

**NEWFOUNDLAND AND LABRADOR  
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES**

**AN ORDER OF THE BOARD**

**NO. P.U. 4(2014)**

1 **IN THE MATTER OF** the *Electrical Power*  
2 *Control Act, 1994*, SNL 1994, Chapter E-5.1 (the  
3 "*EPCA*") and the *Public Utilities Act*, RSNL 1990,  
4 Chapter P-47 (the "*Act*"), as amended, and regulations  
5 thereunder; and  
6

7 **IN THE MATTER OF** an application by  
8 Newfoundland and Labrador Hydro for approval  
9 to treat costs associated with repairs to the fuel oil  
10 system at the Holyrood Thermal Generating Station  
11 as an extraordinary expense pursuant to sections  
12 69, 78 and 80 of the *Act*; and  
13

14 **IN THE MATTER OF** Order No. P.U. 41 (2013)  
15 approving the creation of a deferral account for  
16 the costs associated with the repairs to the fuel oil  
17 system and setting aside the issue of the recovery  
18 of the costs.  
19  
20

21 **The Application**

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23 Newfoundland and Labrador ("Hydro") filed an application on December 9, 2013 for approval to  
24 treat the expenses associated with the repair of the fuel oil system at the Holyrood Thermal  
25 Generating Station ("Holyrood") as a major extraordinary repair and to defer the expenses (the  
26 "Application"). The Application requests that the Board make an order approving 2013 costs of  
27 \$1,059,686 associated with repairs to the fuel oil system at Holyrood as a major extraordinary  
28 repair such that the costs of those repairs are amortized over a five-year period and that the  
29 unamortized balances are included in the rate base. A report *Holyrood Fuel Oil System -*  
30 *Operation and Maintenance Challenges in 2013* was filed as part of the Application.  
31

32 Notice of the Application was provided to: Newfoundland Power Inc. ("Newfoundland Power"),  
33 the Consumer Advocate, Corner Brook Pulp and Paper, North Atlantic Refining Limited, Teck  
34 Resources Limited, Vale Newfoundland and Labrador Limited and Praxair Canada Inc.  
35

36 The Board issued Order No. P.U. 41(2013) on December 13, 2013 approving the creation of a  
37 deferral account for Hydro's 2013 costs relating to the repairs to the fuel oil system but set aside

1 Hydro's proposals in relation to the recovery of the 2013 costs to be addressed in a subsequent  
2 Order of the Board.

3  
4 On December 16, 2013 the Board issued a schedule for the process to review the remaining  
5 issues in the Application. On January 8, 2014 requests for information were issued to Hydro by  
6 Newfoundland Power, the Consumer Advocate and the Board. A total of 42 requests for  
7 information were issued to Hydro. Written submissions were filed by the Consumer Advocate,  
8 Newfoundland Power and Corner Brook Pulp and Paper, North Atlantic Refining Limited and  
9 Teck Resources Limited on January 22, 2014. Vale Newfoundland and Labrador Limited and  
10 Praxair Canada Inc. did not file submissions. Hydro filed a reply submission on January 24,  
11 2014.

### 12 13 **Evidence and Submissions**

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15 In the Application Hydro explains that in 2013 there were a number of operational and  
16 maintenance issues with the fuel oil equipment at Holyrood as a result of the quality of fuel oil  
17 delivered in four separate shipments in January and February of 2013. The fuel oil contained  
18 high content levels of aluminum and silicon. Fuel oil stability was also an issue. Hydro explains  
19 that the fuel oil quality issues affected the main fuel oil tank suction heaters, the fuel oil day tank,  
20 the fuel oil suction strainers, the fuel oil pumps, the fuel oil heat exchangers, the fuel oil  
21 recirculation and control valves and the boiler burner nozzles. In addition Holyrood experienced  
22 two fuel oil spills in 2013 due to premature wear on the tubes on the suction heater of fuel oil  
23 tanks 1 and 2. Hydro's evidence sets out the details of the specific issues and required corrective  
24 action and repairs associated with the quality of fuel delivered in early 2013.

