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January 29, 2025

Board of Commissioners of Public Utilities
Prince Charles Building
120 Torbay Road, P.O. Box 21040
St. John's, NL A1A 5B2

Attention: Jo-Anne Galarneau
Executive Director and Board Secretary

Re: Application for the Approval of an Increase to Hydro's Target Return on Equity and Revisions to Return on Equity Rate Change Deferral Account and Excess Earnings Account Definitions

Please find enclosed Newfoundland and Labrador Hydro's ("Hydro") application for an increase to Hydro's target return on equity ("ROE") and revisions to Hydro's ROE Rate Change Deferral Account and Excess Earnings Account definitions ("Application").

Pursuant to Order in Council OC2009-063 and Board of Commissioners of Public Utilities ("Board") Order No. P.U. 49(2016), Hydro is to have the same target ROE as was most recently set for Newfoundland Power Inc. ("Newfoundland Power") and that target is to be adjusted in the years between general rate applications ("GRA") to ensure it continues to be the same as Newfoundland Power's ROE. The Board recently approved an increase in Newfoundland Power's ROE from 8.50% to 8.60%, in Board Order No. P.U. 3(2025). Hydro's Application proposes to revise its 2019 Test Year ROE from 8.50% to 8.60%, as was approved for Newfoundland Power, effective January 1, 2025.

As is further discussed in Hydro's Application, Hydro is also proposing a deviation from the current methodology. Hydro proposes to record the revenue requirement impact of the change in ROE monthly in the ROE Rate Change Deferral Account until the next test year. Hydro would not propose base rate changes in 2025 other than in the upcoming GRA. To effect the revised ROE and the deviation from the current methodology, Hydro is proposing revisions to the ROE Rate Change Deferral Account definition as well as the Excess Earnings Account definition, effective January 1, 2025. Further discussion regarding these proposals is contained within Schedule 1 of this Application.

Should you have any questions, please contact the undersigned.

Yours truly,

NEWFOUNDLAND AND LABRADOR HYDRO

A handwritten signature in blue ink, appearing to read "Shirley A. Walsh", written over a horizontal line.

Shirley A. Walsh
Senior Legal Counsel, Regulatory
SAW/kd

Encl.

ecc:

Jo-Anne Galarneau
Board of Commissioners of Public Utilities

2

Board of Commissioners of Public Utilities

Jacqui H. Glynn
Board General

Consumer Advocate

Dennis M. Browne, KC, Browne Fitzgerald Morgan & Avis
Stephen F. Fitzgerald, KC, Browne Fitzgerald Morgan & Avis
Sarah G. Fitzgerald, Browne Fitzgerald Morgan & Avis
Bernice Bailey, Browne Fitzgerald Morgan & Avis

Linde Canada Inc.

Sheryl E. Nisenbaum
Peter Strong

Newfoundland Power Inc.

Dominic J. Foley
Regulatory Email

Teck Resources Limited

Shawn Kinsella

Island Industrial Customer Group

Paul L. Coxworthy, Stewart McKelvey
Denis J. Fleming, Cox & Palmer
Glen G. Seaborn, Poole Althouse

Increase to Target ROE and Revisions to ROE Rate Change Deferral Account and Excess Earnings Account Definitions

January 29, 2025

An application to the Board of Commissioners of Public Utilities



IN THE MATTER OF the *Electrical Power Control Act, 1994*, SNL 1994, Chapter E-5.1 (“EPCA”) and the *Public Utilities Act*, RSNL 1990, Chapter P-47 (“Act”), and regulations thereunder; and

IN THE MATTER OF an application by Newfoundland and Labrador Hydro (“Hydro”) for an Order approving Hydro’s target return on equity (“ROE”) and revisions to Hydro’s ROE Rate Change Deferral Account and Excess Earnings Account definitions pursuant to Sections 58 and 80 of the *Act*.

