

1 **Q. If the Newfoundland and Labrador Hydro Amended General Rate Application**  
 2 **were, for any reason, not to be concluded in 2016, discuss the impacts of the**  
 3 **deferred cost recovery and the delayed filing of a full Newfoundland Power General**  
 4 **Rate Application on Newfoundland Power Inc.'s costs, revenues and rate of return**  
 5 **and on Newfoundland Power's customers, including the effect on inter-generational**  
 6 **equity.**

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 8 **A. A. Summary Information**  
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10 Table 1 shows Newfoundland Power's current forecast of revenues and returns for 2016  
 11 and 2017, (designated by F) and the forecast of revenues and returns for 2016, reflecting  
 12 the proposals in the Application (designated 2016R).  
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**Table 1**  
**Summary of Forecast Revenues and Returns**  
**2016-2017**

	<b>2016F</b>	<b>2016R</b>	<b>2017F</b>
<b>Revenues (\$000,000s)</b>	646.5	646.5	648.7
<b>Return on Rate Base</b>	7.06%	7.32%	6.68%
<b>Return on Equity</b>	8.08%	8.66%	7.15%

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 16  
 17 The deferred cost recovery proposed in the Application will provide Newfoundland  
 18 Power the opportunity to achieve a return on equity of 8.66% in 2016. If Newfoundland  
 19 and Labrador Hydro's ("Hydro") amended general rate application ("GRA") was not  
 20 concluded in 2016, then Newfoundland Power would still have an opportunity to earn a  
 21 just and reasonable return in 2016 on a prospective basis.  
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23 If the deferred cost recovery proposed in the Application were not approved, and Hydro's  
 24 GRA was still ongoing through 2016, then it is possible that the Board might practically  
 25 be determining Newfoundland Power's 2016 costs in late 2016, or 2017. This would not  
 26 provide Newfoundland Power a reasonable opportunity to recover its 2016 costs on a  
 27 prospective basis.  
 28

29 If the deferred cost recovery proposed in the Application were approved, and  
 30 Newfoundland Power were to file a GRA in 2016 with a 2017 test year, it would have the  
 31 opportunity to recover (i) its 2016 costs, including a return on rate base determined by  
 32 adjusting the parameters in Order No. P.U. 13 (2013) in a manner consistent with Board  
 33 practice, and (ii) its forecast 2017 costs, including a return on rate base determined by the  
 34 Board to be appropriate for 2017.

1 The deferred cost recovery would not have a material impact on Newfoundland Power's  
2 forecast of 2017 revenues or returns.<sup>1</sup>  
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4 **B. Ratemaking is Prospective**  
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6 The prospective dimension of regulation in Newfoundland and Labrador is well accepted.  
7 In the Newfoundland and Labrador Court of Appeal's majority opinion in a stated case  
8 presented by the Public Utilities Board in 1996, it was indicated that:  
9

10 "The process of rate setting is generally prospective by nature...In  
11 developing the utility's requirements, the Board focuses on a "test year" as  
12 the basis for its estimates and adjustments. Traditionally, in North  
13 America the test year was chosen as the latest 12 month period for which  
14 complete data were available. More recently, due largely to inflation,  
15 boards adopted a forward-looking test year which in effect amounts to a  
16 forecast of what expenses and costs, and hence revenue requirements, will  
17 be. This has been the practice of the Board and is supported by the  
18 [*Public Utilities Act*] and the [*Electrical Power Control Act*]." (Stated  
19 Case, para. 77)  
20

21 In Order No. P.U. 39 (2006), the Board considered a Newfoundland Power application to  
22 defer filing of its next general rate application until conclusion of a then outstanding  
23 Hydro general rate application. Newfoundland Power's application sought, amongst  
24 other things, deferred cost recovery of increased depreciation expense related to the  
25 conclusion of a true-up amortization and replacement energy costs.  
26

27 In granting the order requested by Newfoundland Power, the Board observed:  
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29 "The Board sets electricity rates on a prospective basis using forecast costs  
30 for a test year or years. This is consistent with accepted regulatory  
31 principles and established practice and in line with the Board's mandating  
32 legislation. Section 3(a)(ii) of the *EPCA* directs the Board to establish  
33 rates wherever practicable based on forecast costs for the supply of power  
34 for 1 or more years. Section 80(4) permits the Board to use estimates of  
35 the rate base and the revenues and expenses of a public utility when  
36 setting rates." (at page 6)

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<sup>1</sup> The principal impact of the deferred cost recovery on Newfoundland Power's 2017 forecast relates to the carrying costs of the deferred recovery for 2017.

