

November 23, 2015

The Board of Commissioners of Public Utilities
Prince Charles Building
120 Torbay Road, P.O. Box 21040
St. John's, NL A1A 5B2

Attention: Ms. Cheryl Blundon
Director Corporate Services & Board Secretary

Dear Ms. Blundon:

Re: Newfoundland and Labrador Hydro – 2016 Interim Industrial Rates Application

Following is Hydro's reply to the parties' submissions with regard to the above noted application.

1.0 Application Background

On January 28, 2015 Hydro filed an application with the Board (the 2015 Interim Rates Application) seeking approval of adjustments to its customer rates to provide interim rate relief in advance of conclusion of its General Rate Application (GRA). The 2015 Interim Rates Application also requested approval for rates to be paid by Hydro's Island Industrial Customers (IIC) in compliance with Orders in Council OC2013-089 and OC2013-090, as amended, which provided direction to the Board and to Hydro, respectively, with regard to the phasing-in of rate changes to Hydro's IIC.

In Order No. P.U. 21(2015), the Board approved a 10% increase in IIC base rates (excluding specifically assigned charges) and the implementation of RSP Surplus adjustments that resulted in a 2.7% increase in rates for each individual IIC. A separate RSP Adjustment was maintained for Teck Resources to achieve the equal percentage increase for each customer.

The rate increase required to implement full cost IIC base rates can vary materially depending on the forecast No. 6 fuel cost used to establish rates. Approval of the proposed IIC base rate in the Amended Application (based on a forecast No. 6 fuel cost of \$93.32 per barrel (\$Cdn)) will require a base rate increase of 26.8% relative to the interim base rate approved July 1, 2015. However, there has been a material reduction in No. 6 fuel cost since the filing of the Amended Application. The forecast No. 6 fuel cost for the 2015 Test Year is approximately \$64.41 per barrel (\$Cdn) if it is based on the 2016 fuel price forecast provided

to the Board on October 15, 2015.¹ The use of this more current forecast No. 6 fuel cost in the 2015 Test Year results in an average rate increase for IIC in the range of 13% – 15%.²

Hydro believes it is appropriate for the Board to update the 2015 Test Year No. 6 fuel cost forecast in determination of final customer rates. Hydro believes the 2016 forecast No. 6 fuel cost of \$64.41 per barrel (\$Cdn) is reasonable for use in determining the 2015 Test Year cost of service. If, in the final GRA Board Order, the Board approves the forecast No. 6 fuel cost for 2016 of \$64.41 per barrel (\$Cdn) as the 2015 Test Year fuel cost to be used in establishing final customer rates, Hydro will use this fuel cost in determining the 2015 Test Year revenue requirement and rate design in its compliance filing.

The current schedule for the ongoing GRA indicates an Order of the Board on final customer rates will not be issued in time for the implementation of new IIC rates to become effective January 1, 2016. The required phase-in of IIC rates by September 1, 2016 will require a rate increase on the implementation date of final GRA rates and a further rate increase on conclusion of the phase-out of the RSP Surplus Adjustments on September 1, 2016. A delay in increasing IIC rates beyond January 1, 2016 will also contribute to a 2016 net income deficiency for Hydro. Hydro's application presents proposals to limit the 2016 net income deficiency from IIC while not imposing an additional rate increase at this time.

2.0 The Application

The 2016 Interim Industrial Rates Application proposes another step in the phase-in of Island Industrial Customers (IIC) rates on January 1, 2016 in which the base rates increase but the effective rate results in no increase for each IIC. The 2016 Interim Industrial Rates Application proposes to implement interim base rates, effective January 1, 2016, that reflect a No. 6 fuel cost of \$64.41 per barrel (\$Cdn) in the base energy rate for the 2015 Test Year. The proposed demand charge is consistent with the proposed demand charge in the Amended Application. Because the methodology for determining specifically assigned charges is currently being contested before the Board, Hydro is proposing no change in specifically assigned charges at this time.³

Using this basis for setting each of the components of IIC rates results in a forecast 3.7% increase in base rate revenues (i.e., demand charge, energy charge and specifically assigned charges) based on the 2015 Test Year forecast.⁴

¹ The 2015 Test Year No. 6 fuel cost of \$64.41 per barrel (\$Cdn.) is calculated using the 2016 forecast fuel price including the forecast fuel price impact on the year-end 2015 inventory cost of No. 6 fuel.