To: The Board of Commissioners of Public Utilities (“Board”)

THE APPLICATION OF HYDRO STATES THAT:

A. Background

1. Hydro, a corporation continued and existing under the *Hydro Corporation Act, 2024*, is a public utility within the meaning of the *Act*, and is subject to the provisions of the *EPCA*.
2. Order in Council OC2009-063 was issued on March 17, 2009, directing that the Board adopt policies for all future general rate applications (“GRA”) filed by Hydro, beginning with the first Hydro GRA filed after January 1, 2009. The policies were that in calculating the return on rate base (“RORB”) for Hydro, to set the same target ROE as was most recently set for Newfoundland Power Inc. (“Newfoundland Power”) through a GRA or through Newfoundland Power’s Automatic Adjustment Mechanism.
3. In Board Order No. P.U. 49(2016), the Board determined that Hydro’s target ROE should be subject to an adjustment process in the years between GRAs so that it continues to be the same as Newfoundland Power’s ROE.
4. In Board Order No. P.U. 30(2019), the Board approved the definitions of the ROE Rate Change Deferral Account and Excess Earnings Account. The methodology applied to determine the change in Hydro’s revenue requirement by rate class and rate design resulting from the change was included within the ROE Rate Change Deferral Account definition.

5. Newfoundland Power filed its GRA in December 2023 requesting an increase in its ROE. In Board Order No. P.U. 3(2025), the Board approved an increase in Newfoundland Power's ROE from 8.50% to 8.60%.

B. Application

6. Consistent with Order in Council OC2009-063 and Board Order No. P.U. 49(2016), Hydro proposes to revise its 2019 Test Year ROE from 8.50% to 8.60%, as was approved for Newfoundland Power, effective January 1, 2025.
7. Utilizing the approved methodology for the adjustment mechanism, the change in revenue requirement resulting from the increased ROE is \$463,000. This results in an increase in RORB from 5.43% to 5.45% as demonstrated in Appendix A to Schedule 1 of this application. The allocation of the revenue requirement increase to each customer group is provided in Table 1 of Schedule 1.
8. The currently approved Rate Implementation Process, as discussed in Schedule 1, requires Hydro to make an application to change rates for customers as a result of the increase in the ROE.
9. As a result of the materiality of the revenue requirement adjustments by the customer group, the stipulated domestic rate increases arising from the rate mitigation plan, and Hydro's intent to file a GRA in the second half of 2025, Hydro proposes to deviate from the existing general process. Hydro suggests recording the revenue requirement impact of the change in ROE monthly in the ROE Rate Change Deferral Account until the next test year. Hydro would not propose base rate changes in 2025 other than in the upcoming GRA.
10. Additionally, Hydro proposes to modify the ROE Rate Change Deferral Account Rules for Disposition to allow the transfer of the balances attributable to Newfoundland Power and the Island Industrial Customers to the Supply Cost Variance Deferral Account ("SCVDA") Utility Customer Balance and Industrial Customer Balance on March 31 of each year. The disposition of these balances will be according to the rules to be proposed and approved for the SCVDA.
11. Further details regarding the proposed process changes are provided in Schedule 1, with the proposed revised ROE Rate Change Deferral Account definition included in Attachment 2 to Schedule 1.

12. Hydro further proposes to amend the Excess Earnings Account definition to include the revised 2019 Test Year RORB of 5.45%. The proposed amended Excess Earnings Account definition is included in Attachment 3 to Schedule 1.

C. Newfoundland and Labrador Hydro's Request

13. Hydro requests that the Board make an Order pursuant to Sections 58 and 80 of the Act approving:
- i. A ROE of 8.60% effective January 1, 2025;
 - ii. A RORB of 5.45% effective January 1, 2025;
 - iii. A revised 2019 Test Year Revenue Requirement of \$643,504,433;
 - iv. A revised ROE Rate Change Deferral Account definition effective January 1, 2025;
 - v. A revised Excess Earnings Account definition effective January 1, 2025; and
 - vi. A deviation to the currently approved methodology to update the rate structure for Newfoundland Power, Island Industrial Customers, Hydro Rural Labrador Interconnected Customers, and Labrador Industrial Customers to reflect an ROE of 8.60% in the next test year.

D. Communications

14. Communications concerning this application should be forwarded to Shirley A. Walsh, Senior Legal Counsel, Regulatory for Hydro.

DATED at St. John's in the province of Newfoundland and Labrador on this 29th day of January 2025.

