% (which results in a \$7.4**
5 **million increase in expense in the forecast year). Please illustrate how the Energy**
6 **Supply Cost Variance deferral account impacts the calculation.**

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8 **A. A. Background**
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10 In general, the relationship between Purchased Power Expense and the Total Revenue
11 from Rates primarily reflects the proportion that Newfoundland Power's Purchased
12 Power Expense is of Newfoundland Power's overall cost to serve customers. A change
13 in the ratio of Purchased Power Expense to total Revenue from Rates (the "Ratio") is an
14 indication of the relative changes in Purchased Power Expense to changes in the
15 Company's overall costs.

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17 If the Ratio is increasing over time this indicates that Purchased Power Expense is
18 increasing at a higher percentage rate than Newfoundland Power's overall costs and vice
19 versa. During short periods of time, typically between general rate applications, the Ratio
20 will also be influenced by a number of factors such as the operation of regulatory
21 mechanisms that allow recovery of certain cost variances in Purchased Power Expense in
22 the future. The Board has approved Newfoundland Power's deferred recovery of certain
23 abnormal Purchased Power Expense variances including variances in demand costs
24 which are part of the utility rate paid by the Company for power supply.¹

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26 **B. 64.55% vs. 65.69%**
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28 Newfoundland Power has reviewed possible sources for the 64.55% and the 65.69%
29 referred to in this Request for Information ("RFI"). The basis of this calculation was not
30 provided in the RFI. It appears the 64.55% ratio was based on the Company's annual
31 returns to the Board in which revenue *includes* other revenue. The 65.69% appears to
32 have been determined from Exhibit 1, of Schedule 1 to the Application which *excludes*
33 other revenue.

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35 The inconsistent treatment of other revenue appears to be the primary reason for the
36 difference between the 64.55% and the 65.69% provided in the RFI. When other revenue
37 is removed from the calculation, the 64.55% figure becomes 65.58%. 65.58% is 0.11%
38 different from the 2016F figure of 65.69%.

¹ The variance is determined on an average cost per kWh basis.

1 **C. The Illustrations**

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3 This RFI specifically requests an illustration of how the Energy Supply Cost Variance
4 mechanism impacts the calculation of the Ratio. The Energy Supply Cost Variance (the
5 “ESCV”) mechanism is the regulatory mechanism that permits Newfoundland Power to
6 recover from, or refund to, customers, through the annual Rate Stabilization Account
7 adjustment, variances between actual purchased power *energy* costs and the purchased
8 power *energy* costs used to determine customer rates.² Complementary to ESCV
9 mechanism is the Demand Management Incentive (“DMI”) mechanism that permits
10 recovery (refunds) for variance between actual purchased power *demand* expenses and
11 the purchased power *demand* expenses used to determine customer rates.³

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13 Tables 1, 2 and 3 provide a calculation of the Company’s Purchased Power Expense,
14 Revenue from Rates, and Ratio of Purchased Power Expense to Revenue from Rates
15 respectively for actual 2010 to 2014 results and the forecast for 2016. The tables provide
16 the information with and without the impact of the ESCV and DMI mechanism.

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**Table 1: Total Purchased Power Expense
Including the impact of the DMI mechanism
2010 – 2014 & 2016F
(\$000’s)**

	2010	2011	2012	2013	2014	2016F
Purchased Power Expense ⁴	355.4	365.6	377.5	392.9	404.5	424.7
DMI impact ⁵	1.0	1.8	0.8	(0.4)	0.6	0.0
Total	356.4	367.4	378.3	392.5	405.2	424.7

² The variance is determined on an average cost per kWh basis.

³ The variance is determined on an average cost per kWh basis.

⁴ Weather Adjusted.

⁵ A DMI impact that is greater than zero is a savings that flows back to customers.

**Table 2: Total Revenue from Rates
Including the impact of the ESCV mechanism
2010 – 2014 & 2016F
(\$000's)**

	2010	2011	2012	2013	2014	2016F
Revenue from Rates ⁶	535.3	552.6	561.2	586.8	619.5	637.7
ESCV impact ⁷	2.2	6.9	9.7	7.8	1.8	7.7
Total	537.5	559.5	570.9	594.7	621.3	424.7

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**Table 3: Ratio of Revenue from Rates to
Purchase Power Expense
2010 – 2014 & 2016F
(%)**

	2010	2011	2012	2013	2014	2016F
Without DMI, ESCV impact (A)	66.39	66.16	67.27	66.96	65.29	66.60
With DMI, ESCV impact (B)	66.31	65.67	66.26	66.00	65.22	65.80
Difference (A – B)	0.08	0.49	1.01	0.96	0.07	0.80

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Table 3 shows that in every year from 2010 to 2014 and 2016 forecast, the ratio of Revenue from Rates to Purchased Power Expense is higher without the impact of the DMI and ESCV considered. The difference is mostly related to the ESCV mechanism as the impact on the ratios of the DMI mechanism is smaller.

10 The average of the ratios, *without* the DMI and ESCV impacts from 2010 to 2014 is
11 66.40% compared to 2016F of 66.60%. The 0.20% higher ratio in 2016F reflects that the
12 forecast results in Purchased Power Expense increasing *more* than the Revenue from
13 Rates relative to the actual five year historic average.

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15 The average of the ratios, *with* the DMI and ESCV impacts from 2010 to 2014 is 65.88%
16 compared to 2016F of 65.80%. The 0.08% lower ratio in 2016F reflects that the impact
17 of the DMI and the ESCV results in Purchased Power Expense increasing *less* than
18 Revenue from Rates relative to the actual five year historic average. Given the impact of
19 ESCV is larger than the DMI mechanism, the overall impact that the mechanisms have
20 on the Ratios is primarily due to the ESCV mechanism.

⁶ Weather Adjusted.

⁷ An ESCV impact that is greater than zero is a cost to customers that is recovered through the Company's Rate Stabilization Account adjustment.