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Board of Commissioners of Public Utilities
120 Torbay Road
Prince Charles Building
St. John's, NL
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Attention: Ms. Doreen Dray

September 20, 2013

Dear Ms. Dray,

**Re: Newfoundland and Labrador Hydro
2012 Average Rate Base and 2012 Average Deferred Charges**

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We have completed our review of Newfoundland and Labrador Hydro's ("the Company's") 2014 Capital Budget Application (Section K) as it pertains to the calculation of the 2012 average rate base and 2012 average deferred charges.

The results of our review are noted below:

2012 Average Rate Base Calculation and 2012 Average Deferred Charges

The average rate base for 2012 and 2011 as calculated by the Company and provided in Section K, Page K-1 of its 2014 Capital Budget Application is \$1,526,051,000 and \$1,493,218,000 respectively. The average deferred charges for 2012 and 2011 provided in Section K, Page K-1 are \$65,670,000 and \$68,047,000, respectively.

Our procedures with respect to verifying the calculation of the 2012 average rate base and 2012 average deferred charges were directed towards the verification of the data incorporated in the calculations and the methodology used by the Company. Specifically, the procedures which we performed included the following:

- agreed all carry-forward data to supporting documentation including audited financial statements and internal accounting records and reports, where applicable;
- agreed component data (capital expenditures, depreciation, etc.) to supporting documentation;
- checked the clerical accuracy of the continuity of the rate base and deferred charges for 2012; and

- reviewed the methodology used in the calculation of the average rate base with reference to the Public Utilities Act, the Hydro Corporation Act and Board Orders.

Based upon the results of the above procedures we note the following:

2012 Rate Base

- In P.U. 5 (2012) the Board approved the capital expenditures relating to the project 'To Replace the Fuel Oil Heat Tracing system at the Holyrood Thermal Generating Station'. The Board has ordered that recovery of this project's associated costs will not be allowed at this time. The Order required Hydro to separate and record these costs in an account, the disposition of which will be considered by the Board should Hydro make subsequent application for recovery of some or all of the associated costs. In accordance with this Order, Hydro has excluded capital cost additions of \$783,000 from its rate base calculation in relation to Holyrood fuel oil heat tracing costs.
- In 2012 the Company recorded an asset retirement obligation of \$22,878,000 which is associated with the Holyrood Thermal Generating Station - \$20,772,000 and the disposal of Polychlorinated Biphenyls - \$2,106,000. The Company has also recorded accumulated amortization of \$3,193,000 associated with the asset retirement obligations. The Company has included this obligation in the cost of property, plant and equipment but has excluded the amount from rate base. In P.U. 29 (2012) the Board ordered that Hydro shall appropriately recognize and record asset retirement obligations in accordance with International Financial Reporting Standards and stated that regulatory treatment of the particular asset retirement obligations included in the application will be appropriately considered in the context of a general rate application.
- In P.U. 24 (2012) the Board approved capital expenditures for the upgrade of the Cat Arm access road. This project was completed in 2012 with capital expenditures of \$234,000 and the expenditures were included in rate base. The Order required Hydro to provide a status report on the application for a Crown Easement no later than its filing of the 2012 Capital Expenditure Report and also ordered that Hydro shall not include the expenditures in its rate base until the Board has confirmed in writing that to do so would be consistent with generally accepted sound public utility practice. In February 2013 and September 2013 Hydro provided a status report on the Crown Easement application stating that Hydro was still awaiting its easement. Currently there is no Board approval of the inclusion of the cost in rate base. If this amount had not been included in rate base, average rate base would have decreased by \$117,000.
- In 2012 the Company used \$1,374,000 of the 'Allowance for Unforeseen Items' account to cover the cost of capital expenditures relating to the Black Tickle Diesel Fire Restoration Project. On March 14, 2012, the community of Black Tickle experienced a power outage as a result of a fire at the diesel plant. In September of 2012, Hydro filed a report to the Board regarding the use of the 'Allowance for Unforeseen Items' account for the Black Tickle Diesel Fire Restoration Project. Included in this report was a description of the background and purpose of the project,

the nature and scope of the work completed on the project thus far, a timeline setting out all relevant project dates, and an estimation of the total costs to be incurred upon completion of the project in early 2013. On January 3, 2013, the Board wrote a letter to Hydro requesting the Company to file a detailed report in relation to the Black Tickle fire restoration project on or before April 1, 2013. Upon receipt of this report, the Board would advise as to how this matter would proceed. In April 2013, Hydro filed a report to the Board in response to this letter. If this amount had not been included in rate base, average rate base would have decreased by \$687,000. Currently, the Board has not made a final decision on the 2012 average rate base and it remains uncertain if these costs can be included in the 2012 rate base.

2011 Rate Base

- In 2011 the Company included \$2,001,920 in capital assets that were included in the 'Allowance for Unforeseen Events' which the Board disallowed. If this amount had not been included in rate base, average rate base would have decreased by \$1,000,960. Currently, the Board has not made a final decision on the 2011 average rate base and it remains uncertain if these costs can be included in the 2011 and 2012 rate base.

Based upon the results of the above procedures we noted the following discrepancies in the calculation of the 2012 and 2011 average rate base:

2012 Rate Base

- **Included in the 2012 average rate base are 2012 capital asset purchases of \$234,000 relating to the upgrade of the Cat Arm access road which has not been approved by the Board.**
- **Included in the 2012 average rate base are expenditures of \$1,374,000 relating to the Black Tickle Diesel Fire Restoration Project which has not been approved by the Board.**

2011 Rate Base

- **Included in the 2011 and 2012 average rate base are 2011 capital asset purchases of \$2,001,920 which has not been approved by the Board.**

We did not note any discrepancies in the 2012 average deferred charges, and therefore conclude that the average deferred charges of \$65,670,000 included in Section K, Page K-1 of the Company's Application is accurate and in accordance with Board Orders and established regulatory practice.

I trust this is the information you requested. If you have any questions, please contact me.

Yours sincerely,
Grant Thornton LLP



Kim Simms, CA
Principal