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1 **Request IR-24:**

2  
3 **NSPML will accumulate AFUDC while the ML project is being constructed. In the event**  
4 **that the ML is completed on time, but MF or LIL is not completed on schedule, and hence**  
5 **power does not begin to flow until a date beyond the current schedule, will AFUDC for the**  
6 **ML project continue to accumulate until power actually begins to flow? Will Nova Scotia**  
7 **ratepayers be responsible through rates for this additional AFUDC? Under what scenarios**  
8 **will Nova Scotia ratepayers not be responsible for such additional AFUDC?**

9  
10 **Response IR-24:**

11  
12 NSPML and Nalcor are working together to align their construction schedules to minimize the  
13 difference in completion time between when the Maritime Link and the LCP Phase I projects are  
14 completed in such a manner as to minimize the accrual of AFUDC to the extent possible. Nalcor  
15 anticipates that the LTA and LIL will be completed prior to Muskrat Falls generating station.  
16 The NS Block starts no later than the commissioning of the third hydro unit at Muskrat Falls and  
17 can begin sooner. Therefore, the risk of significant delay between the Maritime Link and the  
18 LCP Phase I projects is not expected to be significant. NSPML expects that AFUDC would  
19 accrue on this capital project during its period of construction as has been the practice with  
20 capital projects at NS Power.

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1 **Request IR-25:**

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3 **The application, and the answer to MPA IR-4, both state that the expected annual average**  
4 **output of the MF project is 4.93 TWh. Based on the historical performance of the Churchill**  
5 **Falls facility, and the planned design of the MF, please provide the expected maximum and**  
6 **minimum expected annual outputs for the MF project, with a statistical confidence of at**  
7 **least 95% if possible?**

8

9 **Response IR-25:**

10

11 NSPML does not have the requested information as it is confidentially held by Nalcor. However,  
12 the commercial arrangement between NSPML and Nalcor makes the delivery of the NS Block  
13 independent of the variability of the output of the MF Project making such information  
14 unnecessary for the purposes of this proceeding.

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1 **Request IR-26:**

2

3 **In the event that the ML, LIL or MF projects experience an extended forced outage such**  
4 **that Nova Scotia will not have access to the Nova Scotia block and other power from Nalcor**  
5 **for a period of months, what arrangements will be in place, after the retirement of the coal**  
6 **plants in Nova Scotia, to ensure sufficient capacity and energy for peak loads?**

7

8 Response IR-26:

9

10 In all cases, NS Power must maintain a planning reserve margin to meet the NPCC requirements  
11 to manage the expectation of loss of firm load to less than one day in ten years. Planning reserve  
12 is additional firm generating capacity over the forecasted annual peak firm demand. Given that  
13 the NS Block is within the scale of the thermal generating units on the system today  
14 (approximately 150 MW), the loss of this Block for an extended period of time would look  
15 similar to the loss or shutdown of a thermal unit. NS Power manages these events today, and will  
16 also in the future, through the maintenance of its planning reserve margin.

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1 **Request IR-27:**

2

3 **In response to MPA IR-7, the applicant referred to the potential for repairs to be required**  
4 **as a result of “factors that are not insurable”. Please provide examples of such factors,**  
5 **based on the current market for insurance of major undersea cable projects.**

6

7 Response IR-27:

8

9 Typical major exclusions from physical damage coverage policies include, by way of example,  
10 loss or damage due to wear and tear, gradual deterioration, rust or corrosion, war and terrorism,  
11 infidelity of the insured, etc.

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1 **Request IR-28:**

2

3 **After the closing of coal plants in Nova Scotia in accordance with current resource plans,**  
4 **could Nova Scotia accept and consume the full amount of power transmitted across the**  
5 **ML, assuming attractive pricing? Would any upgrades or changes to the Nova Scotia**  
6 **power system be required to safely consume the full potential 500 MW of power transiting**  
7 **the ML? What are the expected costs of such upgrades?**

8

9 **Response IR-28:**

10

11 To consume the full 500 MW of energy in Nova Scotia upgrades would be expected to the power  
12 system. Currently, the Nova Scotia system can manage a loss of source of 300 MW; this  
13 represents the simultaneous loss of two units at Lingan. Please refer to NSDOE IR-8 and  
14 McMaster IR-25.

