

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE PUBLIC UTILITIES ACT

- and -

IN THE MATTER OF AN APPLICATION by **Nova Scotia Power Incorporated** to include **Point Tupper Marine Terminal** in its rate base at a value of **\$42.13 million**

BEFORE:

Margaret A. M. Shears, Q.C., Vice-chair
John A. Morash, CA, Member
Kulvinder S. Dhillon, P.Eng., Member

COUNSEL:

NOVA SCOTIA POWER INCORPORATED
René J. Gallant, LL.B.

AVON VALLEY GREENHOUSES LTD., et al.
Robert G. Grant, Q.C.
Nancy G. Rubin, LL.B.

NEWPAGE PORT HAWKESBURY LIMITED and
BOWATER MERSEY PAPER COMPANY LIMITED
George T. H. Cooper, Q.C.
David S. MacDougall, LL.B.

PROVINCE OF NOVA SCOTIA
(Department of Energy)
Stephen T. McGrath, LL.B.

CANADIAN MANUFACTURERS & EXPORTERS
Robert G. H. Patzelt, Q.C.

QUETTA INC.
John H. Reynolds, P. Eng.

WRITTEN SUBMISSIONS: May 2, 2008

CONSULTANT'S REPORT: May 9, 2008

NSPI RESPONSE: May 16, 2008

DECISION DATE: June 30, 2008

DECISION: Request for approval of inclusion in rate base granted; valuation reduced to \$29.9 million, the Net Book Value as at March 31, 2008

INTRODUCTION

[1] This decision is in respect of an Application filed with the Board by Nova Scotia Power Incorporated (“NSPI”) dated November 2, 2007, to include the Point Tupper Marine Terminal (“PTMT”, the “terminal”), located at the site of the Point Tupper Generating Station on the Strait of Canso, in rate base. NSPI’s Application proposes that the inclusion of PTMT in rate base should be at a value of \$42,133,292. This value is based on the cost of the original project, together with carrying costs incurred since the time the terminal began operation in early 2005.

[2] Rate base can be defined as the total value of assets on which a utility is permitted to earn a regulator-approved rate of return, and includes net property, plant and equipment. As a result, the inclusion of an asset of significant value, as is the case in this instance, can have an impact on the rate-making process. The Board understands that the rate base set out in the general rate Application currently before the Board includes PTMT at the valuation proposed by NSPI and, consequently, the calculation of customer rates is based on that assumption, subject to any changes which may result from the Board’s decision on this matter.

[3] NSPI outlined its request as follows:

Nova Scotia Power Inc. (NSPI, the Company) constructed a marine terminal at the site of the Point Tupper Generating Station in 2004. The terminal was commissioned in 2005 and since that time NSPI has utilized the facility to deliver approximately 2.5 million tonnes of solid fuel to NSPI plants at Point Tupper and Trenton.

The Point Tupper Marine Terminal (PTMT) was constructed to serve the needs of NSPI and its customers. The asset was constructed outside of the Utility’s rate base recognizing the possibility that the facility could be sold to a third-party operator together with a long-term

contract to serve the needs of NSPI and its customers, similar to the arrangements with the International Pier in Sydney.

This plan was based on the possibility that ownership and operation of the terminal by a third-party might deliver the lowest cost to NSPI customers. This possibility has not been realized. NSPI has been unable to identify a purchaser for the marine terminal that will result in lower cost to NSPI customers. The lowest cost option for the provision of solid fuel delivery service is for NSPI to maintain ownership of the facility. As a result NSPI is applying to the Nova Scotia Utility and Review Board (UARB, the Board) to include this asset in the Company's rate base.

NSPI seeks to add the Point Tupper Marine Terminal to the Utility's rate base at a cost of \$42,133,292. This value is equivalent to the original cost of the marine terminal plus the cost of financing the asset since it has been placed in service and has been used exclusively to provide service to NSPI customers.

NSPI has engaged KPMG LLP (KPMG) to provide an estimate of the fair-market value of the operations comprising the solid fuel handling facility. KPMG concluded the following:

- "...we have estimated the fair market value of the Marine Terminal operations, as at the Valuation Date, to range approximately from \$40.4 million to \$44.7, with a midpoint of \$42.5 million..."

PTMT is operational and is meeting the original objectives established for the facility. It is providing a reliable long-term delivery point for NSPI import fuel, for use at the Point Tupper and Trenton stations. Importantly, the facility has also expanded the fuel sources and freight options available to NSPI.

The dollar value NSPI is applying to put into rate base (based on original cost and carrying costs) is below the facility's market value. The original cost component is below the cost to construct this asset under current market conditions. NSPI respectfully submits it is appropriate for the Board to approve for addition to NSPI's rate base, \$42,133,292, which is the cost of this investment plus carrying costs incurred since the terminal's in-service date.

