Q. **[Brad Rolph Evidence, page 28]**

In considering the appropriateness of a mark-up on inter-affiliate transactions, Mr. Rolph states:

"I considered whether the absence on a mark-up would create an inappropriate subsidy. First, I considered the implications of Nalcor marking up the costs of rendering certain corporate services to Hydro. Such a mark-up would increase Hydro's revenue requirements and the rates that it charges its customers. Accordingly, I believe that applying a mark-up to the costs of rendering corporate services to Hydro would be inappropriate.

I believe that the same answer applies to situations in which Hydro is providing common or corporate services for the benefit of the public energy projects of its affiliates. To do otherwise, would create a situation in which Hydro's revenue requirement would decline at the expense of Nalcor, one of the public energy projects of its other lines of business or the Province."

Please provide any examples of which Mr. Rolph is aware where a regulator has determined that no mark-up was required because the nonregulated affiliate to which services were provided was publicly owned.

A. I am unaware of any examples where a regulator has determined that no mark-up was required because the non-regulated affiliate to which services were provided was publicly owned.

Q. Is it Mr. Rolph's opinion that differences between Newfoundland Power's inter-affiliate transactions and Hydro's inter-affiliate transactions justify that the two utilities follow different inter-affiliate pricing policies?

A. I was not engaged to evaluate Newfoundland Power's inter-affiliate transactions. In general, if there are differences in the services rendered, the terms and conditions under which those services were rendered, the magnitude of the transactions or data available to determine prices, differences in inter-affiliate pricing policies would be justified.

Q. In Mr. Rolph's opinion, in the calculation of an allocator based on, for example, FTEs, how should Hydro employees who perform common services be accounted for in the allocation calculation? Should they be (i) accounted for as full Hydro FTEs, (ii) removed from the allocation calculation, or (iii) accounted for by some other method?

A. It is my opinion that in the calculation of an allocator, in this example, FTEs, Hydro employees who perform common services should be accounted for as FTEs. To demonstrate my rationale, consider Hydro's Human Resources department. The FTEs in that department also benefit from the services rendered by that department. To exclude those FTEs from the calculation would exclude a group of FTEs that benefit from the services rendered and inappropriately increase the amount of the costs recovered by Hydro from Nalcor and its other lines of business.

Q. In Order No. P.U. 6 (1991), the Board ordered:

"NP shall put in place a quarterly reporting mechanism whereby NP aggregates all inter-corporate transactions by the accepted code of accounts, segregating purchases of goods and services from sales of goods and services. This report will be submitted to the Board together with any contracts and agreements signed during the quarter with any related parties. Transactions exceeding $50,000 individually or per annum must be reported separately and compared to the cost of the same transaction from an arms-length supplier(s). A description of the nature and the amount of the transaction(s) as well as any amount due to or from the related party must be provided."

Does Mr. Rolph believe it is appropriate that the Board impose similar inter-affiliate transaction reporting requirements on Hydro?

A. As described in the Materiality section of the Expert Report, a $3 million dollar adjustment to the costs recovered or paid by Hydro would be required to change the effective rate by $0.001. Consequently, the potential understatements of amounts charged by Hydro for rendering common services to affiliates would not be material. Accordingly, it would cause additional work if the Board imposed a quarterly reporting requirement and a review of transactions exceeding $50,000; this work might be considered unnecessary given the lack of materiality of the potential understatements. Alternatively, I would recommend an annual review of inter-affiliate transactions that describes all services rendered and costs charged back to and from affiliates, the amounts involved, and the methods used for determining those amounts. Should this recommendation be adopted, there would be no need to specify a dollar threshold for reviewing individual transactions due to materiality considerations.

Q. [Grant Thornton Financial Consultant's Report, April 25, 2014 ("Grant Thornton Report"). Page 18]

Relative to the 2013 test year, Grant Thornton states:

"the difference in rate of return on book equity of 9.59% and Hydro regulated return on equity of 8.80% arises due to differences between the Company's average rate base and average invested capital balances."

Does Grant Thornton believe that the difference between Hydro's rate of return on book equity and its regulated return on equity is a relevant consideration in determining whether the rates proposed in this Application provide Hydro with an opportunity in earn a just and reasonable return in accordance with the requirements of the Order in Council and the *Electrical Power Control Act, 1994*?

A. Grant Thornton does believe the difference between Hydro's rate of return on book equity and its regulated return on equity is a relevant consideration in determining whether the rates proposed in this Application provide Hydro with an opportunity to earn a just and reasonable return in accordance with the requirements of the Order in Council and the *Electrical Control Act 1994*. This provides the Board with information to assist in understanding how the rates impact the financial statements of Hydro for consideration in their assessment of the proposed rates.

