Q. Page 1, Schedule I: Newfoundland Power states that cost recovery deferrals have been approved for Newfoundland Power outside the context of a general rate application on separate occasions. On page 5, Newfoundland Power provides a synopsis of the Board orders. Please provide the circumstances of each application for cost recovery deferral and an explanation of how the circumstances are similar or different to the background provided in this application. Include in the response the anticipated timing of Newfoundland Power's next general rate application filing when each application was filed and the details of each approval.

A. **A. Attachment**

Attachment A to the response to Request for Information PUB-NP-001 provides details in tabular form concerning the 5 cost recovery deferral applications (collectively, the "prior applications"), including for each application:

(a) the Board order approving the deferred cost recovery;
(b) the year of filing of the application for deferred cost recovery;
(c) the year for which deferred cost recovery was approved;
(d) the amount of deferred cost recovery approved;
(e) the costs for which deferred cost recovery was approved;
(f) the anticipated timing of filing for the Company's next general rate application ("GRA"), at the time of the application for deferred cost recovery;
(g) the anticipated test period for the GRA described in (f);
(h) the actual timing of filing for the Company's next GRA; and
(i) the actual test period for the Company's next GRA.

B. Prior Applications of Newfoundland Power

The Issue of GRA Deferral

All of the prior applications were based upon Section 80 of the *Public Utilities Act.* Each approval for deferred cost recovery effectively allowed Newfoundland Power an opportunity to earn a just and reasonable return on a prospective basis.

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. Because of this, the deferred cost recovery approved effectively deferred a Newfoundland Power GRA.

Types of Costs Deferred

The Board has approved deferred cost recovery for a range of different utility costs.

These have included the expiration of depreciation and other amortizations.[1] They have also included costs which were not factored into the making of Newfoundland Power's then current customer rates.[2] This range of costs has specifically included deferred cost recovery to improve Newfoundland Power's return in a year.[3]

Circumstances Justifying Deferred Cost Recovery

The circumstances supporting deferral of a Newfoundland Power GRA in the prior applications were varied.

In 2005, following settlement of a major tax case, Newfoundland Power was granted deferred cost recovery for 2006 because filing a GRA in that year was impractical.[4] At the time of the 2005 application, it was anticipated that a Newfoundland Power GRA would be filed in 2006 with a 2007 test year.[5]

In 2006, Hydro filed a GRA prior to the filing of a Newfoundland Power GRA which was anticipated to be filed that same year. As a result, Newfoundland Power sought deferred cost recovery to enable the Company to earn a reasonable return in 2007 while permitting customer rates to be established for the Island interconnected system in an orderly manner.[6]

For each of 2011 and 2012, deferred cost recovery was approved to effectively counter the impact of expiring regulatory amortizations. In each case, it was anticipated that the next Newfoundland Power GRA would be filed in 2012 with a 2013 test year.[7]

The deferred cost recovery to improve Newfoundland Power's 2012 return was granted following the Board's decision to suspend operation of the automatic adjustment formula in 2011.[8] In 2012, the Company filed an application to establish a fair return on equity for 2012. The Board approved the deferred cost recovery of the difference between the allowed return on equity reflected in Newfoundland Power's then current customer rates

[1] See Order Nos. P.U. 40 (2005), P.U. 39 (2006), P.U. 30 (2010) and P.U. 22 (2011).
[2] See Order No. P.U. 39 (2006), where the Board approved the deferred cost recovery of approximately $1.8 million in replacement energy costs related to the 2007 refurbishment of Newfoundland Power's Rattling Brook hydroelectric plant.
[3] See Order No. P.U. 17 (2012), where the Board approved the deferred cost recovery of approximately $2.5 million which represented the difference between a 8.38% and 8.80% 2012 return on equity for Newfoundland Power.
[4] See Order No. P.U. 40 (2005), page 12, lines 9-15.
[5] See *Newfoundland Power's 2006 Accounting Policy Application*, page 3, lines 13-14.
[6] See Order No. P.U. 39 (2006), page 4, lines 16-20.
[7] The requirement to file a GRA in 2012, with a 2013 test year, was originally created following Newfoundland Power's 2010 GRA in Order No. P.U. 43 (2009). Order Nos. P.U. 30 (2010) and P.U. 22 (2011) approved the respective deferred cost recoveries for 2011 and 2012.
[8] See Order No. P.U. 25 (2011).

and an agreed 2012 return on common equity of 8.8% in advance of a GRA previously ordered to be filed in 2012.[9]

Determining the Appropriateness of the Amount of Deferred Cost Recovery

The Board has used a variety of means to assess and determine the appropriateness of cost deferrals in advance of approving them.

These have included use of values that have been tested in the previous test year.[10] The Board has effectively tested the appropriateness of cost deferrals in standalone deferred cost recovery applications.[11] Capital budget applications have provided the Board with a reasonable basis for establishing the value of an item for deferred cost recovery.[12] The Board has also used agreement between an applicant and intervenor as a basis for determining the appropriateness of deferred cost recovery.[13]

Regulatory Practice

The Board has approved deferred cost recovery for Newfoundland Power in each of the prior applications because it concluded it was an appropriate means to permit Newfoundland Power an opportunity to earn a just and reasonable return in the succeeding year, pursuant to Section 80 of the *Public Utilities Act*.

Past Board approvals have covered a range of utility costs. The circumstances supporting deferred cost recovery (in the absence of a GRA) have also been diverse. The means by which the Board has assessed and determined the appropriateness of deferred cost recoveries in advance of approving them has similarly been varied.

Deferred cost recovery is a regulatory tool that permits the Board to authorize recovery of costs not reflected in the determination of existing customer rates without the requirement of a GRA. 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 applications for deferred cost recovery, including each of the prior applications, the Board has been satisfied that the deferred cost recovery proposed was appropriate and necessary in the particular circumstances.

