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Attention: Ms. Cheryl Blunden

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November 4, 2020

Dear Ms. Blunden,

**Re: Newfoundland and Labrador Hydro
2017, 2018, and 2019 Average Rate Base**

We have completed our review as requested in your letter dated September 2, 2020 relating to Newfoundland and Labrador Hydro's ("the Company's") ("Hydro") 2021 Capital Budget Application (Section I) as it pertains to the computation of the 2017, 2018, and 2019 average rate base for which the Company requests Board of Commissioners of Public Utilities ("Board") approval.

The procedures undertaken in the course of our financial analysis do not constitute an audit of the Company's financial information and consequently, we do not express an opinion on the financial information.

Our procedures with respect to verifying the calculation of the average rate base 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, where applicable;
- agreed component data (capital expenditures; depreciation; etc.) to supporting documentation;
- checked the clerical accuracy of the continuity of the rate base for 2017, 2018, and 2019; and,
- agreed the methodology used in the calculation of the average rate base to the Public Utilities Act to ensure it is in accordance with Board Orders and established policy and procedure.

The table below summarizes the differences between the 2021 Capital Budget Application (Section I) and Hydro's 2017 to 2019 Annual Return reports:

Table 1: Comparison of 2017, 2018, and 2019 Average Rate Base

(000's)	<u>2017</u>	<u>2018</u>	<u>2019</u>
2021 Capital Budget Application ¹	\$ 2,068,754	\$ 2,265,683	\$2,306,047
Per Original Annual Return	<u>1,979,748</u>	<u>2,182,151</u>	<u>2,306,047</u>
Difference	<u>\$ 89,006</u>	<u>\$ 83,532</u>	<u>\$ -</u>

Note 1: Section I - Revision 2 filing by Hydro on November 2, 2020.

2017 Average Rate Base Calculation

We noted that the 2017 average rate base of \$2,068,754,000 presented in Table 1 differs from the original 2017 Annual Return of \$1,979,748,000 by \$89,006,000. In the 2017 annual return filing Hydro included \$65,287,000 for average deferred charges which comprised of only deferred charges approved by the Board at the time of the annual return filing. The original Section I in the 2021 Capital Budget Application also included \$65,287,000 in average deferred charges for 2017, however this was an error and the average deferred charges balance should have been \$154,293,000, which is \$89,006,000 higher than what was reported. Hydro filed Revision 2 on November 2, 2020 that corrects this error. The following table illustrates this comparison:

Table 2: Comparison of 2017 average deferred charges: 2021 Capital Budget Application Revision 2 vs. 2017 Annual Returns

(000's)	<u>2017</u>		<u>Difference</u>
	<u>Capital Budget</u>	<u>Annual Return</u>	
Deferred charges, end of current year	\$ 128,737	\$ 63,337	\$ 65,400
Deferred charges, end of prior year	<u>179,849</u>	<u>67,237</u>	<u>112,612</u>
Average Deferred Charges for Rate Base	<u>\$ 154,293</u>	<u>\$ 65,287</u>	<u>\$ 89,006</u>

The restated average deferred charges of \$154,293,000 was filed in Revision 2 on November 2, 2020 as an amended Section I that incorporates deferred charges existing in 2017 which were approved in subsequent Board orders. Specifically, the increase of \$89,006,000 pertains to the following balances included in the restated deferred charges:

- Energy Supply Cost Variance, Holyrood Conversion Rate, and the Isolated System Supply Cost Variance deferral accounts ("Supply Cost Deferrals") for 2015, 2016, and 2017 approved in Order No. P.U. 16 (2019).

- Cost Deferral Accounts for 2014, 2015, and 2016 approved in Order No. P.U. 22 (2017) pertaining to the 2017 opening deferred charges.

We have verified that the above deferred charges have been appropriately reflected in the restated 2017 average rate base included in Section I Revision 2, filed November 2, 2020.

