

**Date :** 4/14/2011 4:14:13 PM

**From :** "Bazeley, Dave"

**To :** "Bown, Charles W."

**Cc :** "Scott, Paul G."

**Subject :** Normal vs Nalcor Process

**Attachment :** Normal vs Nalcor Process.doc;

First cut, to see if on the right track for you.

| <b>“Normal” Process</b>                                                                                                                                                                                                                                      | <b>Comments</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | <b>Nalcor Project Proposal</b>                                                                                                                                                                                                                                                                                                                                                                                                                | <b>Comments</b>                                                                                                                                                         |
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| PUB is responsible to ensure that adequate Planning is done for electricity supply.                                                                                                                                                                          | PUB had requested Hydro to do an Integrated Resource Plan, but Hydro, with Government’s support, argued that it was inappropriate while there was uncertainty over Lower Churchill                                                                                                                                                                                                                                                                                                                                                                                                                                 | Nalcor has done planning.                                                                                                                                                                                                                                                                                                                                                                                                                     | PUB is unable to judge its adequacy as it has no jurisdiction over Nalcor                                                                                               |
| When forecasts show a supply shortfall (capacity and/or energy) Hydro would need to present PUB with a plan to meet it, showing that its selected option(s) met the criteria of least possible cost consistent with reliable service                         | Since Hydro became regulated (1996) this has never been allowed to occur. Either Government has exempted new generation (Granite Canal, Abitibi-Fortis, CBPP Cogen) or the new supply has been non-capital and lower cost than existing sources (wind vs Holyrood) so Hydro has not sought approval.<br>As a result, PUB has not established a process. It was thought generally that Hydro would have to examine not only its own projects, but to solicit offers to sell power from the private sector. This happened in 1997, but the process was cancelled when the original VBN smelter proposal was shelved. | Nalcor does not intend to present its plan to PUB, and asks Government to force PUB to accept MF & LIL as least cost alternative for Hydro.<br><br>Hydro’s annual filing with PUB of generation expansion alternatives has included two small hydro projects which Hydro considers to be in its portfolio. This limited selection has been defended on the grounds that they are the only projects for which Hydro has recent cost estimates. | The JRP appeared less than fully convinced that all possible alternatives had been explored. Whether the further information supplied satisfied the Panel is not known. |
| PUB would have to rule on whether it accepted Hydro’s recommended action or that something else should be done. Effectively it would decide on the prudence of the investment or commitment involved. PUB may hold a hearing process or some other approach. | The idea of ruling on the prudence is not in the legislation, and there are no precedents. Prudent investment is a concept that has been used in other jurisdictions.<br>If the approved solution were a PPA arrangement from Hydro’s perspective, the PUB can order what part of the cost is included in the rate base..                                                                                                                                                                                                                                                                                          | Nalcor does not intend to present its plan to PUB for approval, but asks Government to force PUB to accept MF & LIL as least cost alternative for Hydro.                                                                                                                                                                                                                                                                                      |                                                                                                                                                                         |
| If PUB accepted a capital project by Hydro as the best solution to the forecast supply shortfall, PUB would then have to rule annually on the appropriate items in Hydro’s capital budget application (CBA)                                                  | PUB can hold a hearing process on the CBA. However, if the project had been deemed prudent, PUB could not disallow expenditures. PUB may have potential to disallow the recovery of cost overruns.                                                                                                                                                                                                                                                                                                                                                                                                                 | Nalcor plans to fund the construction with Emera and Government. For LIL PUB will not consider capital expenditures, initial Rate of Return on Rate Base (RoRB) and extraordinary repairs                                                                                                                                                                                                                                                     | There is no independent oversight or transparency envisaged by Nalcor on capital expenditures, other than for the shareholder.                                          |

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| Hydro would have to report annually to PUB on progress and costs in each CBA.                                                                                                                         |                                                                                                                                                                                                                                                                                                                                                                          | Nalcor only reports to the shareholder and a public Annual Report.                                                                                                                                                                                                                                                                                                   |                                                                                                                                                                                   |
| Once the project is completed and commissioned, Hydro would apply to have the costs recovered in rates. Capital cost would go into the rate base, operational costs into the annual operating budget. | These costs are worked into the Cost of Service and hence into rates.                                                                                                                                                                                                                                                                                                    | Nalcor proposes that primary costs be disclosed to PUB but that PUB have no discretion to approve or disapprove them, other than for LIL sustaining capex, opex and changes to the (subject to being equal to NP's return). PUB would have no view of MF other than the PPA cost, which it asks Government to ensure is either exempt from or approved by PUB.       | PU would set the transmission tariff on LIL, but the primary cost drivers would be beyond PUB purview.                                                                            |
| The contribution of the specific capital project to the overall rate base in subsequent years would <i>decrease</i> as the value depreciates and the debt is paid off.                                | Effectively what goes into rates from a capital project declines on real terms over time.                                                                                                                                                                                                                                                                                | Nalcor's proposal for the PPA includes paying the transmission tariff for all capacity on LIL (even though Hydro's power will use 40% in the first year, forecast to gradually increase as Island demand grows), plus a generation rate that covers initially 66% of MF cost and <i>increases at CPI</i> (even though MF is almost entirely a capital cost project). | No justification for the increase in the generation rate has been presented.                                                                                                      |
| Hydro's approved rates then determine NP's rates. NP does not have a contract with Hydro, but presumably buys its required power from Hydro as the least cost alternative.                            | Whether this would continue in the situation where Hydro's rates increase rapidly would depend on alternatives available to NP. It has the responsibility to supply its customers at lowest possible cost consistent with reliable service, so logically if it could find a lower cost alternative, even a partial one, it should propose it to PUB and get it approved. | Nalcor asks Government to ensure that NP buys all incremental power from Hydro, preferably contractually for greater certainty. Nalcor also asks Government to take steps to ensure that NP has no other alternatives.                                                                                                                                               | How Government addresses these requests has not been determined. In particular, ensuring that a privately-held company signs a contract with which it may not agree is uncertain. |