Q. What studies and methodologies used by Hydro to calculate the 2013 test year working capital and materials and supplies allowances did Grant Thornton review to assess the reasonableness of the allowances?

A. In our review of the average rate base, and specifically working capital and materials and supplies, for the 2013 test year, we relied on information provided by Hydro in its responses to CA-NLH-126, CA-NLH-127, CA-NLH-128, and CA-NLH-188, and we compared this information to the 2012 actuals included in Hydro's 2012 Annual Returns to assess its reasonableness. We did not review any studies or methodologies other than those referred to in the above noted RFI responses.

Q. **[Grant Thornton Report, page 32, lines 16 to 25]**

Page 76 of Order No.P.U.19 (2003) states:

"In the Board's view the range of rate of return on rate base can act as an incentive device to encourage NP to seek efficiencies between rate hearings, which can then be passed on the customers. This is evidenced in the operational efficiencies and cost savings that have been implemented by NP since the last rate hearing in 1998".

In Grant Thornton's opinion, is evidence of operational efficiencies and cost savings required to justify increasing Hydro's range of return on rate base for incentive purposes?

A. The use of a range of return is accepted conceptually as an incentive mechanism to control and reduce costs in a regulatory environment. While evidence of past operational efficiencies and cost savings would demonstrate the historical effectiveness of the incentive mechanism we do not believe it is a requirement for the consideration of an incentive mechanism (including increasing the allowed range of return) on a go forward basis. The Board would need to take all factors, including past effectiveness, into consideration in its decision.

Q. [Grant Thornton Report, page 99, lines 8 - 9]

Based on Grant Thornton's review, forecast 2013 capital expenditures included in the rate base for 2013 test year are overstated. Does Grant Thornton agree that this also results in an overstatement of interest capitalized during construction expense included in the 2013 test year revenue requirement?

A. According to Table 30 (page 60) in our report, the amount of interest capitalized during construction for forecast 2013 is approximately $1,000,000 greater than the actual 2013 interest capitalized during construction. Therefore we agree that as a result of forecast 2013 capital expenditures included in the 2013 test year, being overstated, it appears that it has resulted in an overstatement of interest capitalized during construction in the 2013 forecast.

However, we do not have the information to determine the impact that uncompleted projects would have on the gross interest expense, and which of the uncompleted projects included capitalized interest therefore we are not able to determine the impact the net interest expense would have on the 2013 test year revenue requirement.

Q. **[Grant Thornton Report, page 108]**

Section 3.2.8 WBS Task 800 – Construction, page 3.9 of the *Holyrood Thermal Generating Station Decommissioning Study states*:

"Some construction will be required during demolition as a considerable portion of the existing powerhouse structure will be retained for future operations. Construction will include structural modifications and installation of cladding at the powerhouse and the pumphouse #1, as well relocation of electrical and mechanical systems and sub-surface water and sanitary connections."

In Table 4.2.1 of the *Holyrood Thermal Generating Station Decommissioning Study*, these construction costs are indicated to total $3.4 million. The calculation of the asset retirement obligation associated with the decommissioning of the Holyrood Thermal Generating Station, as provided in the response to Request for Information NP-NLH-091, includes these construction costs.

Does Grant Thornton believe that including construction costs as part of an asset retirement obligation is appropriate?

A. Our Report (page 108, line 16) notes that Hydro has used CPA Handbook Section 3110, *Asset Retirement Obligations*, as its basis for calculating its asset retirement obligation ("ARO") with respect to the decommissioning of the Holyrood Thermal Generating Station ("HTGS"). That section of the CPA Handbook applies to *"...legal obligations associated with the retirement of a tangible long-lived asset that result from its acquisition, construction, development or normal operations."* The recognition of the liability will therefore be governed by the specific decommissioning requirements established by the applicable regulatory authorities.

The Holyrood Thermal Generating Station Decommissioning Study included in the Evidence refers to *"Regulatory Requirements of Decommissioning"* in Section 2.3. It cites a number of guiding documents, legislative provisions and regulations that are expected to establish the legal obligations associated with decommissioning the HTGS.

Limited guidance is provided under CPA 3110 regarding costs to be included in the estimate of asset retirement obligations. With respect to measurement, CPA 3110 states "*The amount recognized as an asset retirement obligation shall be the best estimate of the expenditure required to settle the present obligation at the balance sheet date*." Whether construction costs should be included in the costs would be determined by the specifics of the "*...law, statute, ordinance or written or oral contract or by legal construction of a contract under the doctrine of promissory estoppel*" which define the obligation.