(NSPI Application, November 2, 2007, pp. 1-2)

[4] In its letter accompanying the Application, NSPI also indicated that:

...it is NSPI's expectation that this asset will be depreciated according to the useful lives of the generation plants served by this facility.

(NSPI Application, November 2, 2007, p. 1)

BACKGROUND

[5] This matter was first raised with the Board in a letter dated January 8, 2004, from NSPI's then Chief Operating Officer, Chris Huskison. NSPI advised the Board that it intended to construct a new coal unloading terminal at Point Tupper, Nova Scotia.

[6] NSPI set out a number of reasons for this decision, including:

1. NSPI is convinced that it is in our customers' interests to have a new flexible coal terminal in the Strait area.
2. NSPI is convinced that, if possible as in Sydney, the ownership and operation of a coal terminal is better conducted by a third party.
3. NSPI has proceeded in good faith to have a third party develop a new coal terminal at Point Tupper.
4. NSPI's current dependence on mechanized vessels does not allow economic access to coals beyond South America and therefore limits economic access to very low and ultra low sulphur coals
5. NSPI is in the final stages of obtaining the permits necessary to build a coal terminal capable of unloading large bulk carriers at Point Tupper.

(NSPI letter, January 8, 2004, p. 1)

[7] NSPI described its intended plan with respect to the terminal construction project as follows:

The benefits of this new terminal come from three areas:

1. Reduction in the absolute cost of landing coal at Point Tupper;
2. Reduced dependence on mechanized vessels, a tight and expensive vessel market; and
3. The ability to access coals from worldwide coal basins

The value of these benefits amounts to between \$3M - \$4M per year.

Failure to have this terminal in service by April 1, 2005 will result in an annualized additional cost to customers of \$3M - \$4M.

We therefore currently find ourselves in a dilemma.

We do not have time to take this terminal through a traditional capital approval process. But without the terminal we will incur higher costs for the delivery of coal than we are currently forecasting for 2005. If we proceed with the terminal we will either need an expedited approval process or some mechanism to build the terminal without regulatory approval.

In the event this project is delayed for more than a few days, we will lose a full year due to seasonal construction issues and face higher construction costs. In other words, the first year of savings will be lost if we do not proceed right away.

Ultimately, we believe that this terminal will be able to be sold to a third party and NSPI will be able to take service from that third party.

In order to facilitate the sale and the expedited construction of the terminal we are proposing that the terminal be built by NSPI, the legal entity, outside the rate base. We would then conduct a process to divest of the terminal once the terminal is operational. Failing that process we would come to the UARB for approval to have the terminal included in rate base on a cost recovery basis. This would follow the same approach that we followed with the CBDC surface assets in Cape Breton.

We are requesting your approval for NSPI to proceed with construction of this terminal outside rate base, with the option to seek inclusion in rate base at a future time...

(NSPI letter, January 8, 2004, pp. 2-3 Emphasis added)

[8] In a response dated January 22, 2004 to NSPI's letter, the Board advised NSPI that:

...While the Board has no opinion, at this time, on whether NSPI's decision to proceed with the construction of the coal handling terminal at a projected overall capital cost of \$34 million was the correct decision, the Board has no objection to NSPI constructing the terminal outside of rate base. At such time as NSPI applies to the Board to have the terminal included as part of rate base, or applies to the Board to have the terminal sold and leased back to NSPI, the Board will determine whether or not the proposed transaction, and its related cost, is appropriate after performing its normal review procedures.

(Board letter, January 22, 2004, p. 2)

[9] While no request was made by NSPI to include the PTMT in rate base until November of 2007, costs relating to it were raised during the proceeding (P-882) on the 2006 general rate application filed by NSPI. A number of Intervenor in that proceeding objected to NSPI's proposed inclusion of \$2.3 million in PTMT capital recovery charges as part of its fuel costs. In the Board's decision on that matter, it found that these charges should not form part of the fuel costs to be recovered from ratepayers, stating that:

The Board has considered the evidence surrounding the PTMT. The main concern is related to the capital recovery charge of \$2.3 million which NSPI wishes to recover as part of its fuel costs for the 2006 test year.

Dr. Raschke was of the view that NSPI should not be permitted to include any of the \$2.3 million in its fuel costs because the PTMT is not in rate base. Ms. Hennings, on the other hand, was of the opinion that the PTMT has excess capacity, and that there should be a disallowance of a portion of the \$2.3 million cost associated with the facility, based on the "used and useful concept". She stated that

... regulatory bodies sometimes eliminate part of the investment costs from rate base if the utility has built excess capacity that is not both used and useful. The used and useful criteria could be applied to the PTMT annual cost of capital of \$2.30 million per year.

