

1 Q. Re: “Newfoundland and Labrador Hydro Cost of Service Methodology Review  
2 Application,” Pre-Filed Testimony of Andrew McLaren, August 5, 2019, p.  
3 18/18-19.

4 The InterGroup Consultants Ltd. (“InterGroup”), in line with The Brattle Group’s  
5 (“Brattle”) recommendation, indicates the preference that Muskrat Falls power  
6 purchases be classified according to the system load factor, as opposed to  
7 Hydro’s recommendation that the equivalent peaker methodology be adopted.  
8 On page 18 (lines 18-19), InterGroup states that, with respect to the  
9 classification of the Muskrat Falls facility, “. . . unusually high or low baseload  
10 investment may distort the energy portion of the classification.”

11 a) Please elaborate on what is meant by “distort” and explain how high or  
12 low baseload investment gives rise to distortion?

13 b) Does InterGroup agree that, in general, it is more common that large  
14 generation projects built to lower energy costs will experience significant cost  
15 overruns, as compared to peaker projects that take far less time to construct?  
16 If yes, does InterGroup agree that treating a material portion of cost over-runs  
17 as energy-related is consistent with cost-causality? If no, why not?

18 A. a) The cited reference is noting the conclusions of Brattle [Brattle report page  
19 36].

20 The Brattle conclusion is valid, in that any time an analysis is conducted that splits  
21 costs into two components (demand and energy in this case) and then completely  
22 fixes the value of one component (demand, via the Equivalent Peaker  
23 methodology), the residual component (energy) can swing wildly depending on the  
24 total that one is trying to arrive at (in this case, the total cost of the baseload plant).  
25 This approach concentrates the entire risk associated with actually experienced  
26 baseload plant cost swings on the energy component and neuters any effect on  
27 the capacity component (since capacity cost is fixed based on a theoretical  
28 concept that does not have to be proven in fact). The result is that the energy  
29 component takes all swings for cost risk, and for imprudent expenditures (in this  
30 case, where prudence is not tested), and for mistaken planning assumptions.

1           b)     No, not necessarily. Cost overruns relate to poor budgeting and poor  
2 processes for establishing contingency reserves, which can occur on any type  
3 of project. It is true that projects that mostly relate to off-the-shelf-products may  
4 be subject to less uncertainty and cost risk, but “cost risk” should be  
5 understood to include both cost increases and decreases from budgeted  
6 amounts when proper cost estimating is done. Further, whether a project goes  
7 over budget does not necessarily mean the project will be over budget for  
8 regulatory purposes, as increases in budget normally have to be tested for  
9 prudence first, before they can be included in rates.