

1 **Q. [Brad Rolph Evidence, pages 33-43]**

2 **In Mr. Rolph's opinion, would it be reasonable for Hydro to charge a mark-up on**
3 **its common services charged to its affiliates by an arm's length amount, between**
4 **two percent and five percent, as proposed by the OECD?**

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7 **A.** My opinion as it relates to the question is detailed at page 31 starting a line 1 in the report
8 I issued to Board dated June 1, 2015 entitled *Newfoundland and Labrador Hydro, Expert*
9 *Report, Evaluating the Pricing Policy of Affiliate Common Services, Common Expenses*
10 *and Corporate Services.*

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12 *Nalcor and Hydro are provincial crown corporations and are not subject to tax.*
13 *Consequently, relying on the tax implications for guidance on this matter would be*
14 *ineffective. Alternatively, I considered whether the absence [of] a mark-up would*
15 *create an inappropriate subsidy. First, I considered the implications of Nalcor*
16 *marking up the costs of rendering certain corporate services to Hydro. Such a mark-*
17 *up would increase Hydro's revenue requirements and the rates that it charges its*
18 *customers. Accordingly, I believe that applying a mark-up to the costs of rendering*
19 *corporate services to Hydro would be inappropriate.*

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21 *I believe that the same answer applies to situations in which Hydro is providing*
22 *common or corporate services for the benefit of the public energy projects of its*
23 *affiliates. To do otherwise, would create a situation in which Hydro's revenue*
24 *requirement would decline at the expense of Nalcor, one of the public energy*
25 *projects of its other lines of business or the Province. However, not all of Nalcor's*
26 *energy projects are entirely publicly owned; some of its energy projects are partially*
27 *owned by other provincial governments or private interests. In the context of energy*
28 *projects involving private interests, the absence of a mark-up on the costs of*
29 *rendering common services or corporate services for the direct benefit of these*
30 *private energy projects would lower the amounts charged for such services and*
31 *increase the profits generated by these projects to the benefit of private interests.*
32 *This outcome would create an inappropriate subsidy at the expense of Hydro and its*
33 *customers. Accordingly, I believe that should Hydro render services to Nalcor or one*
34 *of its other lines of business for the benefit of an energy project involving private*
35 *interests, the costs of rendering such services should be marked-up by an arm's*
36 *length amount, between two percent and five percent as proposed by the OECD.*

37
38 *Whether or not Hydro or its affiliates apply a mark-up to the costs incurred*
39 *rendering intercompany services should be considered from the perspective of*
40 *materiality and practicality. [Analysis contained in Section 5 of my report dated June*
41 *1, 2015, demonstrated that] marking-up the costs to be recovered by Hydro from its*
42 *affiliates, or vice versa, for rendering common or corporate services would not be*
43 *material. Accordingly, the efforts to determine the magnitude of, and administer and*
44 *monitor any such mark-up beyond simply relying on the mark-up proposed by the*
45 *OECD might not be practical.*