NEWFOUNDLAND AND LABRADOR HYDRO



Shirley A. Walsh
Counsel for the Applicant
Newfoundland and Labrador Hydro
500 Columbus Drive, P.O. Box 12400
St. John's, NL A1B 4K7
Telephone: (709) 685-4973

Schedule 1

Evidence



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Appendix A: Financial Schedules Supporting Increase in Return on Rate Base

List of Attachments

Attachment 1: ROE Rate Change Deferral Account Definition and Methodology

Attachment 2: ROE Rate Change Deferral Account Definition (Proposed Amendments)

Attachment 3: Excess Earnings Account Definition (Proposed Amendments)

1.0 Background

Order in Council OC2009-063, issued on March 17, 2009, directed the Board of Commissioners of Public Utilities (“Board”) to adopt certain policies for all general rate applications (“GRA”) by Newfoundland and Labrador Hydro (“Hydro”) to follow, commencing with the first Hydro GRA filed after January 1, 2009. The policies were:

- 1) In calculating the return on rate base (“RORB”) for Hydro, to set the same target return on equity (“ROE”) as was most recently set for Newfoundland Power Inc. (“Newfoundland Power”) through a GRA or through Newfoundland Power’s Automatic Adjustment Mechanism;
- 2) That Hydro is entitled to earn annually, a rate of return equal to the weighted average cost of capital, as ordered from time to time, on the entire rate base as fixed and determined by the Board, including amounts used solely for the provision of service to its Rural customers; and
- 3) That the capital structure approved for Hydro should be permitted to have a maximum portion of equity as was most recently approved for Newfoundland Power.

In Board Order No. P.U. 49(2016), the Board determined that Hydro’s target ROE should be subject to an adjustment process in the years between GRAs so that it continues to be the same as Newfoundland Power’s ROE.

The Board approved the definition of the ROE Rate Change Deferral Account in Board Order No. P.U. 30(2019). The approved deferral account definition, which includes the methodology originally filed as Sections 1 to 5 of Exhibit 12 to the 2017 GRA filing, is included in Attachment 1. The methodology has been applied to determine the change in Hydro’s revenue requirement by rate class and rate design resulting from the change, approved in Board Order No. P.U. 3(2025), in Newfoundland Power’s ROE from 8.50% to 8.60%.

This evidence provides Hydro’s calculation of the increase in revenue requirement based on its approved 2019 Test Year as a result of Newfoundland Power’s change in ROE, and Hydro’s proposed approach for recovery. The evidence also proposes revisions to the ROE Rate Change Deferral Account to reflect changes in the rules for disposition and revisions to the Excess Earnings Account definition to reflect the proposed change in RORB.

1 2.0 ROE Rate Change Deferral Account

2 The purpose of the ROE Rate Change Deferral Account is to defer recovery of the change in the test year
3 revenue requirement that will occur due to the customer rate implementation date differing from the
4 effective date of the approved ROE percentage.

5 The utilization of the methodology for the adjustment mechanism included in the ROE Rate Change
6 Deferral Account definition¹ determined that the change in revenue requirement resulting from a
7 change in ROE from 8.50% to 8.60% is \$463,000. The increase in ROE results in an increase in RORB from
8 5.43% to 5.45%. Appendix A provides the finance schedules supporting the increase in RORB and
9 revenue requirement including a statement of income and retained earnings, rate of RORB, and capital
10 structure including the calculation of the revised weighted average cost of capital.

11 Table 1 shows the allocation of this revenue requirement increase to each of the customer groups and
12 the percentage increase from the 2019 Test Year Revenue Requirement.

Table 1: Allocation of Revised Revenue Requirement

Customer Group	Approved 2019 Test Year Revenue Requirement (\$000)	Revised 2019 Test Year Revenue Requirement (\$000)	Change (\$000)	Change (%)
Newfoundland Power – Incl. Rural Deficit	506,977	507,385	408	0.08
Island Industrial	45,662	45,689	27	0.06
Labrador Industrial	4,985	4,991	6	0.12
Hydro Rural Labrador Interconnected – Incl. Rural Deficit	20,636	20,658	22	0.11
Rural Revenues from Deficit Areas	64,781	64,781	-	0.00
	643,041	643,504	463	0.07

13 Table 1 allocates the increase in the Rural Deficit of \$92,000 resulting from the increase in the test year
14 RORB to Newfoundland Power and the Hydro Rural Labrador Interconnected Customers.²

¹ "2017 General Rate Application," Newfoundland and Labrador Hydro, rev. July 4, 2018 (originally filed July 28, 2017), vol. II, Exhibit 12.

