Q. **Reference: Volume 2, Exhibit 2, Attachment 1, pages 2, page 7 and page 11**

Hydro provides (lines 10 to 14 of page 2) a summary of its costing framework which includes three primary means of charging costs among the lines of business (1) Type 1- Administration Fee costs (2) Type 2 – Costs related to the provision of Corporate Services and (3) Type 3 – Cost recovery business units. Hydro states (lines 19 to 21 of page 7) "*Where an employee is expected to provide equal service to the regulated and non-regulated business, the default is a non-regulated business unit.*" Hydro states (lines 8 to 9 of page 11) "*Certain functions incur costs on a cost recovery basis. In these cases, all costs with the activity are charged in accordance with the applicable cost recovery arrangements.*"

a) Confirm (or otherwise explain) that the primary difference between Type 1 and Type 2 is that Type 1 costs are allocated by cost drivers and Type 2 costs are allocated based on timesheets.

b) Explain why the default for assignment of an employee to a home business unit is to a non-regulated business unit as opposed to a regulated business unit.

c) Elaborate on the differences in Hydro's costing framework between cost recovery business units (Type 3) and Type 1 and Type 2 business units.

A. **a)** The primary difference between Type 1 and Type 2 charges is the manner in which costs are assigned to a line of business. Type 1 costs are allocated through an administration fee using appropriate allocators (cost drivers) to distribute costs among lines of business. Type 2 costs are directly assigned to a specific activity or line of business where the work performed can be identified and are charged based on employee time recorded through timesheets.

b) Newfoundland and Labrador Hydro ("Hydro") manages and segregates the costs of its regulated and non-regulated operations to ensure that customers only bear the costs associated with providing regulated service through customer rates.

Hydro assigns home business units based on an employee's role and primary responsibilities. As outlined in Hydro's Intercompany Transactions Costing Guidelines, employees hired within corporate services departments and expected to provide services to both regulated and non-regulated operations are assigned by default to a non-regulated business unit.

This approach acts as a safeguard to ensure that any residual costs not specifically charged to a line of business remain in the non-regulated segment rather than being recovered from regulated customers. Costs attributable to regulated operations are subsequently charged to the regulated business through Hydro's established intercompany costing processes. As a result, only costs that are specifically identified and allocated to the regulated business are included in customer rates.

c) Cost recovery business units (Type 3) are used to capture costs incurred on behalf of another line of business and recover those costs directly from the benefiting line of business in accordance with established cost recovery arrangements. Unlike Type 1 costs, which are allocated using an administration fee and an appropriate allocator, and Type 2 costs, which are directly assigned based on employee time recorded through timesheets, Type 3 costs are charged directly to the benefiting line of business and recovered in full without the use of allocators. As a result, cost recovery business units do not retain costs, but rather serve as a mechanism to accumulate and recover costs incurred on behalf of other business units.