NR 2017-[redacted]

[redacted]

[redacted]

TITLE: Reference Questions on Electricity Rate Mitigation for the Board of Commissioners of Public Utilities (PUB)

ISSUE: Whether to provide reference questions on electricity rate mitigation to the PUB under s. 5 of the *Electrical Power Control Act, 1994* (EPCA).

RECOMMENDATION(S):

It is recommended that:

1) Approval be given for the issuance of an order in Council, pursuant to section 5 of the *Electrical Power Control Act, 1994,* referring to the Board of Commissioners of Public Utilities a matter related to electricity rate mitigation, substantially along the lines of that attached in Annex 2;

2) If required, the Lieutenant Governor in Council, pursuant to subsection 245(2) of the *Corporations Act,* will make a written directive to Nalcor Energy, instructing the board of directors to fully cooperate with the PUB in relation to the reference questions described in section (1).

BACKGROUND:

In Nalcor's June 23, 2017, update on the Muskrat Falls Project (MFP), which includes the Muskrat Falls generating station, the Labrador Island Link Transmission Project (LIL), and the Labrador Transmission Assets Project (LTA); the company provided an update on costs and rate impacts. While the costs of the MFP will impact several rate classes, Nalcor stated that if no mitigating actions are taken, average island residential electricity rates, for example, would increase to 22.89 cents (plus HST) per kilowatt hour (kWh) in 2021 when Newfoundland and Labrador Hydro (NLH) begins paying its contracted MFP costs, increasing to 23.3 (plus HST) cents the year after. The present average island residential electricity rate for customers is 11.7 cents/kWh (plus HST).

Such an increase could reasonably be described as “rate shock,” which the PUB has indicated in the past is an annual rate increase exceeding ten percent, which would cause financial hardship for many residential customers. To illustrate further, it is useful to consider the information on projected electricity rates that Nalcor presented in its June 2017 MFP update, and the potential impacts on the province’s 257,000 families (includes couples, single parents, and individuals). The Department of Finance (FIN) advises that at the June 2017 rate of 11.7 cents per kWh (plus HST), 18,500 “family types” (i.e., couples, single parents, and single individuals) spend 10 percent or more of their disposable annual income on electricity. At the projected 2022 unmitigated rate of 23.3 cents/kwh, the number of family types spending 10 per cent or more of their disposable annual income on electricity would increase to approximately 72,000. If the rate can be mitigated to be 18 cents/kWh, FIN estimates approximately 47,000 family types would spend 10 percent or more of disposable income on electricity. While the impact of the MFP costs on other rate classes has yet to be estimated, it is likely the magnitude of the impact on those rate classes will be similar to that of residential rates.

This submission discusses rate mitigation and smoothing as separate types of actions for reducing addressing rate shock. This submission refers, generally, to rate smoothing as rate increases in advance of MFP commissioning while mitigation refers to options for reducing the amount of revenue NLH will require in rates upon commissioning.

Reducing the projected impact of the MFP on electricity rates is a key priority for the Government of Newfoundland and Labrador (GNL). The GNL’s Budget 2017 directed Nalcor to establish a “Rate Management Reserve” and to source opportunities to lower rates in the future. The Rate Management Reserve was projected to be $210 million in 2020/21 and $245 million in each of the two subsequent years, although if the Province wishes to continue to mitigate electricity rates, additional annual funding will be required. The related load forecast was based on prices starting at 18 cents per kWh. Nalcor’s total estimated cost (or revenue forgone) to mitigate rates from 22.89 cents per kWh to the load forecast basis of 18 cents for 2021, on a straight subsidization basis, is approximately $280 million annually, declining over time primarily due to rates escalating at 2.2 percent per year, and an increasing load forecast in years after the initial price increase. The Department of Natural Resources (NR), FIN, and Nalcor officials have formed a working group to develop further options for rate mitigation. These could include cost cutting measures and revenue growth opportunities through greater electrification (including industrial facilities, Memorial University and electric vehicles), and incentives to attract new customers. The working group has drafted a preliminary list of options for further analysis, which is presented as Annex 3.

In addition to this internal GNL approach, it is likely beneficial for the PUB to take a leading role in rate mitigation, given its subject matter expertise in this area and that a part of current and upcoming General Rate Applications, it will be called on to address certain rate smoothing issues. Premier Ball's December 15, 2015, Mandate Letter to the Minister of Natural Resources provides direction to enhance transparency and accountability with regard to Nalcor. This mandate can be met most thoroughly with regard to rate mitigation by providing reference questions to the PUB seeking options to mitigate MFP-related electricity rate increases. In addition, the PUB process would provide an opportunity for the public to have input into the rate mitigation process.

Such a role for the PUB is also entirely consistent with its mandate. The EPCA includes direction that all sources and facilities for the production, transmission, and distribution of power in the province should be managed and operated in a manner that would result in the most efficient production, transmission, and distribution of power for NL customers, and that power being delivered to consumers in the province should be provided at the lowest possible cost consistent with reliable service. The EPCA further directs that in carrying out its duties and exercising its powers under the EPCA, the PUB shall implement such power policies as outlined is Section 3 of the EPCA, and in doing, so shall apply tests which are consistent with "generally accepted sound public utility practice." The *Public Utilities Act* (PUA) further elaborates on the role of the PUB to broadly examine and approve electricity rates for the province. Accordingly, the PUB is well positioned to review issues that affect electricity rates in NL. Further discussion on how other jurisdictions' regulators have been involved in rate mitigation is provided in the Other Jurisdictions section below.