(SEB, Exhibit N-90, Evidence of Sharon K. Hennings, p. 4)

The Province expressed reservations about allowing a recovery concerning an asset which has not been approved for inclusion in rate base.

Liberty did not recommend any disallowance with respect to the \$2.3 million capital recovery. However, the Board notes that Liberty criticized the documentation associated with the solicitation and award process, finding that it contained the same type of administrative deficiencies as observed in the coal and petcoke procurement process.

To the Board's knowledge, NSPI's request for a capital recovery charge in relation to a non-rate base asset is extremely unusual and perhaps unprecedented. The **Public Utilities Act** clearly contemplates that all assets of a utility which are used and useful in supplying a regulated service shall be included in the rate base fixed by the Board with respect to that particular service. Furthermore, **s. 45** of the **Act** provides that a public utility is entitled to earn a just and reasonable return on the rate base fixed by the Board, and to recover reasonable and prudent operating expenses. There is nothing in **s. 45** or elsewhere in the **Act** which entitles a public utility to recover capital-related charges in relation to assets which it owns outside of its approved rate base. Accordingly, in the Board's view, it would be improper to allow the recovery of the \$2.3 million in fuel expense. Otherwise, a utility could hold assets outside its rate base even though those assets were being used to provide a regulated service. It could recover the capital-related charges through rates even though the Board had never approved the value of the asset for inclusion in rate base, or for depreciation purposes. Having proceeded in this fashion, the utility could then sell the asset without having to allocate to its customers any of the profits realized on the sale. This would be an intolerable situation which, in the Board's view, is simply not compatible with the intent or express provisions of the **Act**.

The Board hastens to add that it is not suggesting any improper motive on the part of NSPI. The evidence clearly indicates that NSPI built the PTMT with the intention of selling it. In the meantime, it has entered into a contract with a third party to operate the terminal and the Board is satisfied that NSPI's customers are benefitting from the arrangement. Moreover, despite the evidence of Ms. Hennings, the Board is not persuaded that the terminal was designed to have excess capacity, although this question need not be definitively addressed unless and until NSPI applies to have the PTMT included in rate base. Should NSPI make such an application, the Board is prepared to consider at that time

whether, in determining the amount to be included in rate base, an allowance should be made for deferred capital charges having regard to the fact that the terminal has, since the commencement of its operation, been devoted exclusively to the receiving and unloading of coal for NSPI's Trenton and Point Tupper generating plants.

(Board Decision, March 10, 2006, 2006 NSUARB 23, pp. 89-92)

[10] Since NSPI's current Application to include PTMT in rate base did not fit the Board's routine capital approval process, the Board, in a letter dated December 14, 2007, advised NSPI that:

...The Board has reviewed this proposal and, in view of the magnitude of the cost; the potential corresponding impact of same; and the concerns expressed by intervenors in the 2006 rate proceeding; believes that consideration of this request warrants a form of public review with an opportunity for input by interested parties prior to a determination being made by the Board.

In addition, the Board intends to retain an independent expert to review and evaluate the content and accuracy of the valuation set out in the KPMG report which was filed by NSPI in support of this request.

Please advise the Board by December 21, 2007 whether NSPI wishes to proceed on this basis.

(Board letter, December 14, 2007, p. 1)

[11] On December 21, 2007, NSPI confirmed its agreement to a public proceeding and, on January 15, 2008, the Board notified all interested parties of the PTMT Application and the public process that would be conducted. The Board subsequently engaged PricewaterhouseCoopers, LLP ("PwC") to review the valuation of PTMT prepared by NSPI's experts KPMG LLP ("KPMG") and to prepare its own valuation report on the Terminal.

[12] On March 19, 2008, the Board issued the following time line for the PTMT public process:

Notification of Intent to Participate	March 28, 2008
Information Requests from Parties	April 4, 2008
NSPI Responses to Information Requests	April 18, 2008
Written Submissions	April 25, 2008
PwC Report	May 2, 2008
NSPI Reply	May 9, 2008

[13] Following an agreed-upon request by the parties for an extension of same on April 10, 2008, the subsequent filing dates were extended by one week.

[14] While the Nova Scotia Department of Energy (“DOE”); NewPage Port Hawkesbury Limited and Bowater Mersey Paper Company Limited (“NPB”); Canadian Manufacturers and Exporters, Nova Scotia Division (“CME”); Avon Valley Greenhouses Ltd., *et al.* (“Avon”); and John Reynolds, Quetta Inc. (“Quetta”) all gave notice of their intent to participate, only three of the participants—Avon, NPB, DOE—issued Information Requests (IRs) and filed written submissions.