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1 **Request IR-29:**

2

3 **Please confirm that the Fair Market Value of the ML assets to be transferred to Nalcor**  
4 **after 35 years of operation will be greater than the \$1 transfer price. Please provide your**  
5 **estimate of the expected Fair Market Value of the assets at that time, including the**  
6 **method(s) of calculation of that value, and reasonable high and low estimates for the range**  
7 **of potential values.**

8

9 **Response IR-29:**

10

11 The transfer price between the two arm's length parties (NSPML and Nalcor) is \$1 as outlined in  
12 Article 7.1(a) of the Joint Operations Agreement (Appendix 2.10 of the Application and as such  
13 is considered to be the FMV as agreed upon by the parties). This price is the result of and part of  
14 the full commercial negotiation between NSPML and Nalcor.

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1 **Request IR-30:**

2

3 **Please describe any tax consequences that are expected to be incurred by NSPML, and**  
4 **Nova Scotia ratepayers upon the transfer of the ML assets to NALCOR after 35 years of**  
5 **operation, given the transfer price of \$1, the UCC at that time, and expected FMV of the**  
6 **assets at that time.**

7

8 **Response IR-30:**

9

10 The \$1 transfer price was agreed to between NSPML and Nalcor, separate entities operating at  
11 arms length. For tax purposes, when the transfer is made, the proceeds are deemed to equal the  
12 lesser of cost and FMV. The arm's length parties have determined that FMV at that time is equal  
13 to \$1. This will result in a terminal loss which can be used to offset taxable income in that year  
14 and any excess can be carried back to reduce taxes previously paid. To be conservative for  
15 modeling purposes, the Financial Model did not reflect the value of such prior year recovery of  
16 income taxes. Any such tax benefit will be fully passed through to NS customers.

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1 **Request IR-31:**

2  
3 **(a) Can the transaction between NSPML and Nalcor be considered to be a capital**  
4 **lease? NSPML is building the ML, the sole customer is Nalcor, Nalcor is paying for**  
5 **use of the asset through in-kind payments of energy annually for 35 years, and at**  
6 **the conclusion is receiving the asset for \$1, which will be less than Fair Market**  
7 **Value at the time.**

8  
9 **(b) If the transaction is deemed by the Canada Revenue Agency to be a capital lease,**  
10 **what tax consequences would result (based on existing tax laws, regulations and**  
11 **rules)?**

12  
13 **(c) How would these affect Nova Scotia ratepayers?**

14  
15 **(d) Does NSPML have any tax advice on the nature of the transaction with Nalcor from**  
16 **a tax perspective? If so, please provide that advice, confidentially if necessary.**

17  
18 **Response IR-31:**

19  
20 **(a) Based upon its review of the commercial contracts, it is NSPML's view that this**  
21 **transaction will not be treated as a capital lease for accounting purposes. Please refer to**  
22 **Attachment 1 for further explanation.**

23  
24 **(b) NSPML's view is that this transaction would not be treated as a lease by CRA since this**  
25 **commercial agreement is not a lease. CRA takes a legal view when assessing leases – if a**  
26 **commercial arrangement is a lease from a legal perspective, then it is a lease for tax**  
27 **purposes. If a commercial arrangement is not a lease from a legal perspective, then it is**  
28 **not treated as a lease for income tax purposes – even if it is accounted for as a lease.**  
29 **NSPML's view is that CRA will accept the bona fide legal relationship of the commercial**  
30 **agreement.**

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Maritime Link Project (NSUARB ML-2013-01)  
NSPML Responses to Morrison Park Advisors Information Requests

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- 1 (c) Not applicable based upon responses to (a) and (b).
- 2
- 3 (d) Please refer to response to NSUARB IR-175.

Emera Inc.  
 1223 Lower Water Street  
 Halifax, NS  
 B3J 3S8




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## MEMORANDUM

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Date: February 18, 2013

To: FILE

From: Holly Bernard, CA – Emera Senior Manager Accounting Policy

CC: David Bezanson, CA – Emera Corporate Controller

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Subject: **Lease Analysis**

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In accordance with the term sheet dated November 2010 and subsequently formalized in the Maritime Link – Joint Development Agreement, the Energy and Capacity Agreement and related agreements, NSPML is responsible for the costs of constructing the Maritime Link in exchange for the “Nova Scotia Block”. This energy will be generated by Nalcor Energy’s Muskrat Falls hydro-generation facility in Labrador and delivered to NSPML via the Maritime Link. The remaining capacity on the Maritime Link will be utilized by Nalcor for exporting its surplus energy.