Thus, while the PUB has a mandate to address rate mitigation for regulated NLH operations, MFP operations are exempt from the provisions of the PUA and EPCA, pursuant to the *Muskrat Falls Project Exemption Order* and accompanying direction to the Board (OC2013-343), which requires the PUB to allow recovery of MFP costs in rates, including capital, operating, and maintenance costs. GNL put in place the exemption order as a means of ensuring compliance with provisions of the November 20, 2012, *Federal Loan Guarantee* ("FLG1"), signed by the Governments of Canada, Newfoundland and Labrador, and Nova Scotia as well as Nalcor and Emera Inc. FLG1 Schedule A states that GNL commits to ensuring that the regulated rates of NLH will allow it sufficient revenue to pay its MFP-related obligations. While GNL chose to meet this FLG1 commitment by effectively exempting MFP costs from PUB disallowance, this should not prohibit the PUB from reviewing and reporting to GNL on the prudence and reasonableness of MFP sustaining capital, operating, and maintenance costs, which are significant components of the anticipated MFP-related rate increases. Furthermore, the Government of Canada has a vested interest in supporting actions to make rates more affordable as doing so will help to reduce the risk of higher rates that would push customers away from electricity and reduce NLH revenue to pay its MFP obligations and risk triggering the federal loan guarantees.

MFP development issues are the subject of a separate and concurrent submission to Cabinet on a public inquiry into the MFP. Therefore the proposed PUB reference questions do not seek to address MFP sanctioning, development, or financing issues. In any event, costs already incurred cannot be disallowed retroactively, pursuant to the terms of the financing agreements/FLG, and thus could not be used to mitigate rates.

There are two possible scenarios through which PUB involvement in rate mitigation related to the MFP could arise: 1) Government could direct the PUB via reference questions from the

Lieutenant-Governor in Council (LGIC) under the EPCA; or, 2) Government could wait for the PUB to take self-directed action through its authority under the *Public Utilities Act* (PUA) to investigate unreasonable rates.

Reference Questions to the PUB

The LGIC may refer a question to the PUB on a matter related to rate mitigation under the EPCA. The LGIC has discretion to make the reference questions as general or specific as desired, to specify criteria, factors and procedures, and to set timelines for the reference. This process would result in non-binding recommendations being made by the PUB.

While Government may set timelines for the PUB to complete its work, the timelines would have to reasonably consider the PUB's ongoing regular hearings and activities, and also consider that one of four commissioner positions is now vacant and another commissioner's term is expiring in April 2018. If vacancies are not filled, the PUB's work on the reference could take longer to complete. The timeline for completion should also reflect that it is likely reasonable to expect the PUB to take longer to complete a rate mitigation process than the GNL/Nalcor internal process, given that when a question is referred to the PUB by the LGIC, the PUB is required to hold public hearings with submissions and rounds of formal "Requests for Information" likely from Newfoundland Power, the consumer advocate, industrial customer group, intervenors and other interested parties. [redacted]

The PUB's mandate is to regulate electric utilities in the province to ensure that the rates charged are just and reasonable for ratepayers, and the PUB has no mandate to address broader socio-economic issues or issues pertaining to taxpayers, generally. However, within these confines, it must be recognized that even in response to highly prescriptive reference questions, it is difficult to anticipate all factors the PUB will take into account in its investigation, what will be the results of the investigation, what recommendations the PUB will make, and in general, what will be the content of PUB's report. While these recommendations are not binding, they will be public. NR staff held several discussions with PUB staff (i.e. not PUB commissioners) in order to seek to ensure, insofar as possible, a common understanding of the intent and desired outcome of the reference questions.

With regard to the proposed draft reference questions specifically, they require the PUB to review and report to the Minister of Natural Resources on options to fund the mitigation of rates resulting from the MFP entering into service; options to smooth the transition to higher rates in advance of the MFP entering into service; and report on the potential impacts of the identified rate mitigation options on rates, based on the most recent MFP cost estimates. The draft reference questions are appended as Annex 2.

Await PUB Action

Instead of directing the PUB, GNL could wait for the PUB to exercise its own discretion on whether to address rate shock. The PUB is presently assessing a NLH General Rate Application (GRA) to increase rates in 2018 and 2019 and use savings from off-Island supplies to reduce Holyrood thermal generating costs, which NLH estimated in a GRA filing would accumulate savings of approximately $143 million over the period to be applied to rates beginning in August 2020 to reduce rate shock. However, this is a much narrower window for the PUB to consider rate mitigation than proposed reference to the PUB. The PUB also has jurisdiction to initiate its own investigation under of the *PUA*, if it believes a rate is unreasonable or unjustly discriminatory. However, it is unlikely this could be an effective approach to rate mitigation for several reasons:

- the PUB could likely only take this step after receiving an application for 2020 rates, thus limiting its ability to implement measures in advance to assist with rate mitigation;
- authority provided by this provision would not easily lend itself to an investigation of rate mitigation as the remedies provided in the *PUA* in relation to this provision are limited to regulated rate inputs, and do not include other sources of revenue;

- o the scope of remedies available to the PUB under the *PUA* would not allow the implementation of measures outside of the disallowance of costs, which may be largely prevented by the *Muskrat Falls Exemption Order* and accompanying direction to the PUB, along with other MFP-related exemption orders;
- o without direction from Cabinet, the PUB's jurisdiction would not extend to non-regulated aspects of Nalcor Energy, such as export power, the MFP project entities, Nalcor Energy Marketing, and Nalcor's corporate structure.

<u>ALTERNATIVES:</u>

It is recommended that:

1. Direction be given undertake the process recommended on page 1: **(Recommended)**

<u>Advantages</u>

- Provides a degree transparency and accountability around development of rate mitigation options that likely could not be achieved through an internal Government or Nalcor processes;
- Enables public input into rate mitigation through an effective regulatory mechanism already in place;
- Provides Government with an independent expert assessment of electricity sector rate mitigation options;
- If the PUB concludes that MFP–related, or other Nalcor operational, savings can be achieved, Government will have the option as to whether or not to direct Nalcor to reduce such costs accordingly;
- Does not require Government to end NR's Rate Mitigation Committee with FIN and Nalcor.

<u>Disadvantages</u>

- Risk of PUB interpreting reference questions in unexpected ways thus extending scope beyond Government's intention;
- It might be challenging for Government to reject any PUB recommendation that does not align with competing Government policy objectives;

- Might suggest to some that Government lacks confidence in Nalcor CEO or Board to develop effective rate mitigation options.

2. To await PUB action to take self-directed action through its authority to investigate unreasonable rates

   Advantages

   - Does not require immediate action on behalf of GNL.