² The increase in the Rural Deficit is reallocated based on the 2019 Test Year Rural Deficit (96.1% for Newfoundland Power and 3.9% for customers on the Hydro Rural Labrador Interconnected System).

1 The deferral account definition specifies that the annual ROE revenue requirement adjustments for
2 Newfoundland Power and Island Industrial Customers reflecting the revised test year ROE percentage be
3 converted to monthly revenue requirement adjustments and recorded in the account for each month of
4 delayed rate implementation. For Hydro Rural Labrador Interconnected and Labrador Interconnected
5 Industrial Customers, if the effective date of revised customer rates is subsequent to the effective date
6 of the approved test year ROE, the test year revenue requirement impacts of delayed implementation
7 will be recorded in the account.

8 **2.1 Proposed Cost Recovery**

9 The ROE Rate Change Deferral Account, along with rules for balance accumulation, contains rules for the
10 Rate Implementation Process. The existing implementation process for changing customer rates that
11 result from ROE revenue requirement adjustments requires:

- 12 **1)** An application by Hydro to change rates for Hydro Rural Labrador Interconnected and Labrador
13 Interconnected Industrial Customers reflecting the allocated revised test year revenue
14 requirement based on the effective date of the revised test year ROE; and
- 15 **2)** Proposals by Hydro to change rates for Newfoundland Power and Island Industrial Customers
16 reflecting the revised test year ROE revenue requirements to accompany Hydro's applications to
17 update the Rate Stabilization Plan ("RSP") adjustments.

18 The report on the Automatic ROE Adjustment, included as Attachment 1, notes that the process for
19 implementation of compliance rates reflecting a Newfoundland Power GRA would be required to
20 change due to the automatic update to Hydro's test year revenue requirement resulting from a change
21 in ROE from Newfoundland Power. The compliance application for Newfoundland Power would also
22 need to reflect the revised supply cost from Hydro as a result of any required change in the approved
23 ROE for Hydro.

24 Hydro is proposing to deviate from the general process previously outlined, while still following the
25 approved deferral account definition, as a result of the following:

- 26 **a.** The materiality of the revenue requirement adjustments by customer group per Table 1;
- 27 **b.** The rate mitigation plan announced on May 16, 2024, stipulated the domestic rate increases
28 attributable to Hydro's costs to 2.25% annually; and

1 c. Hydro is preparing to file its next GRA in the second half of 2025.

2 Given these considerations, Hydro is proposing to record the revenue requirement impact of the change
3 in ROE monthly in the ROE Rate Change Deferral Account until the next test year and not propose base
4 rate changes in 2025 outside of its next GRA.

5 For Newfoundland Power and the Island Industrial Customers, as their rates are mitigated, Hydro
6 proposes that the 2025 balance in the deferral account be transferred to the Supply Cost Variance
7 Deferral Account (“SCVDA”) on March 31, 2026, and changes to the base rate reflecting the 8.60% ROE
8 be effective in the next test year.

9 For Labrador Industrial and Hydro Rural Labrador Interconnected Customers, Hydro will propose
10 recovery of the deferral account balance in the next GRA and propose changes to base rates reflecting
11 the 8.60% ROE in the next test year.

12 **2.2 ROE Rate Change Deferral Account – Proposed Amendments**

13 The current ROE Rate Change Deferral Account definition rules for disposition state:

14 **1)** On June 30 of each year, the balance attributable to Newfoundland Power will be transferred to
15 the Newfoundland Power RSP Current Plan for disposition through the RSP recovery adjustment
16 for the subsequent 12-month period.

17 **2)** On December 31 of each year, the balance attributable to Island Industrial Customers will be
18 transferred to the Island Industrial Customers RSP Current Plan balance for disposition through
19 the Industrial Customer RSP recovery adjustment for the subsequent 12-month period.