25  
26 Hydro estimates that the total cost of the required fuel oil equipment maintenance, replacement,  
27 inspection, repair, and cleanup was \$1,059,686. Hydro explains that:

28  
29 *"Hydro now applies to the Board that the fuel oil system repairs be treated as*  
30 *extraordinary expenses in accordance with approved policy and that the expenses be*  
31 *deferred over a period of five years as the repairs to the fuel oil system equipment do not*  
32 *result in replacement of major components, are not typical of the normal repair*  
33 *expenditures, and the costs exceed \$500,000. Further, the costs associated with the repairs*  
34 *are considerable and would constitute a significant adverse effect on Hydro's earnings*  
35 *were they to be expensed in the year in which they were incurred."* (Application,  
36 Correspondence, dated December 9, 2013, page 1)

37  
38 The Consumer Advocate does not support Hydro's proposals in relation to the recovery of the  
39 costs relating to the repairs of the fuel system and the inclusion in rate base of the unamortized  
40 balance. The Consumer Advocate submits that, while the circumstances giving rise to the need  
41 for the repairs may have been out of the ordinary, Hydro has not shown in this case that the  
42 circumstances are extraordinary as regards the effect on Hydro's regulated earnings. He points to  
43 the Board's findings in Order No. P.U. 31(2008) in which the Board declined to allow Hydro to  
44 defer a \$1.4 million expense for repairs to the Unit 2 turbine at Holyrood on the basis that Hydro  
45 had not shown that expensing these costs would cause a shock to its earnings. The Consumer  
46 Advocate also notes that, according to NP-NLH-007 and NP-NLH-008, Hydro's internal labour  
47 costs of \$241,600 associated with the repairs to the Holyrood fuel oil system were not

1 incremental to its initial 2013 operating budget since Hydro was able to defer other planned  
2 work.

3  
4 In his submission the Consumer Advocate also raises the potential of future operational and  
5 maintenance issues in the fuel oil system which may be associated with the quality of the fuel oil  
6 supplied. He notes that, according to NP-NLH-011, an agreement between Hydro and its supplier  
7 regarding the acceptable amounts of damaging constituents has not been put into place. The  
8 Consumer Advocate also submits that it is presently unclear how Hydro proposes to ensure that  
9 the fuel has acceptable levels of aluminum and silicon. The Consumer Advocate recommends  
10 that Hydro advise the Board and the parties of the steps it proposes to take to ensure that similar  
11 losses are avoided in the future.

12  
13 In its submission Newfoundland Power notes that the repairs to the fuel oil system had the effect  
14 of deferring other planned work. According to Newfoundland Power:

15  
16 *"Since work that would have otherwise been conducted within Hydro's initial 2013*  
17 *operating budget was deferred, the full costs associated with the Holyrood fuel system*  
18 *repairs cannot be considered extraordinary and incremental to Hydro's 2013 expenses.*  
19 *Had the damage to the fuel oil system not occurred, Hydro would have completed other*  
20 *planned work and would still have incurred at least some, if not all, of the operating cost*  
21 *amounts requested in the Application."*(Newfoundland Power, Written Submission,  
22 page 1)  
23

24 Newfoundland Power submits that Hydro has not established that the costs incurred to repair the  
25 fuel oil system at Holyrood are extraordinary requiring special treatment, and also submits that  
26 the Application requests deferral of costs that are less material to earnings than the 2007 costs  
27 requested and denied by the Board in Order No. P.U. 31(2008).

28  
29 Corner Brook Pulp and Paper, North Atlantic Refining Limited and Teck Resources Limited  
30 support the position taken by the Consumer Advocate in his submission, both in relation to  
31 Hydro having not demonstrated circumstances warranting deferral of the expenses and, secondly,  
32 in relation to whether Hydro has taken sufficient measures to avoid a recurrence. These  
33 customers suggest: i) implementation by Hydro of testing procedures that would allow for  
34 detection of the identified fuel oil quality issues prior to shipment; ii) Hydro entering into a  
35 written agreement with the supplier to address the identified fuel quality issues; and iii) Hydro  
36 submitting to the Board a report on the implementation of these measures and any other the  
37 Board may order.

