

1 Q. Does Hydro intend to file a 2014 test year when it files an amended 2013 General
2 Rate Application in the fall of 2014? If no, explain in detail why not.

3
4
5 A. Yes, Hydro intends to file 2014 test year evidence, for the purpose of a
6 determination by the Board of a 2014 revenue requirement. Hydro proposes that,
7 upon the Board's determination of a 2014 revenue requirement, any resultant net
8 income deficiency will be deferred and recovered in future rates. Thus, the 2014
9 test year filing will not be made for the purpose of designing 2014 rates and a 2014
10 Cost of Service study will not be required. For 2015, Hydro will complete both a
11 Test Year and a Cost of Service study, as it will be proposing that rates be designed
12 on the basis of a 2015 Test Year.

13
14 In this context, Hydro's use of the term "test year" is meant to be that as defined in
15 the National Association of Regulatory Utility Commissioners (NARUC) Rate Case
16 and Audit Manual¹, page 10, as follows:

17
18 **Determining the Appropriateness of the Test Year**

19 *The test year is a period of measurement for a recent, consecutive twelve-*
20 *month period consisting of a full year of operations where data is readily*
21 *available. While many jurisdictions have traditionally used, and continue to*
22 *use, historical test year data, some commissions either allow or mandate*
23 *the use of a projected or future test year. In either case, the test year is*
24 *used to examine earned returns compared to either previously authorized*
25 *earnings levels (based on approved rates of return) or compared to*
26 *requested earnings levels (based on requested or recommended rates of*

¹ Filed in response to GRA RFI NLH-NP-005.

return). Whether using a future or historic test year, the auditor should judge the appropriateness of the test year that has been proposed. Is it representative, after adjustments, of the period in which rates take effect?

When looking at an historic test year, one of the first questions asked is whether the test year is too stale to make it a reasonable basis upon which to establish rates for a future period. In looking at the appropriateness of the test year (and whether it might be too old), one should look at what has happened since the end of the test year and the current time. Are the historic costs and revenues normal or recurring? Has extraordinary growth occurred during the intervening time (e.g., has a new industrial customer come on line)? Or, has there been a negative impact on revenues through shift reductions at the local foundry? In looking at the months beyond the end of the test year, have the growth rates for rate base, expenses, and revenues all remained fairly close and constant, maintaining the test year relationship among these three elements, or has one element changed dramatically, making the test year out of kilter with current operations? If so, can this situation be resolved through adjustments to the test year?

When looking at a future test year, one will want to examine the test year selected for reasonableness. Is this period mandated by rules, statute, or Commission directive? Is the test year founded on a historical base or documented figures, such that its projections are readily understandable and traceable?

Please note that the above NARUC definition of "Test Year" does not necessarily require a Cost of Service study. The purpose of a Test Year is to determine revenue requirement. The purpose of a Cost of Service study is to

1 fairly allocate costs (and as a result, facilitate rate design). Hydro requires that
2 its costs be tested for 2014, but as it is not designing rates for 2014, a 2014 Cost
3 of Service study is therefore not required. For 2015, Hydro will complete both
4 a Test Year and a Cost of Service study as it is proposing rates, based on its
5 2015 Test Year.
6