

**NEWFOUNDLAND AND LABRADOR
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES**

AN ORDER OF THE BOARD

NO. P.U. 23(2015)

1 **IN THE MATTER OF** the Electrical Power
2 Control Act, 1994, SNL 1994, Chapter E-5.1 (the
3 “EPCA”) and the Public Utilities Act, RSNL 1990,
4 Chapter P-47 (the “Act”), as amended, and regulations
5 thereunder; and
6

7 **IN THE MATTER OF** an application by Newfoundland
8 Power Inc. for approval to delay the filing of its next
9 general rate application and for deferred cost recovery
10 of \$3,991,000 for 2016.
11

12
13 **The Application**
14

15 On April 15, 2015 Newfoundland Power Inc. (“Newfoundland Power”) filed an application with
16 the Board seeking approval to file its next general rate application by June 1, 2016 with a 2017
17 test year, and to set up a deferred cost recovery for 2016 of approximately \$4.0 million (the
18 “Application”). The Application states:
19

20 *Newfoundland Power requests, pursuant to Sections 67 and 80 of the Act, that the Board*
21 *make an Order:*
22

- 23 (i) *approving a 2016 forecast average rate base for Newfoundland Power of*
24 *\$1,054,192,000;*
25 (ii) *approving a just and reasonable 2016 rate of return on rate base for*
26 *Newfoundland Power of 7.38% in a range of 7.20% to 7.56%;*
27 (iii) *approving deferred cost recovery of \$3,991,000 for 2016;*
28 (iv) *directing Newfoundland Power to file its next general rate application by June 1,*
29 *2016 with a 2017 test year; and*
30 (v) *continuing Newfoundland Power’s existing rates, tolls and charges until modified*
31 *by further order of the Board.*
32

33 A copy of the Application was provided to Newfoundland and Labrador Hydro (“Hydro”) and
34 the Consumer Advocate, Mr. Thomas Johnson.
35

36 Requests for information were filed by the Board, Hydro and the Consumer Advocate and were
37 answered by Newfoundland Power on May 8, 2015. Hydro filed further requests for information
38 which were answered by Newfoundland Power on May 25, 2015.

1 On June 2, 2015 Hydro and the Consumer Advocate filed submissions. On June 8, 2015
2 Newfoundland Power filed a reply submission.

3 4 **Background**

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6 In Order No. P.U. 13(2013) the Board ordered, among other things, that, unless otherwise
7 directed by the Board, Newfoundland Power shall file its next general rate application with a
8 2016 test year on or before June 1, 2015.

9
10 Following the filing of this Application, in Order No. P.U. 15(2015) the Board deferred the filing
11 date for Newfoundland Power's next general rate application from June 1, 2015 to October 16,
12 2015 but did not change the requirement for a 2016 test year.

13 14 **Application Proposals**

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16 The Application requests approval to change the date that Newfoundland Power is required to
17 file its next general rate application from June 1, 2015 to June 1, 2016 and to base the application
18 on a 2017 test year rather than a 2016 test year. The Application also requests approval of a 2016
19 cost recovery deferral of \$3,991,000¹. The Application states:

20
21 *Newfoundland Power's current forecast 2016 return on rate base is 0.32% below the*
22 *forecast 2016 pro forma return on rate base. In addition, Newfoundland Power's current*
23 *forecast 2016 return on common equity of 8.08% is 0.72% below the cost of equity of 8.80%*
24 *approved by the Board in Order No. P.U. 13 (2013).*

25
26 *This analysis indicates that current customer rates will not provide Newfoundland Power the*
27 *opportunity to earn a just and reasonable return on its forecast 2016 rate base within the*
28 *meaning of Section 80 of the Public Utilities Act. This is substantially the result of forecast*
29 *increases in Newfoundland Power's rate base resulting from 2016 capital expenditures*
30 *required to provide service to customers.*²

31
32 Newfoundland Power states that approval of the proposed 2016 cost recovery deferral will assist
33 in the orderly establishment of rates charged to customers served by the Island Interconnected
34 system by facilitating the conclusion of Hydro's current general rate application which will
35 establish Newfoundland Power's wholesale cost of supply. The Application states that if it is
36 required to file a general rate application by June 1, 2015:

- 37
38 (i) *Newfoundland Power's cost of wholesale electricity supply would be uncertain and*
39 *subject to change from that outlined in the application;*
40 (ii) *the application would likely not be concluded until sometime in 2016; and*
41 (iii) *the costs associated with conduct of the application would be increased from what*
42 *they would otherwise be.*

¹ The proposed 2016 cost recovery deferral is comprised of an increase in the 2016 return on rate base of \$2,534,000 plus an allowance of \$1,457,000 for income tax effects.