The following analysis is from the perspective of NSPML and addresses whether the arrangement results in a lease under US GAAP. The issue is whether NSPML (as lessor) is deemed to be leasing the Maritime Link to Nalcor (as lessee) in exchange for the receipt of power (the Nova Scotia Block) for a specified period of time.

### **Determining whether an arrangement is a lease**

**840-10-15-3** *The evaluation of whether an arrangement contains a lease within the scope of the Leases Topic shall be based on the substance of the arrangement using the following guidance. That evaluation shall be made at inception of the arrangement based on all of the facts and circumstances.*

Although the Maritime Link is not structured as a lease arrangement, it is required to be assessed under US GAAP to determine if in substance, the arrangement is a lease.

**840-10-15-4** *This Topic does not address whether an undivided interest or a pro rata portion of property, plant, or equipment could be the subject of a lease. The issue of how to determine if a component part of property, plant, or equipment is itself property, plant, or equipment is not a subject of this Topic. Nevertheless, arrangements that identify a physically distinguishable portion of property, plant, or equipment are within the scope of this Topic.*

Based on the fact that NSPML will receive the benefit of 170MW of the total 500MW capacity of the Maritime Link and the remaining capacity will be used by Nalcor there is a view that Nalcor could be leasing its portion of the Maritime Link. The above standard states that an undivided interest is not subject to lease accounting and therefore if we conclude that the Maritime Link cannot be sub-divided into a Nalcor fixed asset and a NSPML fixed asset, the arrangement would be scoped out from the point of view of Nalcor leasing the portion of the PPE that relates to their use.

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The definition of an “undivided interest” is “an ownership arrangement in which two or more parties jointly own property and title is held individually to the extent of each party’s interest”. Nalcor does not jointly own the Maritime Link as legal title is entirely with NSPML. The arrangement between NSPML and Nalcor does not result in Nalcor incurring a proportionate amount of the expenses or revenues as would be common in a typical joint ownership arrangement, but rather NSPML will be responsible for the construction and operating costs and Nalcor will provide the Nova Scotia Block. As a result, we conclude that the Maritime Link cannot be divided for these purposes and therefore the portion of the Maritime Link that is used for the benefit of Nalcor cannot be scoped into section 840.

The following analysis was prepared on the basis that Nalcor would be leasing the whole of the Maritime Link. To determine if the arrangement qualifies as a lease – we look to the guidance under ASC 840-10-15-6

**840-10-15-6** *An arrangement conveys the right to use property, plant, or equipment if the arrangement conveys to the purchaser (lessee) the right to control the use of the underlying property, plant, or equipment. The right to control the use of the underlying property, plant, or equipment is conveyed if any of the following conditions is met:*

|   |   |
|---|---|
| <p><i>a. The purchaser has the <u>ability or right to operate the property, plant, or equipment or direct others to operate the property, plant, or equipment in a manner it determines while obtaining or controlling more than a minor amount of the output or other utility of the property, plant, or equipment.</u> The purchaser's ability to operate the property, plant, or equipment may be evidenced by (but is not limited to) the purchaser's ability to hire, fire, or replace the property's operator or the purchaser's ability to specify significant operating policies and procedures in the arrangement with the owner-seller having no ability to change such policies and procedures. <u>A requirement to follow prudent operating practices (or other similar requirements) generally does not convey the right to control the underlying property, plant, or equipment.</u> Similarly, a contractual requirement designed to enable the purchaser to monitor or ensure the seller's compliance with performance, safety, pollution control, or other general standards generally does not establish control over the underlying property, plant, or equipment.</i></p> | <p>Nalcor is involved in the development of the Maritime Link as part of the Joint Development Committee. However, unless there is an event of default, Nalcor does not have the ability to replace NSPML as the operator during the 35 year period.</p> <p>Through the Joint Operating Committee Nalcor has the right to set operating and maintenance standards, but these must be consistent with good utility practice. The guidance specifically addresses this and states that this <i>generally does not convey the right to control the underlying property, plant and equipment.</i></p> <p><b>Conclusion: Criteria for right to operate or to controlling the output not met.</b></p> |
| <p><i>b. The purchaser has the ability or right to</i></p>  | <p>There is nothing in the agreements or</p>  |