² The rate change percentage depends on the methodology used in allocating operating and maintenance costs to specifically assigned charges. See response to NP-NLH-005, Attachment 1.

³ This proposal is consistent with the Board's decision in Order No. P.U. 14(2015).

⁴ The calculation of the 3.7% is provided in Attachment 1 to response to NP-NLH-005.

Hydro also proposes to revise the RSP Surplus Adjustments effective January 1, 2016 to offset any rate increase from implementing new base rates. The proposed RSP Surplus Adjustments of (\$1.52) per kW and (0.294¢) per kWh are to be effective for the period January 1, 2016 to August 31, 2016. The revised RSP Surplus Adjustments are calculated to provide the same net demand and energy charges that are currently approved for IIC billing (i.e., approved effective July 1, 2015 on an interim basis).

Order No. P.U. 21(2015) required Hydro to file revisions to the RSP Rules to clearly provide for the transfer from the IIC RSP Surplus to fund the difference between the approved base rate increase and the effective base rate increase for IIC. Hydro has also included revised RSP rules in this filing to comply with this Board directive.

3.0 Discussion

Board approval of the 2016 Interim Industrial Rates Application will have no financial impact on either Newfoundland Power or its customers. Newfoundland Power has filed no comments on the Application. The Consumer Advocate does not support Hydro's Application to increase base rates to IIC effective January 1, 2016.

Vale submitted that "Hydro should be granted interim rates to reduce the potential for intergenerational inequity created by changes within the Island Industrial Customer Group. Vale also supports (i) the calculation of interim rates by adjusting the forecast cost of No. 6 fuel to \$64.41 per barrel and (ii) the RSP Surplus Adjustments requested by Hydro."⁵

After considering the Application in light of OC2013-089, the IIC Group indicates it accepts that "...it is open to the Board, on this direction language, to not wait until the end of the three-year phase in period, or until final rates are established by a GRA decision and order (and the subsequent Hydro compliance filing process) to start applying the IIC RSP Surplus, on an interim rates basis, to grant interim relief to Hydro with respect to an anticipated revenue shortfall (even if the exact amount of that shortfall is not currently known)".⁶ The IIC Group acceptance is consistent with the approval by the Board of interim IIC rates effective July 1, 2015 and the implementation of RSP Surplus Adjustments to limit customer rate impacts.⁷

The ICC Group goes on to state: "If the Board sees fit to grant Hydro this interim relief, then the IIC Group support Hydro's proposal that the net effective January 1, 2016 rate increase to the Industrial Customers should be 0%, by virtue of Hydro's proposal to not seek any SAC

⁵ Source: Page 2, lines 12 – 16 of Vale's written submission dated November 19, 2015.

⁶ Source: IIC Group submission dated November 20, 2015, page 1.

⁷ The Board approved current interim IIC rates in Order No. P.U. 21 (2015).

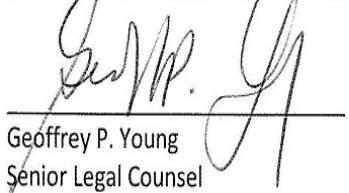
charges in the interim rates. Hydro's proposals in this regard serve the objective of avoiding the inclusion of contentious elements in the interim rates".⁸

In summary, Hydro's Application provides a reasonable balance of the interests of the utility and customers. The Application: 1) makes another progressive step in the phase-in of IIC rates; 2) limits the 2016 net income deficiency from IIC as a result of delaying final IIC rates beyond January 1, 2016; and 3) gives reasonable consideration to customer impacts of the proposed rates while avoiding contentious issues that are currently being considered by the Board.

Should you have any questions, please contact the undersigned.

Yours truly,

NEWFOUNDLAND AND LABRADOR HYDRO



Geoffrey P. Young
Senior Legal Counsel

GPY/bs

cc: Gerard Hayes – Newfoundland Power
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Genevieve M. Dawson – Benson Buffett

⁸ Source: IIC Group submission dated November 20, 2015, page 2.