² If the proposed cost recovery deferral is approved, Newfoundland Power's forecast 2016 return on rate base would be 7.32% and its forecast return on common equity would be 8.66%, which Newfoundland Power submits are within the historical ranges used by the Board to assess the reasonableness of returns.

1 The Application states that the Board should grant the Order requested because it permits the
 2 orderly establishment of rates, it is consistent with regulatory principle and practice and it is
 3 consistent with regulatory efficiency.
 4

5 **Submissions**

6
 7 Hydro submits that Newfoundland Power's request for final approval of an increased revenue
 8 requirement for 2016 based on untested costs is unreasonable. Hydro argues that, given the
 9 uncertainty in Newfoundland Power's 2016 forecast, the deferred cost recovery should be
 10 approved for deferral on an interim basis with recovery subject to a further order of the Board
 11 following testing of costs through a general rate application. Hydro argues that there is
 12 substantial uncertainty relating to Newfoundland Power's 2016 forecast. Hydro notes uncertainty
 13 around Newfoundland Power's forecast revenue growth, power purchase expense, cost of capital
 14 and depreciation expense. Hydro states that, in aggregate, the uncertainties could total \$9.0
 15 million. Hydro submits Newfoundland Power's 2016 forecast return on equity contains a great
 16 deal of uncertainty as to how much of the \$4.0 million will be needed to achieve the approved
 17 rate of return in 2016. Hydro states:

18
 19 *Since 2010, NP's actual return on equity has exceeded the 8.80% allowed in Order No. P.U.*
 20 *13(2013). In fact, in all but one of the past five years, NP's actual return on equity has*
 21 *exceeded 9.00%, with an average actual return on equity of 9.10% over this same period.*
 22 *Hydro submits that this history of earnings exceeding the approved return on equity for*
 23 *establishing customer rates combined with \$9.0 million of forecast uncertainty requires*
 24 *further review by the Board of 2016 costs prior to finalization of customer rates for 2016.³*
 25

26 In relation to the Board's jurisdiction to approve a deferral on an interim basis, Hydro submits
 27 that the Board has a broad discretion in dealing with deferral accounts.
 28

29 The Consumer Advocate submits that the Application should be denied. He argues that the
 30 Application rests on the untested assumption that the rate of return on common equity of 8.8%
 31 that was approved for 2013, 2014 and 2015 remains appropriate for 2016. The Consumer
 32 Advocate states that this equity return has not been approved for 2016 and Newfoundland Power
 33 has not filed evidence to support a rate of return on common equity of 8.8% for 2016. The
 34 Consumer Advocate states:

35
 36 *In the absence of a finding of fact that 8.80% is a just and reasonable rate of return for 2016*
 37 *the cornerstone of the Company's request is missing. Without this cornerstone, there is no*
 38 *support for the untested assertion that Newfoundland Power does not have a reasonable*
 39 *opportunity to earn a just and reasonable return in 2016.⁴*
 40

41 The Consumer Advocate states that the Board was very clear that the equity return of 8.8% was
 42 to be used for the 2013, 2014 and 2015 test years but would have to be reviewed for 2016. The
 43 Consumer Advocate states:

³ Hydro Submission, June 2, 2015, page 5.

⁴ Consumer Advocate Submission, June 2, 2015, page 3.

