

1 Q. **Reference: Chapters 5 and 6; Exhibits 14 to 17**

2 Hydro's Application proposes a number of changes to cost allocation methodologies and rate
3 design. These proposals rely upon a variety of principles, including embedded cost causation,
4 demand and energy cost classification, marginal-cost pricing, opportunity-cost pricing, and
5 customer price signals. Explain how Hydro has ensured that these proposals operate together as
6 a cohesive framework for establishing rates. In particular:

- 7 a) Describe the overarching principles Hydro applied in developing the proposed cost
8 allocation methodologies and rate design.
- 9 b) Explain how the proposed cost allocation methodologies and rate design collectively
10 achieve the objectives of fairness, cost causation, economic efficiency, and equitable
11 cost recovery.
- 12 c) Explain how Hydro reconciles the use of embedded-cost principles for cost allocation
13 with the use of marginal-cost and opportunity-cost principles in rate design.
- 14 d) Explain how Hydro determined which system costs are appropriately reflected through:
15 i) demand-related cost allocation; ii) energy-related cost allocation; iii) demand charges;
16 iv) First and Second Block Energy rates; and v) other rate components.
- 17 e) Explain how Hydro ensured that demand-related system costs reflected in marginal or
18 opportunity-cost pricing signals have been appropriately distinguished from those
19 recovered through embedded cost allocation methodologies.
- 20 f) Explain how Hydro assessed whether the proposed cost allocation methodologies and
21 rate design, when considered collectively rather than individually, produce an equitable
22 allocation of costs among customer classes. If not, explain why.
- 23 g) Confirm whether Hydro performed an overall assessment of the cumulative interaction
24 of the proposed cost allocation methodologies and rate design. If so, provide that
25 assessment. If not, explain why not.

1 h) Explain whether Hydro considered alternative integrated approaches that would have
2 resulted in a different overall balance between demand-based recovery, energy-based
3 recovery and marginal-cost pricing.

4
5
6 A. Newfoundland and Labrador Hydro (“Hydro”) generally designs rates for three groups of
7 customers in a General Rate Application, which includes Newfoundland Power Inc.
8 (“Newfoundland Power”), Island Industrial customers, and customers on the Labrador
9 Interconnected System. The rate changes for customers in the rural deficit areas are set
10 primarily based on changes to Newfoundland Power rates based on a series of Orders in Council.

11 Hydro develops cost allocation methodologies and rate design proposals in accordance with
12 established regulatory principles and the requirements of the *Public Utilities Act* and the
13 *Electrical Power Control Act, 1994*. These principles include rates that are just and reasonable,
14 the avoidance of undue discrimination, fair and equitable allocation of costs among customer
15 classes, appropriate matching of costs and cost drivers, rate stability and predictability, and
16 intergenerational equity. Cost allocation methodologies and rate design are developed and are
17 reviewed by the Board of Commissioners of Public Utilities (“Board”) through separate
18 proceedings as circumstances, system characteristics, and cost drivers evolve over time.

19 Cost allocation methodologies determine the allocation of Hydro's revenue requirement among
20 customer classes using accepted cost-of-service principles, including functionalization,
21 classification, and allocation of costs based on cost causation. Hydro's cost-of-service
22 methodologies have been considered through dedicated proceedings, including Hydro's 2018
23 Cost of Service Methodology Review,¹ and Hydro's Cost of Service Methodology Application filed
24 on August 22, 2025.² The treatment and allocation of specific system costs have therefore been
25 addressed through those proceedings rather than through rate design in isolation.

¹ Approved in Board Order No. P.U. 37(2019).

² Approved in Board Order No. P.U. 14(2026).

1 Rate design, in turn, establishes how each customer class recovers its assigned revenue
2 requirement through specific rate components. Depending on the customer class and the
3 objective being addressed, rate structures may incorporate embedded-cost principles, marginal-
4 cost considerations, opportunity-cost pricing signals, operational considerations, customer
5 understanding, and rate stability considerations. The most recent changes to the rate structure
6 for Newfoundland Power was addressed in the Application for Adjustments to the Wholesale
7 Utility Rate-Revision 1 filed with the Board on September 25, 2024³ and changes to the Island
8 Industrial rate structure are being proposed in this Application.

9 The specific rationale for individual cost allocation methodologies and rate design proposals is
10 provided in the evidence supporting those proposals and should be considered in the context of
11 the respective applications and proceedings in which they were developed and reviewed.

³ Approved in Board Order No. P.U.1(2025).