NSPI APPLICATION

[15] In its Application, NSPI outlined its reasons and justification for inclusion of PTMT in rate base, including a fair market value¹ (“FMV”) assessment of the terminal by KPMG, its valuation consultant. NSPI’s underlying justification for including PTMT in rate base is that ratepayers have been receiving the full benefit of NSPI’s use of the facility

¹FMV is defined by KPMG as “...the highest price available in an open and unrestricted market between informed prudent parties acting at arm’s length and under no compulsion to act, expressed in terms of money or money’s worth.” (NSPI Application, November 2, 2007, Appendix I, KPMG Valuation Report, p. 2)

since it began operating in 2005, while "...NSPI's shareholders have borne the full cost of financing the asset, without recovery from customers...."²

[16] NSPI identified a number of factors which support the need for the construction of PTMT, which can be summarized as follows:

- Closure of Devco resulting in the need to import coal to generate electricity;
- Importation by vessel is the least cost alternative;
- Point Tupper and Trenton generating stations are best served by a terminal at the Strait of Canso;
- Unlike the International Pier in Sydney, PTMT can accommodate bunkers and belted self-unloaders;
- Two supply points provide more coal supply security than one;
- PTMT facilities allow worldwide solicitation and increased competitive pricing which provides NSPI with lower cost coal supply alternatives.³

[17] NSPI also argued that, as PTMT's sole use since opening has been to supply coal to two generating stations which are integral to the provision of electricity to ratepayers, the financing costs and other costs related to PTMT over that period of time, in addition to the original construction cost of the project, should also be recoverable. NSPI stated that:

With this Application, NSPI is seeking to add PTMT to its rate base and recover these costs. It is proposed this be achieved through the capitalization of the financing costs associated with the amount approved by the Board for inclusion in rate base. Annual Allowance For

²NSPI Application, November 2, 2007, p. 4

³NSPI Application, November 2, 2007, p. 3-11

Funds Used During Construction (AFUDC) and start-up capital from 2005 to 2007 is summarized below:

	2005	2006	2007
Opening Balance	34,812,400	3 6,273,939	39,238,500
Current Period Spend	537,478	191,055	64,645
Carrying Cost	924,061	2,773,506	2,830,147
Closing Balance December 31st	36,273,939	3 9,238,500	42,133,292

...

For the purposes of this application there is a distinction between construction cost and financing cost. The construction cost is the cost incurred by NSPI to place the asset in-service. As noted in the KPMG valuation, NSPI estimates that were this project to be undertaken today, the cost incurred for inclusion in rate base would exceed \$39 million, excluding AFUDC.

The additional carrying cost, is a cost currently borne by NSPI shareholders to provide fuel delivery service to NSPI's customers.

Both the construction cost and the carrying costs are real costs and should be fully recovered from NSPI customers through inclusion of these costs in NSPI's rate base.

(NSPI Application, November 2, 2007, pp. 13-15)

[18] As set out above, the KPMG report estimated the FMV of PTMT as of August 31, 2007 "...to range approximately from \$40.4 million to \$44.7 million, with a mid-point of \$42.5 million..."⁴

SUBMISSIONS OF PARTICIPANTS

[19] As noted earlier, written submissions were filed by three participants—DOE, Avon and NPB. A summary of their main points of contention is set out below:

⁴NSPI Application, November 2, 2007, Appendix 1, KPMG Valuation Report, p. 1

[20] In its submission, Avon raised the concerns expressed by one of its experts, Dr. Manfred Raschke, of International Strategic Information Services (“ISIS”), on the need for and cost of PTMT, setting out comments made by him in previous proceedings before the Board.

[21] The basic position of Avon is that PTMT should not be included in rate base as it is not used and useful, and that “...the expenditure was extravagant; the capital costs are economically unjustified.”⁵

[22] Avon cited previous Nova Scotia Court of Appeal decisions in support of its position, and forwarded an analysis of PTMT prepared by its consultants, ISIS, which provided a review of the utilization of the terminal by NSPI and determined that it was far lower than that which the original design of the terminal was intended to accommodate. ISIS also concluded that:

After an analysis of the investment decisions, alternatives considered, and operations of PTMT, ISIS has concluded that the terminal should not be included in the NSPI rate base. NSPI proceeded to build the facility even though the experienced terminal operator it had selected as its partner to own and operate, Logistec, withdrew from the partnership. As NSPI informed the UARB on January 8, 2004, “The capital costs and construction risks were more than they felt comfortable with.”