38  
39 In its reply submission Hydro states that it is appropriate for the Board to consider the fuel oil  
40 system expense as an extraordinary repair cost as it meets the minimum threshold of \$500,000  
41 previously established by the Board and will cause a significant shock to Hydro's earnings that is  
42 considered unreasonably high for a utility that has minimal 2013 net income. Hydro states that if  
43 the fuel oil system repair costs are expensed in 2013 its earnings would be reduced by 16% and  
44 submits that its earnings are such that any single event that causes a 16% reduction constitutes a  
45 shock to its earnings which impacts its ability to earn a just and reasonable return. Hydro also  
46 submits that that work associated with the repairs to the fuel oil system was incremental to

1 planned work at Holyrood and did not replace other planned work as the deferred work will be  
2 completed in a future year.

3  
4 In relation to the suggested preventative measures for the future Hydro submits that this is  
5 outside the scope of this Application. Hydro states that the contract with its supplier is in place  
6 until at least 2014 and that any changes in the specifications would constitute a change in the  
7 tender and require a new tender. Hydro also submits that it has already put measures in place to  
8 help prevent future damages, including working with its supplier to lower concentrations of  
9 aluminum and silicon. Hydro is also considering other testing methods for fuel stability and a  
10 formal aluminum and silicon limit but notes there are no known standards for guidance. Hydro  
11 states that any required changes in the contract will be implemented in future tenders.

### 12 13 **Board Findings**

14  
15 The Board will consider giving special treatment to expenses associated with a major  
16 extraordinary repair if the costs are greater than \$500,000 and would cause a rate shock or shock  
17 in the utility's earnings that is considered unreasonably high. In Order No. P.U. 31(2008) the  
18 Board explained at page 3:

19  
20 *"The Board does not believe that it is appropriate to routinely consider each non-capital*  
21 *expense which is greater than \$500,000 as a Major Extraordinary repair to be deferred.*  
22 *Each case has to be brought to the Board for consideration based on the circumstances."*

23  
24 In that matter Hydro had applied for approval to defer estimated expenses of \$1,433,000  
25 associated with the repair of the Unit 2 turbine at Holyrood as a major extraordinary repair. In its  
26 decision the Board found that Hydro had not demonstrated that expensing the costs of the Unit 2  
27 turbine repair in that year would cause a shock to its earnings and denied the application. The  
28 Board stated at page 4:

29  
30 *"While these expenses are clearly of a non-capital nature and greater than \$500,000*  
31 *Hydro has not shown that the circumstances are extraordinary requiring special treatment.*  
32 *The Board is not satisfied that it is appropriate in the circumstances of this Application to*  
33 *defer the cost of the repairs of the Unit 2 Turbine as a Major Extraordinary Repair."*

34  
35 In Order No. P.U. 44(2006) the Board determined that work on the Unit 2 boiler tube at  
36 Holyrood should be treated as a major extraordinary repair and that the estimated costs of  
37 \$2,666,000 should be amortized over a five-year period. The Board stated at page 4:

38  
39 *"The Board is satisfied having reviewed the record that expensing the cost of these repairs*  
40 *in 2006 would have a significant negative impact on Hydro's earnings. The costs if*  
41 *expensed would almost double Hydro's forecast loss for 2006. The Board finds that, in the*  
42 *current circumstances, these costs would cause a significant shock to Hydro's earnings if*  
43 *they were to be recognized in 2006 and should be deferred over a period of time."*

44  
45 Based on the evidence filed in this Application the Board is satisfied that the expenditures  
46 associated with the Holyrood fuel system repairs are non-capital in nature and were an unplanned  
47 operating expense. In the Application Hydro states that the costs associated with the repair were

1 \$1,059,686, but in NP-NLH-006 Hydro explains that the 2013 costs associated with this deferral  
2 are \$1,036,500, noting in a footnote that the costs were adjusted for an amount inadvertently  
3 included in labor costs (see also CA-NLH-013). Hydro did not amend the amount claimed in the  
4 Application but the Board notes, in NP-NLH-001, Hydro assumes costs of \$1,036,500 to  
5 estimate that its forecast net income for 2013 would be reduced by 16% from \$6,463,000 to  
6 \$5,427,000 if the expenses are not deferred.