1 On the matter of adjusting prior year's costs, the Board recognized that such adjustment  
2 could be inconsistent with the prospective nature of regulation:  
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4 "Consistent with regulatory practice and in the absence of special  
5 circumstances, the Board does not look back to the actual results and make  
6 adjustments to ongoing costs to reflect the differences between forecast  
7 and actual. The Board finds that such an adjustment would be retroactive  
8 in nature and is inappropriate in the circumstances in the absence of  
9 language in the original Order to ground such an adjustment. Consistent  
10 with regulatory practice and in the interests of a predictable and fair  
11 regulatory framework that accepts the necessity and practicality of  
12 prospective regulation the Board will not make the offset proposed by the  
13 Consumer Advocate." (at pages 6-7, Order No. P.U. 39 (2006))  
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### 16 **C. The Issue of Inter-generational Equity**

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#### 18 ***The Deferred Cost Recovery Sought in the Application***

19 The 2016 deferred cost recovery of approximately \$4 million amounts to just over 0.6%  
20 of Newfoundland Power's forecast 2016 revenue from rates. If the deferred cost recovery  
21 proposed in the Application is approved, the future recovery of this amount results in  
22 customers in future years paying \$4 million of 2016 costs. The customer impact of any  
23 amortization of the \$4 million deferred cost recovery sought in the Application would be  
24 small.<sup>2</sup>  
25

26 The principle of inter-generational equity provides that customers in a given period  
27 should pay the cost necessary to provide service in *that* period. The practical application  
28 of this principle by the Board is tempered by regulatory circumstances. For example,  
29 deferred recovery or amortization of a variety of costs over periods of 3 to 5 years has  
30 been routinely authorized by the Board.<sup>3</sup>  
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32 In Order No. P.U. 32 (2008), the Board considered the principle of inter-generational  
33 equity in the context of a Hydro deferred recovery application and found:  
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35 "It has generally been accepted that a reasonable amortization period for a  
36 Major Extraordinary Repair is three to five years. This addresses inter-  
37 generational equity issues and generally coincides with the usual periods  
38 between general rate applications." (at page 3)

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<sup>2</sup> A 3 year recovery amortization of a \$4 million deferral would result in an average bill impact of approximately 0.2%; a 5 year recovery amortization would result in a bill impact of approximately 0.1%.

<sup>3</sup> See, for example, Order Nos. P.U. 19 (2003), P.U. 32 (2007), P.U. 43 (2009) and P.U. 13 (2013).

***The Broader Context***

The current rate paid by Newfoundland Power to Hydro for wholesale electricity supply was established 8 years ago in 2007. Since then, changes in supply and demand on the Island interconnected system and changes in Hydro's costs have substantially altered the degree to which this rate reflects costs. These changes have continuing inter-generational equity aspects which are substantially greater and more complex than any posed by Newfoundland Power's Application.

At March 31, 2015, the credit balance in Hydro's Rate Stabilization Plan was approximately \$294 million. This represents an amount due to Hydro's customers in the future as a result of rates paid which were in excess of Hydro's approved cost of service. Rebalancing Hydro's rates to its current costs is a primary goal of Hydro's outstanding general rate application.

In Order Nos. P.U. 56 and P.U. 58 (2014), the Board approved deferral, but not recovery, of a total of approximately \$56 million in 2014 Hydro costs. These costs are currently subject to the Board's prudence review, which is part of Hydro's general rate application. The final recovery, if any, of these amounts from customers in the future will be determined as part of Hydro's outstanding general rate application.

Hydro's amended general rate application forecasts a 2015 net income deficiency of approximately \$68 million which is sought to be recovered in the future. The final recovery, if any, of these amounts from customers in the future will be determined as part of Hydro's outstanding general rate application.

***Inter-generational Equity in Perspective***

The deferred cost recovery proposed by Newfoundland Power in the Application is consistent with the Board's practice and past application of the principle of inter-generational equity.

Hydro's outstanding general rate application raises substantially larger and more complex issues of inter-generational equity.

These facts imply that, from a consumer perspective, rebalancing Hydro's rates to its current costs before reassessing Newfoundland Power's rates would be the best practical application of the principle of inter-generational equity to the circumstances currently before the Board. The deferred cost recovery proposed by Newfoundland Power in the Application is consistent with this.