(Avon Written Submission, May 2, 2008, ISIS Review, p. 3)

[23] DOE did not take a formal position on the Application but did raise the issue as to whether NSPI’s move from the Martin Marietta Terminal to the PTMT was necessary and took issue with NSPI’s position that expanded supply sources for coal and more competitive pricing from regular suppliers would occur as a result of PTMT’s capacity.

⁵Avon Written Submission, May 2, 2008, p. 2

DOE pointed out that the argument made by NSPI—that PTMT’s ability to accommodate large bulkers and self-unloading vessels (which was not possible at either the Martin Marietta facility or the International Pier in Sydney) would result in a substantial benefit—has not yet been realized.

[24] DOE noted that since the construction of PTMT never received formal approval by the Board, the decision to construct was at the risk of the shareholders. DOE also raised questions regarding the estimated useful life of the Point Tupper and Trenton generating stations and possible changes to environmental regulatory standards.

[25] NPB raised similar concerns to those expressed by Avon and DOE regarding the proposed inclusion of PTMT in rate base and suggested that NSPI’s Application should be denied as, in its view, NSPI had not clearly demonstrated that PTMT provided the lowest cost option for the supply and transportation of coal supply to the two generating stations.

[26] NPB also stated that NSPI was not aggressive enough in its attempts to sell, or develop secondary business for PTMT, and suggested that:

Therefore, NPB submits that the Board should not consider the approval of NSPI’s request for the addition of PTMT to rate base at this time. Rather, NSPI should be required to undertake a more comprehensive effort to transfer the ownership and operation of the PTMT facility to a third party, the outcome that NSPI was “convinced” would be preferable, and/or seek to develop secondary business for the facility to reduce the costs sought to be borne by ratepayers.

(NPB Written Submission, May 2, 2008, p. 4)

[27] NPB submitted that the burden of proof is on NSPI to “...demonstrate that the costs associated with the construction and operation of PTMT are fair, reasonable and

justifiable before such costs are added to rate base and recovered from ratepayers... NPB submits that NSPI's current application does not provide adequate information to discharge this burden."⁶

PWC REPORT

[28] PwC reviewed KPMG's valuation of PTMT and filed two reports dated May 9, 2008, with the Board—a limited critique of the KPMG estimate of value of PTMT as at August 31, 2007—and an estimate of value of the asset as at January 31, 2008. PwC concluded that the appropriate FMV of PTMT was slightly lower than that identified by KPMG, stating that: "...we estimate the FMV of PTMT at the Valuation Date to be in the range of \$35.5 million to \$43.4 million. The midpoint of our range is \$39.5 million."⁷

[29] PwC also commented on NSPI's proposal to include carrying costs:

56. NSPI has applied to transfer an amount of \$42,133,292 into rate base. This includes a recovery of the financing costs borne by NSPI since construction. This is comprised of the following:

Opening Balance (Aug 2005) – Funds Used During Construction	34,812,400
Capital Start-Up Costs (2005 to 2007)	793,178
Carrying Costs (2005 to 2007)	<u>6,527,714</u>
	<u>42,133,292</u>

57. If the Board approves the Application, there are a number of alternative amounts at which PTMT may be transferred, including the following:

⁶NPB Written Submission, May 2, 2008, p. 6

⁷PwC Report, Estimate of Value, May 9, 2008, p. 2

	\$
Original Cost	35,605,580
Replacement Cost	36,291,000*
Cost plus carrying charges	42,133,292
KPMG's Estimate of Value	42,546,000
PwC's Estimate of Value	39,506,000

**Replacement cost is based on NSPI's estimate of current replacement cost (\$39,194,000) less depreciation since inception*

. . .

59. In our view, if the Board's decision regarding an appropriate value at which to transfer PTMT into rate base is predicated solely on the concept of fair market value at a current date, then it would not be appropriate to include any additional amount in respect of carrying costs. The KPMG and PwC Reports are based on fair market value at their respective valuation dates.

(PwC Report - Limited Critique of KPMG Estimate - May 9, 2008, p. 11)

[30] PwC also pointed out that the Net Book Value⁸ ("NBV") of PTMT is lower than the estimated market value:

The net book value of PTMT as at March 31, 2008 (subsequent to valuation date), is \$29,939,656, as provided by NSPI ...

(PwC Report, Estimate of Value, May 9, 2008, p. 16)

NSPI RESPONSE

[31] NSPI took issue with the views expressed by Avon and NPB that the Application to incorporate PTMT in rate base should be denied. It pointed out that while

⁸NBV of a capital asset is generally considered to be the original cost, less amortization and depreciation

NPB also indicated that such a request could be deferred and reconsidered in the future, it provided no suggested value with respect to the asset.