1 *The Board clearly anticipated that a review of the rate of return on common equity would be*
 2 *required for the 2016 test year. That review has not taken place and therefore it cannot be*
 3 *assumed on the basis of a cursory review of the reasonableness of that rate that having a*
 4 *forecast return below 8.80% will not "provide Newfoundland Power" the opportunity to*
 5 *earn a just and reasonable return on rate base that is consistent with the fair return*
 6 *principle and the provision of least cost reliable power" in the 2016 year.*⁵
 7

8 The Consumer Advocate states that Newfoundland Power's evidence is deficient in that it does
 9 not seek an order to establish the equity return for 2016 at 8.8% and does not include expert
 10 evidence on the appropriate equity return for 2016. According to the Consumer Advocate it
 11 would be unprecedented for the Board to approve a return on equity without a full review of
 12 evidence supporting the proposed return or an explicit agreement of the parties. The Consumer
 13 Advocate submits that the response to PUB-NP-004 can be interpreted to be consistent with the
 14 view that returns on equity have generally been declining since 2013 and argues that the allowed
 15 return on equity would be reduced significantly if it were subjected to normal testing.
 16

17 The Consumer Advocate states that any adjustment to revenue or cost items could well reduce or
 18 eliminate the shortfall in revenue forecast by Newfoundland Power. The Consumer Advocate
 19 states:
 20

21 *Hence, whatever equity return is approved by the Board for 2016, it cannot be concluded*
 22 *that Newfoundland Power's forecast earnings if subjected to the discipline of a general rate*
 23 *application would fall fellow(sic) the bottom end of the equity return range.*⁶
 24

25 The Consumer Advocate submits that the evidence is insufficient to make a determination that
 26 Newfoundland Power does not have a reasonable opportunity to earn a just and reasonable return
 27 on equity for 2016.
 28

29 In its reply submission Newfoundland Power argues that the relief sought in the Application is
 30 justified by the current regulatory calendar before the Board, particularly Hydro's ongoing
 31 general rate application process, stating:
 32

33 *The circumstances giving rise to the Application effectively require the Board to establish*
 34 *hearing priorities within a time constrained regulatory calendar. In determining those*
 35 *priorities, the Board is obliged to consider, and balance, the interests of the utilities and the*
 36 *utilities' customers. Approval of the relief requested in the Application will ensure that*
 37 *Newfoundland Power has the opportunity to earn a fair and reasonable return in 2016 while*
 38 *ensuring the orderly establishment of reasonable rates for consumers.*⁷
 39

40 Newfoundland Power submits that, if its general rate application proceeds concurrently with
 41 Hydro's, the length and cost of both proceedings can be expected to increase.
 42

43 Newfoundland Power submits that the only additional cost that is proposed to be recovered from
 44 customers in 2016 is the cost to finance the increased 2016 rate base resulting from 2016 capital

⁵ Consumer Advocate Submission, June 2, 2015, page 6.

⁶ Consumer Advocate Submission, June 2, 2015, pages 8-9.

⁷ Newfoundland Power Reply Submission, June 8, 2015, pages 1-2.

1 expenditures required to provide service to customers. Newfoundland Power argues that the
2 amount of the proposed deferral was determined in accordance with regulatory practice and the
3 evidence filed is consistent in quality and detail with that routinely relied on by the Board for
4 regulatory decision making. Newfoundland Power explains that rates will continue to reflect the
5 tested values approved by the Board in Newfoundland Power's last general rate application.
6

7 Newfoundland Power further states that the array of circumstances in which the Board has
8 approved deferred cost recovery indicates the versatility of this form of regulatory relief and that
9 approval of the 2016 deferred cost recovery would be consistent with the Board's determinations
10 on similar Newfoundland Power applications.
11

12 In relation to the Consumer Advocate's submission regarding recent approved rates of return in
13 other jurisdictions, Newfoundland Power notes that on May 26, 2015 the Regie de l'energie
14 Quebec maintained a return on equity of 8.9% for Gaz Metro for 2016 and 2017.
15

16 In relation to Hydro's submission that Newfoundland Power's application for deferred cost
17 recovery should be approved on an interim basis, Newfoundland Power states it filed its
18 Application with sufficient time to allow adequate opportunity for review of the proposal and the
19 evidence filed.
20

21 Newfoundland Power submits that the Board's approval of the Application would be consistent
22 with the application of regulatory principles including prospective ratemaking, intergenerational
23 equity, minimization of regulatory lag, the timely recovery of costs and regulatory efficiency.
24 Newfoundland Power states that neither the Consumer Advocate nor Hydro appear to dispute the
25 extraordinary nature of Hydro's general rate application or the foreseeable consequences which
26 would result from Newfoundland Power filing its general rate application in October, 2015.
27