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|  |   |
|--|---|
| <p><i>control physical access to the underlying property, plant, or equipment while obtaining or controlling more than a minor amount of the output or other utility of the property, plant, or equipment.</i></p>   | <p>commercial arrangement that would suggest that Nalcor may control physical access of the Maritime Link with the exception of an event of default or when the Maritime Link transfers to Nalcor at the end of 35 year period.</p> <p><b><i>Conclusion: Criteria for right to control not met.</i></b></p>   |
| <p><i>c. Facts and circumstances indicate that it is remote that one or more parties other than the purchaser will take more than a minor amount of the output or other utility that will be produced or generated by the property, plant, or equipment during the term of the arrangement, and the price that the purchaser (lessee) will pay for the output is neither contractually fixed per unit of output nor equal to the current market price per unit of output as of the time of delivery of the output.</i></p> | <p>The arrangement explicitly states that Nalcor must use the transmission rights assigned by NSPML to Nalcor to deliver the NS Block. The NS Block equates to 170MW of the total capacity of 500MW of the Maritime Link. Consequently NSPML receives the benefit of more than a minor amount of the capacity of the Maritime Link.</p> <p>The restriction on the 170MW further supports that Nalcor does not have an unrestricted right to use the Maritime Link for its own purposes.</p> <p><b><i>Conclusion: Criteria for right to control not met.</i></b></p> |

### **Conclusion**

The Maritime Link is not a lease as the criteria above are not met.

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1 **Request IR-32:**

2

3 **If NSPML spends more on the ML than is called for by the 20 for 20 principle, then Nalcor**  
4 **will pay a “true up” to NSPML to bring the capital expenditure down to 20% of the overall**  
5 **project spend. How will this true up payment be represented for tax purposes on the UCC**  
6 **of the Maritime Link?**

7

8 Response IR-32:

9

10 Please refer to NSUARB IR-191 part (b). NSPML notes that the true up arising from the  
11 20 For 20 Principle happens at NSPML’s DG3; total as spent dollars are not relevant to this  
12 calculation. The true up is designed to ensure that 20 percent of the total cost is paid by NSPML,  
13 and 20 percent of the energy is provided to NS Power customers.

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1 **Request IR-33:**

2  
3 **NSPML will be responsible for constructing AC transmission assets in Newfoundland**  
4 **between Granite Canal and Bottom Brook. These assets will be part of the Newfoundland**  
5 **transmission system, controlled by Nalcor, and potentially be connected to and serving**  
6 **Nalcor customers in the future.**

7  
8 **(a) Will NSPML have legal title to these assets?**

9  
10 **(b) Will NSPML take CCA against these assets for tax purposes?**

11  
12 **(c) Will NSPML share in any revenues received by Nalcor from customers that may be**  
13 **connected to this line in the future?**

14  
15 **(d) How will such revenues affect Nova Scotia ratepayers?**

16  
17 **Response IR-33:**

18  
19 **(a) Yes, NSPML will have legal ownership of these assets.**

20  
21 **(b) Yes.**

22  
23 **(c) No. NL transmission services are not an additional cost exposure to NSPML for use of**  
24 **the cross island transmission system. Incremental cost burdens which result from a new**  
25 **customer will be the responsibility of Nalcor.**

26  
27 **(d) Not applicable based upon the reply to (c).**

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1 **Request IR-34:**

2  
3 **Referring to your response to MPA IR-15: After 35 years of operation of the ML, it will be**  
4 **transferred to Nalcor for \$1, and is expected to continue to operate for its full life of 50**  
5 **years.**

6  
7 **(a) Under what energy pricing scenarios in years 35-50 will Nalcor earn “windfall**  
8 **profits” wheeling power into the New England market?**

9  
10 **(b) Under what energy pricing scenarios in years 35-50 will NSPML earn “windfall**  
11 **profits” in the form of an opportunity to benefit from low power prices, owing to its**  
12 **economic position in the energy loop?**