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9 See Order No. P.U. 43 (2009), page 3, lines 3-8.

10 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.

11 In Order No. P.U. 40 (2005), the Board determined the appropriate amount of a deferred revenue accrual, in part, by assessing the reasonableness of a tax settlement entered into by Newfoundland Power and the Canada Revenue Agency after the prior test year.

12 In Order No. P.U. 39 (2006), the additional replacement energy costs relating to the 2007 refurbishment of Newfoundland Power's Rattling Brook hydroelectric plant were considered by the Board as part of the Company's 2007 capital budget application.

13 The Board approval of the deferred cost recovery to improve Newfoundland Power's 2012 return in Order No. P.U. 17 (2012) was the subject of a settlement agreement between Newfoundland Power and the Consumer Advocate.

In Order No. P.U. 4 (2014), the Board considered a recent Newfoundland and Labrador Hydro ("Hydro") application for deferred cost recovery. There, in describing the use of deferred cost recovery, the Board observed:

> "Allowing for the recovery of unanticipated expenses outside of a test year is an extraordinary measure that the Board will order only when it is satisfied that it is ***appropriate and necessary in the circumstances***."[14] (emphasis added)

C. Application to the Current Circumstances

The Current Circumstances

The customer rates established following Newfoundland Power's last GRA became effective on July 1, 2013.[15] Newfoundland Power's last GRA order included the directive that Newfoundland Power's next GRA be filed by June 1, 2015, to establish customer rates for 2016.

On July 30, 2013, Hydro filed its currently outstanding GRA (the "amended Hydro GRA"). The amended Hydro GRA has been extraordinary. This is due, at least in part, to the magnitude and complexity of the issues raised in Hydro's amended GRA. It is also attributable to the length of proceedings associated with it.

It is reasonable to expect that the conclusion of proceedings on the amended Hydro GRA will not occur before the end of 2015. It is also reasonable to conclude that both the amended Hydro GRA and Newfoundland Power's next GRA cannot both be concluded before the end of 2015.

Consistency with Regulatory Practice

The circumstances disclosed in the evidence filed in support of the Application indicate the Board's approval of the 2016 deferred cost recovery is appropriate and necessary in the circumstances.

The 2016 deferred cost recovery of $4 million proposed by Newfoundland Power, 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.

It is also reasonable and appropriate because it effectively allows (i) Newfoundland Power an opportunity to earn a just and reasonable return in 2016, and (ii) deferral of

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[14] See Order No. P.U. 4 (2014), page 5, lines 17-19.
[15] See Order No. P.U. 23 (2013).

Newfoundland Power's next GRA to June 1, 2016, to establish customer rates for 2017. Deferral of Newfoundland Power's next GRA will permit the Board the opportunity to conclude proceedings on the amended Hydro GRA before considering Newfoundland Power's next GRA. Given (i) the magnitude of the issues raised in Hydro's GRA and (ii) relative proportion of Newfoundland Power's cost of supply to its total cost to serve its customers, such a course is broadly consistent with the practical application of regulatory principles.

In 2006, the Board approved 2007 deferred cost recovery of $7.6 million for Newfoundland Power. This enabled Newfoundland Power to defer a GRA and positioned the Company to file its GRA following conclusion of the Hydro GRA which was before the Board at the time of Newfoundland Power's application for deferred cost recovery. The circumstances surrounding this prior application are substantially similar to the current circumstances. In granting the 2007 deferred cost recovery proposed by Newfoundland Power, 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."[16]

The Board's approval of the 2016 cost recovery deferral of approximately $4 million proposed in the Application is consistent with regulatory principles and practice, including the Board's approvals on the prior applications.

D. Further Information

For further information on the impact of the Board's approval of the Application on GRA costs, refer to the response to Request for Information PUB-NP-002.

For further information on the impact of the Board's approval of the Application on (i) regulatory lag and cost recovery and (ii) regulatory cost efficiency, refer to the response to Request for Information PUB-NP-003.

[16] See Order No. P.U. 39 (2006), page 6, lines 21-27.

For further information on the implications of the Board's approval for prospective ratemaking and inter-generational equity, refer to the response to Request for Information PUB-NP-006.

For further information on the appropriateness of the Board's approval of 2016 deferred cost recovery of $4 million for Newfoundland Power without full testing of forecast costs, refer to the response to Request for Information PUB-NP-007.

Prior Deferred Cost Recovery
Application Details

	Deferral Application				Next GRA Expected		Next GRA Actual	
Approval (a)	**Year of Filing (b)**	**Year of Recovery (c)**	**Amount ($millions) (d)**	**Deferred Recovery Approved (e)**	**Year of Filing (f)**	**Test Period (g)**	**Year of Filing (h)**	**Test Period (i)**
Order No. P.U. 40 (2005)	2005	2006	5.8	Increased depreciation expense related to the conclusion of a depreciation true-up in 2005.	2006	2007	2007	2008
Order No. P.U. 39 (2006)	2006	2007	7.6	(i) Increased depreciation expense related to the conclusion of a depreciation true-up in 2005, and (ii) forecast replacement energy costs related to 2007 refurbishment of Rattling Brook hydroelectric plant.	2007	2008	2007	2008
Order No. P.U. 30 (2010)	2010	2011	2.4	Net amount of expiring regulatory amortizations.	2012	2013	2012	2013/14
Order No. P.U. 22 (2011)	2011	2012	2.4	Net amount of expiring regulatory amortizations.	2012	2013	2012	2013/14
Order No. P.U. 17 (2012)	2012	2012	2.5	Difference between 8.38% and 8.80% 2012 return on equity.	2012	2013	2012	2013/14