   Disadvantages

   - PUB would not likely undertake in-depth review of mitigation options until NLH files a General Rate Application for 2020 rates, likely in 2018 or 2019;
   - Does not demonstrate immediate action on commitment to rate mitigation;
   - PUB would consider only regulated NLH operations and not other unregulated Nalcor operations such as MF/LIL/LTA operating and maintenance costs or corporate structural efficiencies, etc., which might provide additional potential rate mitigation options;
   - Would not consider solutions other than rate inputs.

3. To continue with only Government/Nalcor Working Group on Rate Mitigation

   Advantages

   - Retains full Government responsibility for rate mitigation outcomes (including the option to enhance transparency of and public participation in the identification of rate mitigation mechanisms)

   Disadvantages

   - Would not demonstrate the same degree of transparency and accountability with regard to Nalcor and MFP costs that would arise through a quasi-judicial PUB process;
   - While Natural Resources chairs the committee, Nalcor and NL Hydro are full participants and as such are unlikely to advocate for any significant changes to Nalcor or NL Hydro from a cost savings perspective;

- Greater public participation would also require the establishment of a mechanism or process;
- Does not automatically provide independent, unbiased assessment of options.

[redacted]

[redacted]

FINANCIAL CONSIDERATIONS:

Government has stated publically that it requires between $60 and $70 million to reduce rates by a cent. With a projected rate of 22.89 cents per kWh, it has been identified that roughly $280 million will be required to reduce rates to 18 cents per kWh in the first year full year of operations. This will slowly decline, as rates are raised by 2.2% per year, to around $250 million in 2024. The Province does not earn a rate of return on the LCP, but it can direct Nalcor to return a dividend to Government at any time. This dividend could include amounts from Nalcor's rate of return (between 8.4% and 9.2%) on the LCP, which is established by contract. It would be within the Province's discretion to use any amount collected by the Province from Nalcor towards rate mitigation.

Budget 2017 directed Nalcor to source $210 million to lower electricity rates. The province has agreed to forego profits from excess MFP energy sales and also allowing for a reduction in its net income / dividends. That is a general reduction not targeted to any specific line of business. The anticipated contribution of export sales from 2020-21 to 2022-23 is $25.2M, $49.0M and $45.5M respectively. The province's plan also assumes the following amounts from Nalcor's dividend to the province, $60M, $75M and $90.9M, be allocated to rate mitigation over the first three years (2020-21 to 2022-23) and $90M annually thereafter. This leaves an unknown of approximately $120 million of the $210 million reserve to be identified by Nalcor.

Recent discussions with senior Nalcor finance officials have indicated that Nalcor has only managed to identify saving (through the use of off island power purchases to reduce Holyrood generation costs) to fully cover 2020/21 and partially cover 2021/22. While Government has stated to Nalcor that they are expected to identify further sources for the $120 million for 2021/22 and beyond, there remains a significant risk that these savings will not be found. Should this happen, Government will face further deterioration in the net income from Nalcor included in the fiscal framework.

Any costs of the PUB in respect of this review shall be paid by Nalcor, and shall not be considered MFP costs. As noted, GNL's most recent electricity-related reference question to the PUB was the June 2011 Muskrat Falls Reference Question on two predetermined supply options. The PUB issued its report nine months later in March 2012 at a cost of $2.1 million to be recovered from Nalcor. The reference on rate mitigation can be expected to have a marginally higher cost as it is more open-ended and allows three additional months for completion. It is important to note that any net savings or income that can be derived from Nalcor beyond the amounts already included in the fiscal framework, can ultimately be a dividend to GNL (i.e. taxpayers benefit) or a taxpayer-funded subsidy to reduce rates (i.e. ratepayers benefit). Any options and/or recommendations the PUB identifies for rate mitigation would not be binding on GNL and it would remain GNL's prerogative to determine whether to direct the immediate benefit of taxpayers or ratepayers.

INTERDEPARTMENTAL CONSIDERATIONS:

The Public Engagement Division of the Communications and Public Engagement Branch advises it has revised this submission and advises it has no concerns from a Rural Lens or Public Engagement perspective.

LABRADOR OR ABORIGINAL CONSIDERATION:

Island interconnected rates have no direct relation to Labrador interconnected system rates, thus this submission has no impact on these customers. Labrador diesel system rates are tied to Island interconnected rates, thus any action to mitigate Island rates would also benefit Labrador diesel customers.

INTERGOVERNMENTAL CONSIDERATIONS:

IIAS agrees that the Government of Newfoundland and Labrador should advise the federal government of the proposed reference to the PUB in order to provide clarity around intent, and preempt any concerns that the PUB's engagement could result in an outcome that would be contrary to the terms of the FLG.

OTHER JURISDICTIONS:

Taking action to mitigate significant rate increases is common practice in North America. Power Advisory's 2015 report to GNL noted; "…where large capital projects have been added to the supply system and could have caused significant rate increases or "rate shock", policy makers and regulators have mitigated the rate impacts through various measures such as spreading out the initial rate impacts over a longer period of time. Reducing significant rate increases for large long-term capital investments is a common practice."

For example, Manitoba Public Utilities Board Order 73/15 in 2015 approved rate increases in advance of the completion of a large-scale transmission project, and noted that "Manitoba Hydro is making very large capital investments to meet its projected energy and capacity requirements and to replace its aging assets. The funds set aside in the Board-ordered deferral account, including revenues from the 2.15 percent portion of the total rate increase, will be used to smooth the significant rate increases that may otherwise be required when the Bipole III Transmission Reliability Project (Bipole III) is completed, resulting in rate shock."

CONSULTATIONS:

NR has not consulted with Nalcor or its subsidiaries in drafting this submission. Cabinet may wish to instruct NR to advise Nalcor of the reference questions prior to providing the reference to the PUB.