13  
14 **(c) Under what energy pricing scenarios in years 35-50 might Nalcor elect to store**  
15 **power or spill water, leave the Maritime Link unutilized or underutilized and hence**  
16 **reduce opportunities for NS ratepayers to benefit from low-priced power?**

17  
18 **(d) How do you perceive the relative risk and balance of these various economic**  
19 **opportunities in the context of the 20 for 20 principle?**

20  
21 **Response IR-34:**

22  
23 **(a) NSPML has not analyzed the scenarios beyond 35 years.**

24  
25 **(b) NS Power customers, not NSPML, will benefit from having access to additional market**  
26 **priced energy as illustrated in the response to NSUARB IR-37. Any time the netback cost**  
27 **of Nalcor energy is lower than NS Power marginal cost there is potential for cost savings,**  
28 **which will benefit NS customers, as it is anticipated that Nova Scotia will be first in line**  
29 **for the Nalcor energy. .**

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- 1 (c) See response to MPA IR-22 which notes NSPML's expectation that the Maritime Link  
2 will be well utilized. Companies selling energy will generally store their energy if  
3 possible when market prices are very low, in which case NS Power would be  
4 experiencing the same market dynamic. When prices increase, or storage is full, the  
5 sellers of hydroelectricity would sell, thus providing more supply during this period.  
6 NSPML expects that Nalcor is interested in selling its energy for a return rather than  
7 spilling the water for no return. It will have access to transmission in rights in the  
8 Maritimes and therefore it is expected that it would use those rights to transport energy to  
9 energy markets rather than spilling energy.  
10
- 11 (d) NSPML believes that the Project provides NS customers with the lowest-cost long-term  
12 alternative. The term of the Formal Agreements is the result of negotiation and has been,  
13 in part, based upon the expected service life of the Maritime Link. The equivalent of 50  
14 years of energy will have been received at the end of the 35 year term. NSPML  
15 anticipates that, after 35 years, Nalcor will act in its own economic interests as a supplier  
16 just as NS Power will act in its own economic interests. Competition in the market will  
17 help to ensure that energy is available at market prices to NS customers. Nova Scotia will  
18 benefit from new supply options which it does not have today and will be first in line to  
19 access the energy most economically benefiting Nova Scotia strategically in a way no  
20 other alternative does. These scenarios are not relevant for 20 For 20 Principle as  
21 NSPML has been kept whole with energy deliveries over the 35 year term of the ECA.



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1 **Request IR-35:**

2

3 **In response to MPA IR-18, the applicant provided an analysis of the impact of the ML on**  
4 **Nova Scotia customer costs for the first year of the operation of the project. Please provide**  
5 **a similar analysis for the full life of the ML project.**

6

7 Response IR-35:

8

9 Please refer to NSUARB IR-166 and CanWEA IR-115.

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1 **Request IR-36:**

2  
3 **(a) In the combined project encompassing the LTA, MF, LIL and ML, is there expected**  
4 **to be access to any accelerated CCA classes, such as Class 43.1 (at 30%) or Class**  
5 **43.2 (at 50%) for renewable energy assets?**

6  
7 **(b) If so, under the 20 For 20 Principles, will NSPML be able to proportionately share**  
8 **in access to these classes of CCA?**

9  
10 **(c) If not, why not?**

11  
12 **(d) Given the non-taxable status of Nalcor, is access to these accelerated CCA classes**  
13 **being lost at no benefit to ratepayers?**

14  
15 **Response IR-36:**

16  
17 (a-d) Please refer to response to NSUARB IR-165. NSPML does not have legal title to any of  
18 the LCP Phase I assets. NSPML has legal title to the Maritime Link assets only. As such,  
19 the appropriate tax treatment for the Maritime Link assets will be applicable, not those of  
20 the LCP Phase I assets.

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1 **Request IR-37:**

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3 **Does the structure of the entire agreement provide NSPML, and Nova Scotia ratepayers**  
4 **more generally, the flexibility to solicit, or deal with unsolicited, competing offers for long**  
5 **term power at various stages of the project (should these arise over the course of 50 years)?**  
6 **For example, break-up fees, non-solicit provisions, etc.?**

7

8 Response IR-37:

9

10 The structure of the agreements does not preclude NS Power from entering into additional long-  
11 term power purchase arrangements.