[32] With regard to DOE's comments, NSPI noted that although a number of issues were raised, DOE stated that it "...took no position..." on the Application.⁹ NSPI also disputed DOE's suggestion that its coal terminal requirements could be met by continuing to use the Martin Marietta Terminal, stating that since its primary use was to export aggregate, the use of the facility for coal importation and delivery could be relegated to an unacceptable lower priority.

[33] NSPI also argued that despite the concern raised by DOE (along with others)—that PTMT has not been fully utilized in the manner in which it was originally intended (e.g., coal importation from non-traditional suppliers)—the fact that PTMT offers a continued ability to do so constitutes a significant benefit for customers.

[34] NSPI submitted that the position of Avon and NPB—that PTMT is not a used and useful asset which provides a benefit to customers—is incorrect, stating that:

The submissions of Avon and NPB are premised on the mistaken assumption that PTMT was constructed to be sold or transferred to a third party, or to obtain benefits related to a usage that is secondary to PTMT's primary purpose – the delivery of international solid fuel to NSPI's generating stations. Avon declares this incorrect assumption in paragraph 2 of its submission. NPB uses selected excerpts from the background documentation to suggest that an "underlying premise" of PTMT – that it would obtain secondary market value – has "never come to fruition".

Contrary to the statements and implications of the LIC [Large Industrial Customers], PTMT was constructed to serve the requirements of NSPI and its customers. NSPI has made this point on numerous occasions. The Company has expressed the desire and possibility that third party ownership or operation may result in a lower cost for NSPI's customers.

The LIC and their consultants criticized the terminal's construction in a variety of ways. Certain of these criticisms are in conflict with each other. For example, Avon suggests the

⁹DOE Submission, May 2, 2008, p. 1

terminal dock is too small, while NPB suggests the terminal is too large. These criticisms ignore that PTMT was built precisely for the requirements of NSPI and its customers, as anticipated at the time of construction, over the long term.

It was anticipated at the time of construction that third party ownership or secondary market value would require additional capital investment. It was also an important criteria of any sale that NSPI would have a long term commitment to low cost access to the PTMT facility to serve the needs of NSPI customers. The Company has concluded, following reasonable efforts to identify a purchaser, that the lowest cost option for the provision of solid fuel delivery service is for NSPI to maintain ownership of the facility in rate base.

NSPI's correspondence of January 8, 2004 to the Board advises that if the terminal could not be divested, NSPI would apply to the Board to have it included in rate base on a cost recovery basis. The Board accepted this approach to the construction of PTMT reserving the right to establish the valuation for inclusion into rate base at the time of NSPI's application. This approach was reinforced by the Board in its Decision in the 2006 general rate application. The Company now makes such a request.

(NSPI's Response, May 16, 2008, pp. 3-4)

[35] With respect to the issue of carrying costs, NSPI indicated that:

NPB argues that the carrying costs included in the application are not appropriate for inclusion in rate base. This fails to consider recent Board decisions. In the 2006 Rate Decision, the Board provided: "At a future date, NSPI may apply to have the PTMT included in rate base. Should NSPI make such an application the Board is prepared to consider at that time whether an allowance should be made for deferred capital charges." Further, the costs associated with the retirement of the Glace Bay Generating Station, including annual carrying costs on the unamortized balance, were approved by the Board for recovery from NSPI customers. Consistent with this application for PTMT, the unamortized balance plus carrying costs were included in the Company's rate base.

There is no regulatory prohibition on incorporating carrying costs in the valuation of a rate base asset. To the contrary, there is recent regulatory precedent in Nova Scotia for such treatment, and these same intervenors agree that the Fuel Adjustment Mechanism should include carrying costs in respect of the deferred recovery or refund of fuel costs.

(NSPI Response, May 16, 2008, pp. 5-6)

[36] Lastly, NSPI pointed to the similarity between the FMV estimates of PTMT provided by KPMG and PwC which, in its view, support its request for the inclusion of PTMT in rate base at a value of \$42,133,292.

FINDINGS

[37] The Board has carefully considered the submissions of the parties and the comprehensive material before it on this issue.

[38] While the Board believes that this information and the corresponding public process was necessary in order to arrive at a fully informed determination on this matter, the reasons for its decision which are set out below are based on fundamental regulatory rate-making principles and public interest considerations. These include the requirements established pursuant to s. 30(1) and (2) of the *Public Utilities Act* (“*PUA*”), which read as follows:

Power to determine value of property of utility

30 (1) The Board may at any time, with the assistance of such engineers, accountants, valuers, counsel and others as it deems wise or advisable to employ, inquire into and determine the extent, condition and value of the whole or any portion of the property and assets of any public utility **used and useful** in furnishing, rendering or supplying a particular service to or for the public, as of a date to be fixed by the Board. [Emphasis added]

(2) The Board shall determine the value of such property and assets on the basis of the prudent original cost thereof or by such other method as the Board may from time to time prescribe, deducting therefrom the amount of the accrued depreciation of such property and assets as determined by the Board.