NR staff consulted with PUB staff, but not PUB commissioners, in the development of the proposed reference questions and to help to minimize the potential for the PUB to misinterpret any reference questions. PUB staff expressed confidence in the PUB's ability to complete the task effectively with some of the following caveats. PUB staff noted the November 2018 completion deadline would be difficult to achieve without receiving the reference questions by early November and without Government acting swiftly to fill the one current and one impending commissioner position vacancies. The PUB has four full-time commissioner positions, but the chair is currently vacant, and commissioner Dwanda Newman's ten-year term ends in April 2018. Action to appoint a new chair and appoint or reappoint the other commissioner will help ensure PUB capacity to deliver its report on time as it is also working to address a government reference on automobile insurance, review NLH's 2017 General Rate Application, and complete other ongoing regulatory processes. PUB staff also noted that if the reference questions do not include unregulated Nalcor activities, then Nalcor will likely refuse to provide the PUB with any information it might request on such activities.

The PUB also asked government to share the final reference questions a week or two prior to publicly announcing it to enable the PUB time to consider its resources and planning, and in order to be prepared to address these issues when government makes the announcement.

ENVIRONMENTAL CONSIDERATIONS:

The proposed PUB reference has no environmental implications.

COMMUNICATIONS AND CONSULTATION SYNOPSIS:

The communication synopsis is provided in Annex 1.

ANNEXES:

Annex 1 – Communication Plan
Annex 2 – Proposed Reference Questions
Annex 3 – NR, FIN, Nalcor Rate Mitigation Working Group

Hon. Siobhan Coady, MHA
Minister of Natural Resources

November 10, 2017

Annex 1
COMMUNICATIONS PLAN
Department of Natural Resources

Title: Reference questions on Electricity Rate Mitigation for the Board of Commissioners of Public Utilities (PUB)

Issue: Whether to provide reference questions on electricity rate mitigation to the PUB under s. 5 of the Electrical Power Control Act, 1994 (EPCA)

Consulted with:	**Date drafted:**	**Announcement date:** TBD
Corey Snook, Director of Electricity and Alternative Energy John Cowan, Assistant Deputy Minister, Energy Policy	October 12, 2017	

COMMUNICATIONS ANALYSIS

Public Environment

In June 2016, CEO Stan Marshall gave an update on the Muskrat Falls Project's cost and schedule. CBC reported that costs for the project had increased and the domestic rate of power was expected to almost double the current rate:

> The cost of the project has ballooned to $11.4 billion, including interest. That's an increase of $4 billion — with interest factored in — from when the project was first sanctioned in 2012. By 2022, the domestic rate for power is expected to jump to nearly 22 cents per kilowatt hour, almost double the current rate of 11.9 cents. For the average homeowner, Nalcor estimates this could mean an extra $150 per month in power costs, before HST, which Marshall described as not affordable. "Muskrat Falls was not the right choice for the power needs of this province," he said.
> http://www.cbc.ca/news/canada/newfoundland-labrador/stan-marshall-muskrat-falls-update-1.3649540

After the cost and schedule update was given, the Premier announced that he had directed Nalcor to look at ways to manage rates. He said:

> I have already committed to offset electricity rate increases associated with the Muskrat Falls Project through the sale of excess power, and given the rebaselining we are directing Mr. Marshall to identify other opportunities to bring rates closer to those predicted at sanction.

In Budget 2017, the Minister of Finance announced that further direction had been given to Nalcor to lower electricity rates:

> Mr. Speaker, our vision for the province does not include the doubling of electricity rates. It is not acceptable for residents to pay excessive electricity rates. Future electricity rate management is a priority of our government. Nalcor has been directed to source $210 million

> to lower electricity rates starting in 2020-21, with this preliminary rate reserve growing to $245 million in the following fiscal years. We are committed to ensuring electricity rates are competitive and will undertake work to further define mitigation actions and dollars required.
> http://www.budget.gov.nl.ca/budget2017/speech/default.htm

In June 2017, Nalcor publicly announced that there was another billion-dollar increase in the projected cost of the Muskrat Falls Project with expected impacts on rates. As expressed in a CBC story:

> The new estimate is $12.7 billion, including financing and other expenses, according to a briefing by the chief executive of Nalcor Energy, Stan Marshall…Consumers will see the burgeoning cost of Muskrat Falls in their power rates. Nalcor Energy now expects that in 2022, domestic customers on the island of Newfoundland will pay 23.3 cents per kilowatt hour. That will be nearly double today's rate, unless the government takes measures to mitigate the increase.
> http://www.cbc.ca/news/canada/newfoundland-labrador/stan-marshall-muskrat-falls-nupdate-1.4174569

In the same CBC article, the Premier said:

> Our vision for the province does not include doubling electricity rates … rates must remain competitive.

In July 2017, the Canadian Federation of Independent Business released a policy brief stating its concerns of increasing rates on businesses:

> The cost of the Muskrat Falls Project is forecast to essentially double electricity rates for some customers in the province. If this forecast is met, it could mean an additional cost of $170 million annually for small and medium sized enterprises, resulting in reduced profits and/or increased prices for customers. With rate mitigation efforts, electricity rates should not double when Muskrat Falls power generation begins; however, this will likely mean the taxpayer pays.

In September 2017, there was an article in the Financial Post that outlined the concerns of electricity increases:

> Government-owned utilities have a costly, longstanding habit they can’t seem to kick: megaprojects. In B.C., Manitoba, Ontario and Newfoundland and Labrador, public utilities are constructing megaprojects — typically defined as infrastructure projects costing more than $1 billion — that will cost electricity customers, at current estimates, $43 billion. The final cost to electricity customers, already expected to result in double- or triple-digit rate increases, will be a great deal higher once these megaprojects start generating power, given the track record of megaprojects of consistently coming in over budget and behind schedule. Two of the four megaprojects, already deep into construction, have experienced cost overruns of more than 100 per cent and are years behind schedule.
> http://business.financialpost.com/opinion/governments-mega-utility-projects-spell-mega-ruin

Strategic Considerations

The costs of the Muskrat Falls Project will impact rates and is a major concern for residents and businesses in the province.

The June 23, 2017 update on the Muskrat Falls Project by Nalcor Energy forecasts that, without taking mitigating actions, rates for domestic customers on the Island of Newfoundland will increase to 22.89 cents per kilowatt hour in 2021, and related increases are expected for other Island rate classes. This rate increase is primarily attributable to the impact of cost recovery required for the Muskrat Falls Project.

