

1 Q. **Reference: Grant Thornton Financial Consultants Report, dated August 23, 2019.**

2 Please provide the rationale for the use of the flat monthly fuel cost for the operation of  
3 the test year RSP as identified at page 27 of the Grant Thornton Report.

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6 A. In its “2017 GRA Compliance Application,” Newfoundland and Labrador Hydro (“Hydro”)  
7 proposed to compute the Rate Stabilization Plan (“RSP”) monthly fuel cost variations based  
8 on the difference between the actual monthly cost of No. 6 fuel and the annual average  
9 Test Year Cost of Service No. 6 Fuel Cost (\$/Can /bbl.) of \$105.90 per barrel.<sup>1</sup> Hydro’s  
10 proposed change will:

11 i. Align the calculation of monthly No. 6 fuel cost variations in the RSP with the  
12 calculation of fuel cost variations in the Revised Energy Supply Cost Variance  
13 Deferral Account (which is currently approved to operate using the annual average  
14 test year No. 6 fuel price);<sup>2</sup> and

15 ii. Result in a lower 2019 Test Year No. 6 fuel cost reflected in the 2019 Test Year  
16 revenue requirement for the Island Interconnected System (as the weighted  
17 average cost for 2019 under the monthly forecast is \$109.59 per barrel).

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19 **Revised Energy Supply Cost Variance Deferral Account**

20 Due to the material variability in the 2019 Test Year monthly No. 6 fuel cost forecast (i.e.,  
21 from a low price of \$91.06 per barrel to a high of \$117.27), the approval of the test year  
22 monthly fuel forecast for the operation of the RSP can result in earnings gains or losses for  
23 Hydro throughout the year. Potential earnings variability results from the inconsistency in  
24 the calculations of the financial impact of fuel cost variations between the Revised Energy  
25 Supply Cost Variance Deferral Account and the RSP. With the introduction of off-island  
26 purchases into the Revised Energy Supply Cost Variance Deferral Account balance

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<sup>1</sup> Historically, RSP fuel cost variations have been calculated based on the difference between the actual cost of No. 6 fuel each month and the forecast monthly No. 6 fuel cost forecast that was used to compute the annual average Test Year Cost of Service cost of No. 6 fuel per barrel.

<sup>2</sup> The proposed definition of the Revised Energy Supply Cost Variance Deferral Account is provided in Appendix A, of Exhibit 8, to the “2017 GRA Compliance Application.”

1 calculations, the potential financial impact of this variability is now greater than in previous  
2 years.

3  
4 To illustrate the potential financial impact with respect to the difference in the fuel costs  
5 between the RSP and the Revised Energy Supply Cost Deferral Account, it is helpful to  
6 examine the result if the forecast off-island purchases did not materialize. In that scenario,  
7 Hydro would be required to generate most of this energy at Holyrood. Under the average  
8 annual test year approach the cost of Holyrood fuel would be \$105.90 per barrel and there  
9 would be no earnings impact on Hydro as the cost deferred would equal the Holyrood cost  
10 incurred.

11  
12 Under the monthly test year fuel cost approach, the weighted average fourth quarter cost  
13 at Holyrood to replace the off-island purchases would be \$100.32 per barrel which is \$5.48  
14 per barrel less than the cost deferred in the Revised Energy Supply Cost Variance Deferral  
15 Account. Hydro has forecast 134 GWh in off-island purchases in the fourth quarter 2019  
16 (equivalent to approximately 230,000 barrels of No. 6 fuel). Due to the cost per barrel  
17 difference between the monthly and annual test year cost, if there were no off-island  
18 purchases in the fourth quarter 2019, Hydro would defer a higher No. 6 fuel cost than it  
19 would incur which would increase 2019 earnings by approximately \$1.2 million.

#### 20 21 **2019 Test Year Revenue Requirement**

22 In computing projected revenue deficiency for the first quarter of 2019, Hydro determined  
23 that the 2019 revenue requirement related to recovery of No. 6 fuel is impacted by the  
24 monthly variability of the No. 6 fuel forecast for the 2019 Test Year. For the 2019 Test Year,  
25 the fuel forecast was based on the RSP fuel rider forecast for the period July 1, 2019, to  
26 June 30, 2020.

27  
28 Table 1 provides the monthly No. 6 fuel cost forecast used to compute the annual average  
29 test year Cost of Service No. 6 fuel cost.

**Table 1: 2019 Test Year Monthly No. 6 Fuel Forecast per barrel (\$Cdn)**

<b>2019 Test Year Calendar Month</b>	<b>RSP Rider Forecast Month</b>	<b>Test Year RSP Monthly No. 6 Fuel Forecast (\$/Cdn)</b>
January	January 2020	117.72
February	February 2020	117.17
March	March 2020	116.21
April	April 2020	114.94
May	May 2020	114.28
June	June 2020	114.29
July	July 2019	95.50
August	August 2019	93.08
September	September 2019	91.06
October	October 2019	93.23
November	November 2019	98.83
December	December 2019	104.63
<b>Simple Average</b>		<b>105.90<sup>3</sup></b>
<b>Weighted Average</b>		<b>109.59</b>

1 Using the monthly forecast as the basis for determining the 2019 Test Year fuel cost, the  
2 January 2020 No. 6 fuel cost per barrel would be used to determine the projected test year  
3 No. 6 fuel cost for January 2019. The same approach would apply for February 2019 to June  
4 2019 in that the 2020 monthly fuel forecast values (in which the fuel price forecast was at  
5 its highest levels) is used to compute the 2019 Test Year fuel cost for the first six months of  
6 2019. Hydro's 2019 Test Year forecast has the highest forecast No. 6 fuel consumption in  
7 the first quarter of 2019; therefore, the use of the monthly test year forecast values would  
8 contribute a higher Island Interconnected System revenue requirement for the 2019 Test  
9 Year than if the average annual No. 6 fuel cost per barrel of \$105.90 per barrel was used in  
10 computing revenue requirement. Please see Hydro's response to PUB-NLH-012 for further  
11 discussion.

12

### 13 **Conclusion**

14 Hydro believes the use of the annual average Test Year Cost of Service No. 6 Fuel Cost  
15 (\$/Can /bbl.) in the RSP creates consistency with Hydro's other deferral accounts which

<sup>3</sup> The No. 6 fuel cost forecast per barrel is rounded to the nearest \$0.05.

1 currently operate on an annual average, allows the RSP to operate as intended to smooth  
2 earnings fluctuations as a result of variations in fuel price, and is more understandable and  
3 more reasonable for use in determining the No. 6 fuel cost to be included in the 2019 Test  
4 Year.