[39] In addition, it is clear from long-established principles of public utility regulation that the Board must be satisfied that costs to be borne by ratepayers as a result of capital expenditures by a utility (or, in this case, the transfer of an asset to a utility) are prudent, fair and justifiable and provide a necessary service to ratepayers at the lowest reasonable cost.

[40] Based on this premise, there are two questions to be addressed in this case—does the inclusion of PTMT in rate base meet the criteria set out above and, if so, at what value?

[41] The Board finds that it is appropriate to include PTMT in rate base. In coming to this conclusion, the Board wishes to make it very clear that it in no way considers its January 22, 2004 letter to NSPI regarding its plan to construct the PTMT as a ‘precedent’ for this approval, despite the apparent reference to that assumption in NSPI’s May 16, 2008 written response, as noted earlier in this decision. In the Board’s view, no acceptance or approval for the construction of PTMT by NSPI as an unregulated asset was given by the Board, either explicitly or implicitly, in its letter of January 22, 2004. The Board had no authority to approve actions undertaken by the unregulated component of NSPI. It indicated it did not “oppose” the project, but that can hardly be viewed as a future endorsement of same. The Board’s letter, a larger excerpt of which is set out earlier in this decision, clearly indicates that it would review “...the transaction, and its related cost...”¹⁰ should a future application be made. In the Board’s view, its letter sets a higher standard for approval than the “...valuation for inclusion...”¹¹ process which NSPI has described.

[42] Instead, the Board’s finding that it is appropriate to include PTMT in rate base is based on the fact that the Board is satisfied that PTMT is a used and useful asset. The Board agrees with NSPI that the provision of a second terminal for unloading solid fuel

¹⁰Board letter, January 22, 2004, p. 2

¹¹NSPI response, May 16, 2008, p. 4

supply destined for the Point Tupper and Trenton generating plants constitutes a reasonable and justifiable addition to NSPI's assets. In view of NSPI's reliance on coal and the importance of the long-term, uninterrupted operation of these two generating facilities, the ability to have a secure terminal in proximity to these two stations, is a significant benefit to ratepayers. While the Board acknowledges the possible impact of current and future environmental regulatory standards on coal-burning plants, the practical reality is that coal will continue to fuel these generators for the foreseeable future, as the costs and time to replace them with other reliable energy sources will be both significant and lengthy.

[43] The Board understands the argument of participants that PTMT has not been fully utilized, either with respect to its ability to handle large volumes of coal, or its ability to accommodate bulkers. They take the position that, as a result of this under-utilization, PTMT's capacity and costs exceed any benefit which could be derived from it, since much of NSPI's coal continues to come from traditional sources in smaller, self-unloading vessels.

[44] However, the Board is of the view that, while it is correct that these attributes have not yet been fully utilized, this does not eliminate the potential benefit they bring to ratepayers. Both the higher volume storage capability, and PTMT's ability to accommodate bulkers and self-unloading vessels, provide NSPI, and consequently its customers, with leverage to seek out the lowest-cost coal in a global marketplace, and motivate traditional suppliers to compete more aggressively for NSPI's business. Both of these factors are important advantages NSPI would not otherwise have. As recent events have made clear,

the only 'certainty' in what will happen to fuel costs in the future is that there is no 'certainty'. Consequently, it cannot be fairly said that the supply options available as a result of the design of PTMT do not result in a benefit to customers.

[45] It is in this context that the Board finds that PTMT can appropriately be included in rate base as it is satisfied that PTMT does provide a benefit to ratepayers. Does that benefit justify the inclusion of the total original project cost and carrying costs since 2005—the \$42.13 million valuation proposed by NSPI? In the Board's view, the answer to that question is clearly 'no'.

[46] With regard to the valuation of PTMT, it is important to understand that a determination on this issue cannot be addressed solely from the perspective of accounting principles and expert valuation reports. NSPI is not a private retailer purchasing an asset in a competitive environment. It is a regulated utility which is subject to the regulatory and public interest considerations outlined earlier in this decision. In this regard, the Board believes it is important to review the decision made by NSPI in 2004 to undertake the construction of PTMT, outside of rate base, after efforts to find a third party to construct and operate it had failed.

[47] In the Board's view, the decision of NSPI to undertake this project can fairly be described as one which was a 'business venture' outside the ordinary scope of its business as a public utility. NSPI constructed a marine terminal for resale, built on a scale that could accommodate NSPI's fuel supply importation needs in addition to providing other possible business opportunities for a new owner, all without the approval of the Board

that would be required under s. 35A of the *PUA* for a capital expenditure of this magnitude by a public utility.