These projected rate increases, if unmitigated, would likely cause financial hardship for customers in all rate classes on the island portion of Newfoundland and Labrador.

Government is developing options to reduce the impact of these increases to the rates of all customers of the island portion of the province.

An internal committee within government is tasked with ensuring rates are managed as best as possible. The internal committee includes the Department of Natural Resources, Finance, NL Hydro and Nalcor. Natural Resources is chairing the committee. The committee will consider all opportunities that could support rate mitigation and if others need to be brought in to further inform a specific idea or rate mitigation that will happen.

All options are being explored and may include:
- exporting surplus recall energy from the Upper Churchill;
- bringing surplus power from Labrador across the Labrador Island Link for use on the island;
- purchasing and importing less expensive power via the Maritime Link and Labrador Island Link;
- developing export markets to grow revenues from export sales;
- finding ways to use energy more efficiently, reduce peak demand, to free up capacity for exports and domestic customers; and
- expanding customer base within the province.

To assist with Government's rate mitigation initiative, it is recommended that the matter of electricity rate mitigation be referred to the Board of Commissioners of Public Utilities (PUB) with the full cooperation of Nalcor Energy's board of directors.

Having the PUB involved with the process enables public input into rate mitigation through an effective regulatory mechanism already in place, provides transparency and accountability around development of rate mitigation options, and provides an independent expert assessment of electricity sector rate mitigation options.

While government may set timelines for the PUB to complete its work, the timelines would have to reasonably consider the PUB's ongoing regular hearings and activities. Also, there will likely be public pressure to release a copy of the report to general public at the earliest opportunity and to implement any recommendation.

It is expected that PUB involvement will be perceived positively in the public, particularly because the PUB had not been permitted to undertake a review of the project prior to sanction. A public announcement of the PUB review will renew concerns and public dialogue regarding the expected increase in rates and options for managing these rates.

Target Audiences

Internal

- Premier's Office
- Communications and Public Engagement Branch
- Natural Resources
- Justice and Public Safety
- Finance
- Office of Labrador Affairs
- Intergovernmental and Indigenous Affairs Secretariat
- Cabinet
- Caucus

External

- Nalcor
- Government of Canada (Natural Resources Canada)
- Local media (traditional and social)
- Official Opposition
- Third Party
- Indigenous groups including Innu Nation, Nunatsiavut Government, and the NunatuKavut Community Council
- Consumer Advocate
- Public Utilities Board
- Members of the House of Assembly
- Critics of the Muskrat Falls Project
- Residents of Newfoundland and Labrador

Consultations

Officials from Natural Resources have consulted with the departments of Justice and Public Safety, Finance, Intergovernmental and Indigenous Affairs Secretariat, and officials from PUB.

To date, officials from Natural Resources have not consulted with Nalcor or its subsidiaries.

The Premier's Office and Communications and Public Engagement Branch will be consulted with regard to the communications approach for the announcement of the PUB review.

The provincial government will advise the federal government of the proposed reference to the PUB in order to provide clarity around intent, and preempt concerns that the PUB's engagement could result in an outcome that would be contrary to the terms of the federal loan guarantee.

Communications Objectives

- To inform the people of the province regarding the details of the PUB review.
- To reassure the people of the province that government is taking the steps necessary to manage the Muskrat Falls Project to its completion, and to mitigate rates in the coming years.
- To facilitate balanced reporting in local and national media; and balanced comments on social media and in blogs.

COMMUNICATIONS STRATEGY

Overall Approach

The Minister of Natural Resources will lead a news conference to announce the details of the PUB review. The location for the news release is to be determined.

Materials to be developed include media advisory, news release, speaking notes, key messages, questions and answers and tweets.

Social Media

Tweets will be posted regarding the details of the PUB review and government's position.

Key Messages

Today, we are announcing that the Board of Commissioners of Public Utilities will be reviewing rate management options, specifically rate mitigation options, based on the most recent cost estimates of the Muskrat Falls Project.

This will be done with the full cooperation of Nalcor Energy's board of directors.

Having the PUB involved with the process enables public input into rate management for the province.

This process also provides an independent expert assessment of electricity sector rate mitigation options, as well as transparency and accountability around development of rate management options.

Any costs of the PUB regarding this review will be paid by Nalcor, and will not be considered Muskrat Falls Project costs.

The PUB's report will be provided to the Minister of Natural Resources by [November 30, 2018.]

The Minister will make the report public.

Secondary Messages

Future electricity rate management is a priority of our government; and we are committed to doing everything possible to ensure electricity rates are competitive.

The former government used questionable assumptions and cost controls regarding the Muskrat Falls Project; that's why we are faced with this situation to begin with.

We have directed Nalcor to source $210 million to lower electricity rates starting in 2020-21, with this preliminary rate reserve growing to $245 million in the following fiscal years.

In addition, an internal committee within government is tasked with ensuring rates are managed as best possible.

The internal committee includes the Department of Natural Resources, Finance, NL Hydro and Nalcor. Natural Resources is chairing the committee. It will meet every two weeks starting off, and as plans become formalized it would move to monthly.

The committee will consider all opportunities that could support rate mitigation and if others need to be brought in to further inform a specific idea or rate mitigation that will happen.

All options are being explored and may include:
- exporting surplus recall energy from the Upper Churchill;
- bringing surplus power from Labrador across the Labrador Island Link for use on the island;
- purchasing and importing less expensive power via the Maritime Link and Labrador Island Link;
- developing export markets to grow revenues from export sales;
- finding ways to use energy more efficiently, reduce peak demand, to free up capacity for exports and domestic customers; and
- expanding customer base within the province.

The interests of the province's ratepayers are the priority.

Briefing of Members of the House of Assembly

Caucus will be provided with key messages

Follow-up Activities

Once the announcement is made, government will be prepared and open to continue the discussion publicly through social media, Open Line, media invitations, and speaking engagements.

Evaluation Criteria

Public discourse and media coverage will be monitored.