7  
8 Hydro confirms, in NP-NLH-008, that the repairs were unplanned but states that other planned  
9 work was deferred. Hydro does not provide an estimate of the costs of the deferred work. Hydro  
10 does not set out whether the cost of the deferred work has been reflected in the calculation of the  
11 estimated impact on its 2013 earnings. Hydro submits that the planned work that was deferred  
12 will still have to be done in a subsequent year and will be expensed at that time. The Board notes  
13 that the matter before the Board in this Application is whether the circumstances justify special  
14 treatment for the subject expenses in 2013. This determination is based on the circumstances of  
15 2013 and not future years.

16  
17 Allowing for the recovery of unanticipated expenses outside of a test year is an extraordinary  
18 measure that the Board will order only when it is satisfied that it is appropriate and necessary in  
19 the circumstances. It would appear, based on the record, that Hydro deferred work which would  
20 have reduced to some extent the impact of the unplanned expenses on Hydro's earnings in 2013.  
21 Hydro did not provide evidence showing the amount of the expenses which were deferred to  
22 another year. It is therefore not clear, based on the information provided, what impact the costs  
23 associated with the repairs to the fuel oil system would have on its income for 2013. The Board  
24 is not persuaded that the magnitude of the costs in this case is such that it would cause a shock to  
25 Hydro's earnings that is considered unreasonably high. The Board finds that Hydro has not  
26 demonstrated that the circumstances in this case are extraordinary such that the expenses should  
27 be accorded special treatment.

28  
29 As to the issues raised by the parties in relation to the measures that should be taken by Hydro to  
30 prevent similar occurrences, the Board will require Hydro to file a report with the Board no later  
31 than May 30, 2014. This report should set out the actions taken and planned for the future to  
32 ensure it is supplied with fuel of reasonable quality, specifically addressing the issues raised by  
33 the Consumer Advocate and Corner Brook Pulp and Paper, North Atlantic Refining Limited and  
34 Teck Resources Limited.

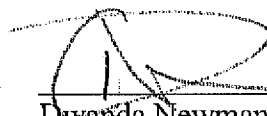
1 **IT IS THEREFORE ORDERED THAT**

- 2
- 3 1. **Hydro's proposal to treat the 2013 costs of repairs to the fuel oil system at the**
- 4 **Holyrood Thermal Generating Station as a major extraordinary repair such that**
- 5 **the costs are amortized over a five-year period with the unamortized balance to be**
- 6 **included in rate base is not approved.**
- 7
- 8 2. **Hydro shall expense the 2013 costs of the repairs to the fuel oil system at the**
- 9 **Holyrood Thermal Generating Station in 2013.**
- 10
- 11 3. **Hydro shall file a report with the Board no later than May 30, 2014 setting out the**
- 12 **actions taken and future plans in relation to the quality of fuel supplied to the**
- 13 **Holyrood Thermal Generating Station.**
- 14
- 15 4. **Hydro shall pay all expenses of the Board arising from this Application.**

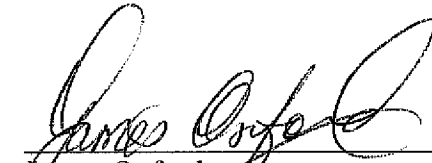
**DATED** at St. John's, Newfoundland and Labrador this 26<sup>th</sup> day of February 2014.



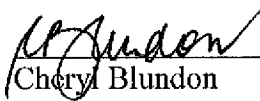
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Darlene Whalen, P.Eng.  
Vice-Chair



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Dwanda Newman, LL.B.  
Commissioner



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James Oxford  
Commissioner



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Cheryl Blundon  
Board Secretary