The example provided in this section which most closely aligns with the HTGS decommissioning is provided in Paragraph A16 of CPA 3110:

> *"An asset retirement obligation may exist for component parts of a larger system. In some circumstances, the retirement of the component parts may be required before the retirement of the larger system to which the component parts belong. For example, consider an aluminum smelter that owns and operates several kilns lined with a special type of brick. The kilns have a long useful life, but the bricks wear out after approximately five years of use and are replaced on a periodic basis to maintain optimal efficiency of the kilns. Because the bricks become contaminated with hazardous chemicals while in the kiln, a law requires that when the bricks are removed, they must be disposed of at a special hazardous waste site. The obligation to dispose of those bricks is within the scope of this Section. The cost of the replacement bricks and their installation are not part of that obligation"*

Applying the guidance, by analogy, to the decommissioning of the HTGS would imply that only the decommissioning costs are part of the obligation and subsequent construction costs would be excluded.

We do note that in Section 3.3.1 of the Holyrood Thermal *Generating Station Decommissioning Study* it states "*selectively demolishing and removing only the boilerhouse will result in additional demolition costs due to the care and attention required to remove only certain parts of the building and equipment without damaging the sections that are to remain occupied and operational*". As a result we are not able to determine the total impact on estimated project costs if construction costs were not included.

The construction costs will result in an asset being acquired. The question, whose answer must be determined by the legal requirements surrounding the decommissioning, is whether these costs will be recognized at that time in the future the expenditure is made, or if an obligation currently exists which would result in the current recognition of an asset.

Q. **[Pre-filed Evidence of J.W. Wilson & Associates, Inc., April 25, 2014 ("J.W. Wilson Evidence"), page 1]**

Dr. Wilson states that:

"It is our conclusion that the cost allocation steps in Hydro's filing have been carried out in general conformance with Hydro's prior filings and with the cost allocation procedures previously approved by the Board."

Has Dr. Wilson reviewed whether Hydro has normalized loads, expenses, revenues, and other components of the test year in accordance with generally accepted practice, or is his statement concerned only with classification and allocation of costs?

A. This statement concerns only the cost allocation steps in Hydro's filing. Dr. Wilson did not examine or evaluate Hydro's practices with respect to normalization of loads, expenses, revenues or other test year components. He did determine that Hydro made regular adjustments for variations in the RSP components, which tends to align revenues and costs over time and minimize the significance of normalization adjustments.

Q. **[J.W. Wilson Evidence, page 3]**

Dr. Wilson observes that Hydro's proposal to set Newfoundland Power's second block rate at 10.4 cents per kWh would weaken the energy price signal in Newfoundland Power's rate. Dr. Wilson suggests the adoption of a two-block energy seasonal differential would permit the retention of a marginal cost energy price signal in Newfoundland Power's two block energy rate.

Would Dr. Wilson agree that maintaining the Newfoundland Power demand rate at its current level instead of setting it at the full embedded cost would also assist in retaining a marginal cost price signal in Newfoundland Power's second block, even if seasonal rates were not adopted?

A. Yes.

Q. **[J.W. Wilson Evidence, page 24]**

Dr. Wilson states:

"…there is little evidence that marginal cost capacity rates have as significant an impact on efficient capacity demand as marginal energy rates do on efficient energy demand."

Given this observation, is it Dr. Wilson's opinion that Hydro's focus on Newfoundland Power's demand price signal is misplaced at this time?

A. Yes. However, this is a matter of relative importance. Dr. Wilson stated that "*while a case can be made for a demand rate that reflects the incremental cost of capacity expansion, especially at the present time when Hydro must deal with increased capacity costs as a result of growing demand, there is little evidence that marginal cost capacity rates have as significant an impact on efficient capacity demand as marginal energy rates do on efficient energy demand.*" (Report at 24.)

Q. **[J.W. Wilson Evidence, pages 21, 22 and 29]**

On page 29, Dr. Wilson states:

"… if the load variation costs are to be covered by the RSP we agree that Hydro's proposed allocation of these costs based on customer energy ratios is an equitable allocation method."

On page 21, Dr. Wilson describes the distorting effect that the difference between the Industrial Customer and Newfoundland Power tail block energy rates has on load variation adjustments to the RSP.

If the combination of the proposed allocation of the portion of load variation costs covered by the RSP and the portion of load variation costs covered by tail block energy rates were to result in Newfoundland Power paying the incremental cost of its load variation and also paying a majority of the incremental costs of the Industrial Customer class load variation, would Dr. Wilson agree that such result is inequitable?

A. Yes.