28 **Board Findings**

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30 Newfoundland Power seeks to delay the filing of its next general rate application to June 1, 2016
31 (with a 2017 test year) and to defer recovery of 2016 costs of approximately \$4 million.
32 Newfoundland Power's primary justification for the Application is the extraordinary nature of
33 Hydro's general rate application and the foreseeable consequences of Hydro's general
34 application on the Board's regulatory calendar.
35

36 The Board acknowledges Newfoundland Power's concerns in relation to the regulatory process
37 associated with Hydro's ongoing general rate application. While the Board accepts that the
38 circumstances surrounding Hydro's general rate application may be extraordinary, the Board
39 believes that a sound regulatory process for Newfoundland Power should not be based on a
40 planned process for Hydro's general rate application. The Board finds that there is no
41 requirement for the Hydro general rate application to conclude before Newfoundland Power files
42 its general rate application and further that issues associated with Hydro's general rate
43 application process can be addressed by the Board as appropriate in Newfoundland Power's
44 general rate application process.

1 In Order No. P.U. 13(2013) relating to Newfoundland Power’s last general rate application the
 2 Board found that a three-year period between general rate applications is generally consistent
 3 with sound utility regulation. The Board ordered Newfoundland Power to file its next general
 4 rate application with a 2016 test year by June 1, 2015. The Board accepted a ratemaking return
 5 on common equity of 8.8% for 2013 and 2014 and further stated that, in the circumstances, this
 6 rate should also be accepted for 2015. In addition the Board made a number of determinations
 7 based on the anticipated filing of Newfoundland Power’s next general rate application in 2015
 8 with a 2016 test year. In particular the Board established a three-year recovery, ending in 2015,
 9 for several deferral accounts, including a Weather Normalization Reserve balance, certain cost
 10 recovery deferrals, hearing costs and the 2013 revenue shortfall. In addition, in relation to
 11 depreciation, the Board stated:

12
 13 *The Board has ordered Newfoundland Power to file its next general rate application on June*
 14 *1, 2015. To ensure that the 2016 test year revenue requirement reflects the most up-to-date*
 15 *depreciation information the Board will require Newfoundland Power to file its next full*
 16 *depreciation study relating to plant in service as of December 31, 2014 with its next general*
 17 *rate application.*⁸
 18

19 A later filing of Newfoundland Power’s general rate application based on a 2017 test year, as
 20 proposed by Newfoundland Power, does not permit a full review and testing of Newfoundland
 21 Power’s 2016 costs, particularly in relation to cost of capital, depreciation, or amortizations of
 22 the deferral accounts. There has been no testing of Newfoundland Power’s 2016 forecast revenue
 23 and costs. Newfoundland Power did not provide evidence which demonstrates that it is
 24 appropriate to continue the ratemaking return of 8.8% for 2016. The Board finds there is no basis
 25 on which to make a finding that it is appropriate to accept the continuation of the 2013 and 2014
 26 test year revenues and costs, including the proposed return, as the basis for a request for the
 27 proposed deferral for 2016. A filing of a general rate application with a 2016 test year will
 28 provide the opportunity for a full testing of all costs to be recovered from customers in future
 29 rates.
 30

31 The Board will not approve the Application and confirms that, based on Order No. P.U.
 32 13(2013) and Order No. P.U. 15(2015), Newfoundland Power is required to file its next general
 33 rate application by October 16, 2015 with a 2016 test year.
 34

35
 36 **IT IS THEREFORE ORDERED THAT:**
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- 38 1. The Application is denied.
- 39
- 40 2. Newfoundland Power shall pay all expenses of the Board arising from this Application.

⁸ Order No. P.U. 13(2013), page 49.

DATED at St. John's, Newfoundland and Labrador this 15th day of July 2015.



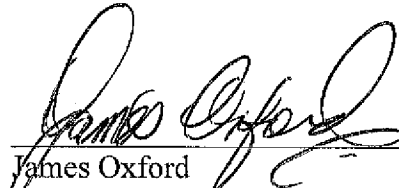
Andy Wells
Chair & Chief Executive Officer



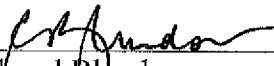
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