Prepared by: Diana Quinton, Director of Communications
Approved by: Gordon McIntosh, Deputy Minister

Annex 2 – Proposed Reference Questions

Reference Questions to the
Board of Commissioners of Public Utilities
Rate Mitigation Options and Impacts

The June 23, 2017 update on the Muskrat Falls Project by Nalcor Energy indicates the capital cost and during-construction financing costs of the Muskrat Falls Project have risen to $12.7 billion, which is more than double the estimated costs submitted to the Board of Commissioners of Public Utilities (the "**Board**") in the 2011 reference question, when the Board was asked to compare the Muskrat Falls Project and an isolated-island alternative. The obligations under the Federal Loan Guarantee, dated November 30, 2012, place the financial burden of the Muskrat Falls Project on Newfoundland and Labrador ratepayers. As a result, the June 23, 2017 update forecasts that, without taking mitigating actions, rates for domestic customers on the Island of Newfoundland will increase to 22.89 cents per kilowatt hour in 2021, and related increases are expected for other Island rate classes. This rate increase is primarily attributable to the impact of cost recovery required for the Muskrat Falls Generating Station, Labrador Transmission Assets, and the Labrador Island Link projects, collectively known as the Muskrat Falls Project (the "**MFP**").

These projected rate increases, if unmitigated, would likely cause financial hardship for customers in all rate classes on the island portion of Newfoundland and Labrador ("**Ratepayers**"). The Government of Newfoundland and Labrador wishes to develop options to reduce the impact of these increases to the rates of all customers of the island portion of the province ("**Rates**").

In July 2017, Newfoundland and Labrador Hydro ("**NLH**") filed a General Rate Application which, among other things, indicates that the transmission assets associated with the MFP will be completed and available for the import of electricity in 2018. Nalcor submits that this will allow access to potentially cheaper sources of electricity prior to MFP entering into service with any related savings to be placed in a deferral account to assist with mitigating MFP-related rate increases.

To assist with Government's rate mitigation initiative, pursuant to section 5 of the *Electrical Power Control Act, 1994*, the Government of Newfoundland and Labrador hereby refers the following matter to the Board:

The Reference Questions

The Board shall review and report to the Minister of Natural Resources on:

1) options to:

    (a) mitigate and manage Rates resulting from the MFP entering into service; and

(b) smooth Rates in anticipation of the MFP entering into service;

including identifying cost savings and revenue opportunities with respect to the electricity generation, transmission, distribution, sales, and marketing assets and activities of Nalcor Energy and its Subsidiaries, including NLH, Labrador Island Link Holding Corporation, LIL General Partner Corporation, LIL Operating Corporation, Lower Churchill Management Corporation, Muskrat Falls Corporation, Labrador Transmission Corporation, Nalcor Energy Marketing Corporation, and the Gull Island Power Company (together the "**Subsidiaries**", and collectively with Nalcor Energy, "**Nalcor**"); and

2) the potential impacts of the identified options, based on the most recent MFP cost estimates.

These questions are the "**Reference Questions**". In answering the Reference Questions, the Board shall consider, among other things, the power policy of the province, as set out in the *Electrical Power Control Act, 1994,* including paragraph 3(b)(iii), which states that the production, transmission and distribution of power should be managed in a manner that results in power being delivered at the lowest possible cost consistent with reliable service, and the following:

- what levels of annual rate increases are sustainable for ratepayers over what period of time, while ensuring competitiveness with other Atlantic provinces.

- new and existing sources of Nalcor income, outside of income from Newfoundland and Labrador ("**NL**") ratepayers, that could be put towards mitigating Rate increases, including income from:
  - Nalcor power exports, including those from generation assets it owns or controls, the MFP, and Churchill Falls recapture power, taking into account any export-related costs such as those relating to Nalcor Energy Marketing;
  - All or part of Nalcor's rate of return on the MFP; and
  - Any other effective opportunities to find synergies, efficiencies and reduce costs.

- whether NLH's regulated return on equity should be the same as that established for Newfoundland Power.

- whether it is more advantageous to Ratepayers to maximize domestic load or maximize exports. Depending on the Board's recommendation, provide options for:
  - increasing domestic load, such as:
    - The electrification of industrial facilities and oil-fueled boilers in heating plants; and
    - Incentives for increased electrification and usage by NL ratepayers, including increasing number of ratepayers, electric vehicles and electric heating; or
  - increasing exports, such as:

- Incentives for energy conservation, including for lowering system peak demand to maximize system capacity reserves, in order to increase availability of energy and capacity for export.

- forward-looking cost savings and opportunities for increased efficiency related to operating and maintenance of MFP.

- what are industry best practices related to external market purchases and sales of electricity.

- options for Rate smoothing in advance of MFP entering into service, including NLH Churchill Falls recapture power and paying for power during the commissioning of the MFP plant under the Power Purchase Agreement between NLH and the Muskrat Falls Corporation, dated November 29th, 2013.

In answering the Reference Questions, the Board shall not consider (a) options for the Provincial subsidization of rates beyond those noted above for Nalcor electricity-related activities, and (b) MFP construction costs.

Where Nalcor determines that any information to be given to the Board for this review is commercially sensitive as defined in the *Energy Corporation Act*, it shall advise the Board, and the Board and its experts and consultants may use such information for this review but shall not release such information to any party.

Any costs of the Board in respect of this review, shall be paid by Nalcor Energy, and shall not be considered MFP costs.

The Board's report shall be provided to the Minister of Natural Resources by [November 30, 2018.]

The Minister shall make this report public.

