Q. 2013-2014 General Rate Application, Amortization of Deferrals

In Section 3.5.1 of the Application NP outlines its proposition to amortize over the three-year period: (i) cost recovery deferrals approved in 2010 for 2011, $2,400,000, in 2011 for 2012, $2,400,000, and in 2012 for 2012, $2,500,000; (ii) third party hearing costs associated with this Application, $1,250,000; (iii) the year end 2011 balance in the Weather Normalization Reserve, ($7,005,0000); and (iv) a 2013 revenue shortfall resulting from a forecast March 1, 2013 implementation of revised customer rates, netting to $0 over the three-year period. The period of amortization is 2013, 2014 and 2015, and the total amount to be recovered is $1,545,000.

If NP decides that its next general rate application will be filed with a 2017 test year, what options does NP believe are available to deal with the over collection that would result from the end of the three-year amortization period at year end 2015 and the continuation of rates, initially intended to include the recovery of the deferral, for an additional year?

A. **A. A Possible 2017 Test Year**

Newfoundland Power's current 5-year financial forecast indicates revenue shortfalls of approximately $4.4 million and $7.6 million in 2015 and 2016, respectively.[1] In order for Newfoundland Power to avoid a general rate application until a 2017 test year, the Company will need to experience changes from currently forecast sales and costs which overcome the 2015 and 2016 forecast revenue shortfalls.[2] Newfoundland Power does not currently consider this to be likely.

In addressing a forecast revenue shortfall, a number of matters require consideration. The forecast 2016 forecast revenue shortfall of approximately $7.6 million reflects the net impact of the concluding amortizations in 2015. The Board should not consider the impact of the concluding amortizations without giving due consideration to both the overall cost of providing service and whether the Company will have a reasonable opportunity to achieve its return in 2015 and 2016.

B. The Company's Perspective on Cost Recovery

Cost variability from test year does not result in "over-collection" or "under-collection" of costs. For example, if labour costs in 2016 are higher than the 2014 test year forecast and interest costs in 2016 are less than the 2014 test year forecast but overall actual costs equal overall test year costs, the Company cannot reasonably be considered to have "under-collected" its 2016 labour costs "over-collected" its 2016 interest costs.

[1] See the 5-year financial forecast which is Attachment A to response to Request for Information CA-NP-398.

[2] A *revenue shortfall* is simply the change in the forecast financial results (expressed in terms of revenue) that would be required for the Company to recover all its forecast costs, including its forecast cost of equity.

In the Company's view, the Board's approval of the test year provides the Company with the *opportunity* to recover its overall costs; test year allowances do not equate to actual cost recovery of each individual component of those overall costs. When an amortization period for a cost recovery in (or credit to) customer rates expires, Newfoundland Power does not "over-collect" or "under-collect" the amount being amortized.

From the Company's perspective, the reasonableness of customer rates in relation to Newfoundland Power's overall cost of service in 2016 should be the primary focus of the Board in considering the impact of expiring amortizations in 2016.

C. Regulatory Options

If the Board believed that there was a *reasonable possibility* that Newfoundland Power's customer rates could become unreasonable in 2016 due to the effect of expiring amortizations (or any other reason, including the Company's cost of capital), the Board has options.

Firstly, the Board could order the Company to file its next rate case with a 2016 test year. This would ensure the Company's revenues and costs are rebalanced for 2016 and eliminate the possibility of rates becoming unreasonable in 2016. If circumstances changed sufficiently to justify a deferral of a rate case to the succeeding year, the matter could be considered at that time.[3]

Secondly, the Board could order the Company to defer the amount of the expiring amortizations commencing in 2016, until further order of the Board.[4] The Board could also, if it saw fit, order that any balance so deferred be made part of the Company's annual Rate Stabilization Account adjustment.

Please refer to responses to Request for Information PUB-NP-110, PUB-NP-115 and CA-NP-396.

[3] See the response to Request for Information PUB-NP-115, lines 34 to 37 and footnote 3 for what an application to consider such a deferral would be, at a minimum, required to show.

[4] The past practice of the Board in considering such matters between test years is to consider the impact of the expiring amortizations on Newfoundland Power's ability to have a reasonable opportunity to achieve its allowed return. (See the response to Request for Information CA-NP-396).