2018 Average Rate Base Calculation

We noted that the 2018 average rate base of \$2,265,683,000 presented in the 2021 Capital Budget Application differs from the original 2018 Annual Return of \$2,182,151,000 by \$83,532,000. The balance is restated due to the following:

- Plant investment increased by \$9,264,000 compared to the originally filed balance as a result of the impact of Hydro's proposal to restate its property, plant and equipment balance using the new depreciation methodology, effective January 1, 2018 approved in Order No. P.U. 16 (2019);
- Average deferred charges increased by \$77,043,000 compared to the originally filed balance primarily due to the Supply Cost Deferrals being approved for recovery in Order No. P.U. 16 (2019); and,
- Hydro's cash working capital allowance decreased by \$2,775,000 compared to the originally filed balance primarily related to updating their net lag percentage from 3.56% to 2.60% approved in Order No. P.U. 16 (2019).

We have verified that the above changes have been appropriately reflected in the 2018 average rate base included in Section I Revision 2, filed November 2, 2020.

2019 Average Rate Base Calculation

We noted that the 2019 average rate base of \$2,306,047,000 presented in the 2021 Capital Budget Application agrees to the 2019 Annual Return.

During our review of the 2019 average rate base we noted an exception regarding the inclusion of \$2.5 million in rate base associated with expenditures in relation to the Bay d'Espoir Access Roads Refurbishment project approved in Order No. P.U. 48 (2016). In Order No. P.U. 48 (2016) the Board approved the expenditures associated with this project, however Hydro was required to record the expenditures in a separate account with the recovery to be addressed in a subsequent order of the Board following a further application by Hydro. There has been no application filed by Hydro for approval to include these expenditures in 2019 rate base. Hydro has appropriately excluded these expenditures in the 2017 and 2018 rate base.

In Section I Revision 2 footnote 3, Hydro has indicated that it obtained government approval of an easement relating to the access roads in December 2019, and as a result has

included the \$2.5 million in Hydro's 2019 rate base. We reviewed the approved easement issued by the Government of Newfoundland and Labrador for the access roads.

The table below presents the revised average rate base for 2017, 2018 and 2019, consistent with Section I Revision 2 as filed by Hydro on November 2, 2020:

Table 3: Hydro's Revised Average Rate Base

(000's)	<u>2017</u>	<u>2018</u>	<u>2019</u>
Total Capital Assets	\$ 2,035,322	\$ 2,115,009	\$ 2,152,552
<u>Deduct Items Excluded from Rate Base</u>			
Work in Process	(33,556)	(31,655)	(37,417)
Asset Retirement Obligations (net of amortization)	789	185	(67)
Net Capital Assets	<u>2,002,555</u>	<u>2,083,539</u>	<u>2,115,068</u>
Net Capital Assets, Previous Year	<u>1,699,168</u>	<u>2,002,555</u>	<u>2,083,539</u>
Unadjusted Average Capital Assets	1,850,861	2,043,047	2,099,304
<u>Deduct</u>			
Average Net Capital Assets Excluded from Rate Base	<u>(21,141)</u>	<u>(12,208)</u>	<u>(9,679)</u>
Average Capital Assets	1,829,720	2,030,839	2,089,625
Cash Working Capital Allowance	6,405	2,640	1,299
Fuel Inventory	43,617	56,041	57,611
Supplies Inventory	34,719	37,021	37,701
Average Deferred Charges	<u>154,293</u>	<u>139,142</u>	<u>119,811</u>
Average Rate Base at Year-End	<u>\$ 2,068,754</u>	<u>\$ 2,265,683</u>	<u>\$ 2,306,047</u>

We reviewed Hydro's revised average rate base as summarised in Table 3. We conclude, based on our procedures, that the 2017, 2018 and 2019 average rate base have been accurately reflected in Section I Revision 2 and are in accordance with established practice and relevant Board Orders except in relation to the 2019 average rate base regarding the Bay d'Espoir Access Roads Refurbishment project as described above.

Other Matters

Based on the results of our procedures we can also confirm the following:

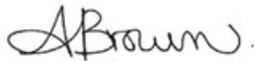
- that the Happy Valley-Goose Bay Interconnection project with a cost of \$12,528,508 was still included within Hydro's work in progress at the end of 2019, which results in this balance being excluded from the 2019 rate base calculation.
- that the loss of \$4.25 million on the sale of the Corner Brook frequency converter to Corner Brook Pulp and Paper Limited was written off from Hydro's Retirement Asset pool in 2019, which results in this balance being excluded from rate base.

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

Yours sincerely,
Grant Thornton LLP



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