Annex 3 – NR, FIN, Nalcor Rate Mitigation Working Group

Ongoing or short term in nature:

- Optimization of TL267 an early utilization of the Labrador-Island Link (LIL)
- Full utilization of Recall power for ratepayers, pre and post MFP commissioning
- Increase utilization of transmission infrastructure
- Prioritize capital spend based on safety and reliability
- Nalcor/Power Supply operating/capital cost oversight
- Redirect Nalcor profit to customers
- Utilize future Rate Stabilization Plan at time of MFP commissioning
- Bilateral agreements vs. real time energy marketing
- Optimize water management (on/off peak and seasonality)
- Capacity and energy opportunities with Corner Brook Pulp and Paper Limited
- Displace oil heat with electric heat (MUN and other government buildings)
- Pre-MF Holyrood fuel displacement

Longer term options:

- Data centres
- Modify Labrador industrial rates
- Modify Labrador residential rates
- Reduce Northern Strategic Plan subsidies
- Segregation of distribution outside Newfoundland and Labrador Hydro
- Newfoundland and Labrador Hydro borrow to finance rate increase
- "Time of Use" pricing to reduce peak demand for capacity exports
- Sell Nalcor assets
- Issue Class C partnership units in the LIL (write off portion of the asset)
- Returns: no return on cost overruns; defer Nalcor return; cap a portion of the returns
- Usage of Twinco Block to serve all Labrador West load
- Opportunities with Hydro Quebec: Gull Island development; MF surplus
- Develop wind and offer as a firm product.
- Ideal Customer (requires high amounts of energy but not capacity)
- Cannabis regulation (residential and commercial load growth)
- Alternatives to selling energy directly to Quebec at NL/QC border

PUB Engagement in Rate Mitigation

November 2017

Proposal

- This submission seeks approval to:
  - Issue reference questions to the Board of Commissioners of Public Utilities (PUB) related to electricity rate mitigation;
  - If required, issue a written directive to Nalcor Energy board of directors to fully cooperate with the PUB in relation to the reference questions.

Reference Questions

The Board shall review and report to the Minister of Natural Resources on:

1) options to:
   a) mitigate and manage Rates resulting from the MFP entering into service; and
   b) smooth Rates in anticipation of the MFP entering into service;
2) the potential impacts of the identified options based on the most recent MFP cost estimates.

Newfoundland Labrador

Areas of Inquiry

- What levels of annual rate increases are sustainable for ratepayers over what period of time, while remaining competitive with Atlantic provinces?
- What new and existing sources of non-ratepayer Nalcor income could mitigate Rates including all exports, MFP rate of return, synergies, efficiencies, savings?
- Should NLH's regulated rate of return on equity equal Newfoundland Power's?

Newfoundland Labrador

Areas for Inquiry (continued)

- Which is better for Ratepayers: maximize exports or domestic load growth?

  Provide options for:
  - Load growth through incentives for greater electrification (e.g. electric vehicles, heating)
  - Increasing exports through incentives to conserve
- What MFP operating and maintenance savings are available?
- What are industry best practices for external market purchases and sales?
- What are the options for Rate smoothing in advance of MFP?

Newfoundland Labrador

Exclusions and Caveats

- Sources of funds limited to electricity – Nalcor/NLH
- Exclude MFP construction costs as they cannot be disallowed
- Nalcor must advise the Board of commercially sensitive evidence, Board and its experts and consultants may use the evidence but not release to any party
- All costs to be paid by Nalcor Energy (i.e. taxpayers) – not included in MFP costs
- Report to the Minister of NR by November 30, 2018
- The Minister shall make this report public

Newfoundland Labrador

Process Considerations - Advantages

- Enables PUB to consider unregulated activities, but limited to electricity
- Provides a degree of transparency and accountability not likely achievable through internal Government or Nalcor process
- Enables public input through an existing and effective regulatory mechanism
- Provides independent expert assessment of options
- Recommendations not binding – options for GNL to consider
- Does not require ending Rate Mitigation Committee (NR, FIN, Nalcor)

Newfoundland Labrador

Risks

- PUB could interpret reference questions in unexpected ways thus extending scope beyond Government's intention (consultations with PUB have minimized this risk)
- It might be challenging for Government to reject any PUB recommendation that does not align with competing Government policy objectives
- Might suggest that Government lacks confidence in Nalcor to develop effective rate mitigation options
- Nalcor Board reaction
- November 2018 completion assumes
  - Commissioner vacancies will be filled as soon as possible
  - PUB receives reference in November – early is better

Newfoundland Labrador

Other Considerations

- Taxpayer versus Ratepayer:
  - Any savings derived from Nalcor unregulated electricity activities would otherwise fund dividends to Government (i.e. benefit taxpayers)
- Nalcor to pay PUB costs (taxpayers) versus NLH (rate payers)

[redacted]

[redacted]

Attach to: **NR2017**[redacted]

[redacted]

Title	**<u>Reference Questions on Electricity Rate Mitigation for the Board of Commissioners of Public Utilities (PUB)</u>**
Summary of Proposal	The Submission seeks approval to refer to the Board of Commissioners of Public Utilities (PUB) a matter related to electricity rate mitigation, substantially along the lines of that attached in the Minister's Submission; and, if required, a written directive to Nalcor Energy, instructing the board of directors to fully cooperate with the PUB.

Secretariat Comment

1. The PUB is an independent regulatory body appointed by the Lieutenant-Governor in Council; it is responsible for the regulation of electrical utilities in the province to ensure the rates charged are just and reasonable. It has the regulatory authority to assess the merits of any rate application and impose any rate mitigation it deems appropriate to avoid rate shock

2. The PUB is currently assessing a NLH General Rate Application to increase rates in 2018-19 and use savings from off-Island supplies to reduce Holyrood thermal generating costs; as such, this specific question has not been included in the proposed reference.

3. The proposed reference questions have been developed by NR in consultation with JPS. The purpose is to ensure that the information obtained from such an inquiry will be most beneficial to inform Government policy, in consideration of the capacity of the PUB. While the potential for operational or corporate efficiencies within Nalcor or NLH is not explicitly targeted in the draft proposed reference questions, the PUB could interpret the reference questions to encompass other efficiencies for Nalcor and NLH.

4. OC2009-063 directed the PUB in calculating the return on rate base for NLH, to set the same target return on equity that was set for Newfoundland Power. The purpose was to increase the total net income that NLH was allowed to achieve and allow the Corporation to move significantly towards the investment grade rating required for it to be a creditworthy counterparty for Lower Churchill generation. It was also intended to enable NLH to have much greater financial stability in the longer term and be able to provide dividend flows to Nalcor Energy that will reduce the parent company's need for funds from Government for investment opportunities. The PUB will be asked to consider if the policy outlined in the Cabinet directive should continue.