[48] The Board's clear understanding at that time was that it was NSPI's intention, not just a 'possible outcome' or 'option'¹², to build the terminal and sell it to a third party who would then operate it and enter into a contract with NSPI to provide for its continued use of the facility. In the Board's view, NSPI must have believed it could realize a profit on the sale of PTMT, as it is unlikely that any reasonable person would construct and sell a multi-million dollar facility on any other basis. That plan, as has been pointed out, was unsuccessful. NSPI issued a Request for Proposals in mid-2004 seeking possible buyers but no sale occurred. As a result, NSPI continues to own PTMT as an unregulated asset. It has entered into an agreement with an unaffiliated third party to operate the terminal and, at present, NSPI is the sole user of the facility.

[49] As set out above, NSPI's decision to construct PTMT was a business venture. As is the norm with business ventures, shareholders bear the risk when making such decisions. There was no guaranteed fall-back position that if the project did not work out as planned, ratepayers would assume all of the costs associated with the risk taken by shareholders. The Board made it clear in its January 22, 2004 letter that the appropriateness of including PTMT in rate base in future would only be considered if and when an application was made.

¹²NSPI Application, November 2, 2007, pp. 1-3

[50] As noted earlier in this decision, NSPI, in large part, has justified its valuation of PTMT on the basis that the original project cost, and carrying costs, have been borne by shareholders since the terminal began operation in 2005. NSPI believes that since the ratepayers have benefited from this arrangement, all of the costs which have been borne by shareholders should now be included in rate base.

[51] The Board disagrees. It is not in keeping with long-established regulatory principles, or common sense for that matter, that ratepayers should 'pick up the tab' when a business venture undertaken by shareholders does not work out as originally intended. In the Board's view, this logic is clearly demonstrable by considering what would have occurred if the asset had been sold at a profit. Shareholders would have realized a financial benefit from the profitable sale of an unregulated asset owned by NSPI. None of these profits would have been shared with ratepayers as the shareholders would have had no responsibility to do so. If ratepayers are not entitled to a share of the profits from the sale of an asset, they should have no responsibility or obligation to bear the risk that the asset may not be sold, or to compensate shareholders for costs or losses which may have been incurred. As a result, the Board can see no justification in retroactively burdening ratepayers with inclusion of the 2005 original cost to construct PTMT, along with the corresponding carrying charges since then—totalling \$42.13 million—in rate base.

[52] With respect to the issue of carrying costs, NSPI indicated in its response that it considers the Board's approved treatment of carrying costs related to the retirement of the Glace Bay generating station as a precedent for its request in this Application. NSPI

also notes the reference to PTMT costs in the Board's 2006 rate decision (set out earlier herein), as well as the agreement on the part of Avon, DOE and NPB with respect to carrying charges being included in the deferred recovery or refund of fuel costs under the Fuel Adjustment Mechanism ("FAM").

[53] In the Board's view, none of these examples support the inclusion of carrying costs in rate base in this case. The Glace Bay facility was a utility-owned asset, the costs of which fell under the Board's regulatory jurisdiction. The Board's findings in its decision on NSPI's 2006 rate application simply deferred the question as to whether costs relating to PTMT should be borne by ratepayers until an application was made to include it in rate base. As well, the Board does not agree with the suggestion made by NSPI that the issue of carrying charges in this application is similar to that in the FAM Agreement.

[54] The Board also finds that the inclusion of PTMT in rate base at FMV is inappropriate. In the Board's view, a distinction should be drawn between the valuation of an asset when transferred into rate base, as has been requested in this case, and the valuation of an asset when sold to an outside party. FMV, as determined by both KPMG and PwC, is based on the highest price available in an open and unrestricted market between informed, prudent parties acting at arm's length.

[55] If the Board were to approve the inclusion of PTMT in rate base at the FMV which has been determined by the valuation experts, the ratepayers would, in effect, be assuming the role of a purchaser. Such a description does not accurately reflect the circumstances at hand, and to categorize ratepayers in this manner would result in an

unjustifiably high addition to rate base and, consequently, increased rates to customers.

The Board believes that this would be neither fair to ratepayers nor in the public interest.

[56] Given the Board's findings with respect to the FMV, and its decision not to accept the original project cost plus carrying costs, the Board has determined that the most appropriate value to include in rate base, after carefully weighing the public interest and regulatory considerations which apply to these circumstances, is the NBV of PTMT as at March 31, 2008, which is \$29,939,656.

[57] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 30th day of June, 2008.

Margaret A. M. Shears

John A. Morash

Kulvinder S. Dhillon