5. It is proposed that the PUB will be asked to consider the sustainability of rate increases while ensuring competitiveness with Atlantic Canada. Cabinet Secretariat notes that consideration could be given to competitiveness nationally or internationally, given that the province markets itself in other jurisdictions outside of Atlantic Canada.

6. Nalcor has not been engaged in the development of the reference questions. NR recommends informing the CEO and Board of Nalcor

prior to providing the reference to the PUB.

7. It is anticipated that Nalcor will cooperate with a review; however, given that Nalcor activities are not normally under the purview of the PUB, there may be times where there are conflicting views regarding commercially sensitive information, which is protected under the *Energy Corporation Act* (ECA). In order to ensure that the PUB receives the information it needs, Government may be required to issue a written directive to Nalcor.

8. Cabinet Secretariat notes that the PUB's consideration of commercially sensitive information, as defined in the ECA, could potentially present an opportunity for litigation, which could delay proceedings.

9. Cabinet Secretariat notes that a reference to the PUB will not preclude Government from developing options for rate mitigation such as cost cutting measures, revenue growth opportunities, establishing an open-access regime and exploring any potential opportunities for re-financing of the Federal Loan Guarantee.

10. In accordance with section 117 of the *Public Utilities Act,* the LGIC appointed Dennis Brown as Consumer Advocate to represent the interest of domestic and general service customers. Mr. Brown's appointment was for one year and expired on October 11, 2017. Cabinet Secretariat notes that Mr. Brown was appointed separately for the 2011 PUB reference question with specific details regarding the reference question. OC2017-328 reappointed Mr. Brown as Consumer Advocate to provide general authority for other matters for which the Consumer Advocate would be consulted, and in addition to any other appointment the Consumer Advocate may receive to participate in specific hearings for the PUB.

Department of Finance

The Department of Finance notes that any costs of the PUB review will be paid by Nalcor. It is recommended by NR that those costs not be considered as MFP costs therefore not included in rates.

Secretariat Recommendation

Cabinet Secretariat recommends approval of the Submission, subject to [redacted] (iii) finalization of the communications plan in consultation with the Communications and Public Engagement Branch.

CO/KQ
November 11, 2017

[redacted]

2017/11/13

MC201[redacted] NR/DM Deputy Clerk File	NR201[redacted]. The Submission of the Minister of Natural Resources respecting Reference Questions on Electricity Rate Mitigation for the Board of Commissioners of Public Utilities was deferred. Ann Marie Hann Clerk of the Executive Council

From: Cowan, John
To: Osmond, Christine M
Cc: Snook, Corey
Subject: RE: NR2017[redacted]
Date: Friday, November 10, 2017 9:56:34 PM
Attachments: image001.jpg

NR officials have never discussed this issue with Nalcor. NR officials would suggest, as noted in the paper, advising the CEO and Board prior to providing to the PUB.

John

From: Osmond, Christine M
Sent: Friday, November 10, 2017 2:39 PM
To: Cowan, John <JCowan@gov.nl.ca>
Cc: Snook, Corey <coreysnook@gov.nl.ca>
Subject: RE: NR2017-[redacted]

Does Nalcor have any indication that a reference to the PUB is being considered?

Does NR recommend that Nalcor be advised of the reference question prior to providing it to the PUB?

Thanks

From: Cowan, John
Sent: Friday, November 10, 2017 2:13 PM
To: Osmond, Christine M
Subject: RE: NR2017-[redacted]

I believe it would be the current Consumer Advocate.

PUA says only…

Consumer advocate

117. (1) The Lieutenant-Governor in Council may appoint a consumer advocate under this Act upon those terms and conditions that the Lieutenant-Governor in Council may determine.

(2) Rep. by 1996 cR-10.1 s61

(3) All costs relating to the consumer advocate shall be borne by the board.

John Cowan
Assistant Deputy Minister (Energy Policy)
Department of Natural Resources

Government of Newfoundland and Labrador
St. John's, NL A1B 4J6
jcowan@gov.nl.ca
O: 709.729.1406 / M: 709.699.0269

logo-main2

From: Osmond, Christine M
Sent: Friday, November 10, 2017 2:01 PM
To: Cowan, John <JCowan@gov.nl.ca>
Subject: FW: NR2017-[redacted]

If the question below hasn't been addressed in the paper can you please provide info? (in the light of time)

Thanks

From: Osmond, Christine M
Sent: Friday, November 10, 2017 8:04 AM
To: Osmond, Christine M
Subject: NR2017[redacted]

Hi,
Can you tell me if it will be necessary for LGIC to appoint a consumer advocate should the reference question proceed? Or would the current advocate by his current appointment take on that role? Do particular directions need to be given to an appointed Consumer Advocate for this review?

Thanks
Christine

Christine Osmond
Cabinet Officer
Cabinet Secretariat, Executive Council
Government of Newfoundland and Labrador
Tel: 709.729.5215

[redacted]

[redacted]

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From: Cowan, John
Sent: Friday, November 10, 2017 2:03 PM
To: Snook, Corey
Subject: FW: NR2017-[redacted]

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From: Cowan, John
To: Osmond, Christine M
Subject: RE: NR2017-[redacted]
Date: Friday, November 10, 2017 2:12:51 PM
Attachments: image001.jpg

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From: Cowan, John
To: Osmond, Christine M
Cc: Snook, Corey
Subject: RE: NR2017[redacted]
Date: Friday, November 10, 2017 10:09:19 PM
Attachments: image001.jpg

No, it is not anticipated, however, given Nalcor activities are not normally under the purview of the PUB, there may be times where they may argue that information is commercially sensitive. In order to ensure that the PUB receives the information it needs, government may be required to use such a mechanism.

John

From: Osmond, Christine M
Sent: Friday, November 10, 2017 2:21 PM
To: Cowan, John <JCowan@gov.nl.ca>
Cc: Snook, Corey <coreysnook@gov.nl.ca>
Subject: RE: NR2017-[redacted]

In reference to recommendation 2 is it anticipated that Nalco would not cooperate with the review, or would this be standard process (i.e required in order for Nalcor to be able to participate in the process?

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[redacted]

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