20 The approval of the SCVDA in Board Order No. P.U. 33(2021) discontinued transfers to the RSP resulting
21 from variations in future costs, and Board Order No. P.U. 4(2022) approved the RSP Rules for Balance
22 Disposition. Since the amortization of the Hydraulic balance concludes on December 31, 2025, with the
23 account expected to be fully recovered on June 30, 2026,³ Hydro is proposing to modify the ROE Rate
24 Change Deferral Account to transfer these amounts to the SCVDA Utility Customer Balance and
25 Industrial Customer Balance on March 31 of each year. The disposition of these balances will be

³ The Isolated Systems Supply Cost Deferral Account annual balance is currently transferred to the RSP for recovery. Hydro will propose an alternate method of recovery in its application for recovery of the 2025 balance in the first quarter of 2026.

1 according to the rules to be proposed and approved for the SCVDA. The proposed amendments to the
2 ROE Rate Change Deferral Account are included as Attachment 2.

3 **3.0 Excess Earnings Account Definition – Proposed** 4 **Amendments**

5 Hydro is proposing to amend the Excess Earnings Account definition to include the revised 2019 Test
6 Year RORB of 5.45%. The proposed amendments to the Excess Earnings Account definition are included
7 as Attachment 3.

8 **4.0 Conclusion**

9 In Board Order No. P.U. 49(2016), the Board determined that Hydro’s target ROE should be subject to an
10 adjustment process in the years between GRAs so that it continues to be the same as Newfoundland
11 Power’s ROE. Hydro has computed its change in revenue requirement as a result of the change in ROE
12 from 8.50% to 8.60% approved for Newfoundland Power in Board Order No. P.U. 3(2025).

13 The existing guidance for the Rate Implementation Process requires Hydro to make an application to
14 change rates for Hydro Rural Labrador Interconnected and Labrador Interconnected Industrial
15 Customers reflecting the allocated revised test year revenue requirement based on the effective date of
16 the revised test year ROE, and to change rates for Newfoundland Power and Island Industrial Customers
17 reflecting the revised test year ROE revenue requirements to accompany Hydro’s applications to update
18 the RSP adjustments or in advance of Newfoundland Power’s compliance application. In this instance,
19 Hydro is proposing to deviate from the general process, while still following the approved deferral
20 account definition, and record the revenue requirement impact of the change in ROE monthly in the
21 ROE Rate Change Deferral Account until the next test year and not propose base rate changes in 2025
22 outside of its next GRA.

23 In addition, Hydro proposes to modify the ROE Rate Change Deferral Account Rules for Disposition to
24 allow the transfer of the balances attributable to Newfoundland Power and the Island Industrial
25 Customers to the SCVDA Utility Customer Balance and Industrial Customer Balance on March 31 of each
26 year. The disposition of these balances will be according to the rules to be proposed and approved for
27 the SCVDA.

Appendix A

Financial Schedules Supporting Increase in Rate of Return
on Rate Base



**Increase to Target ROE and Revisions to ROE Rate Change Deferral Account and Excess Earnings Account Definitions
Schedule 1, Appendix A, Page 1 of 3**

**Newfoundland and Labrador Hydro
Financial Results and Forecasts
Statement of Income and Retained Earnings
(\$000s)**

	Rate Setting Test Year 2019	ROE Adjustment	Revised Rate Setting Test Year 2019
1 Revenue			
2 Energy sales	589,829	463	590,292
Revenue Deficiency	51,813	-	51,813
3 Generation Demand Cost Recovery	1,399	-	1,399
4 CIAC Revenue	1,815	-	1,815
5 Other revenue	2,109	-	2,109
6 Total revenue	646,965	463	647,428
7			
8 Expenses			
9 Operating expenses	136,963	-	136,963
10 Other Income and expense	-	-	-
11 Foreign exchange	2,157	-	2,157
12 Fuels	219,857	-	219,857
13 Power purchases	67,372	-	67,372
14 Power Purchases - Off-Island	14,290	-	14,290
15 Transmission Costs	-	-	-
16 Depreciation	85,429	-	85,429
17 Accretion of asset retirement obligation	364	-	364
18 Interest	93,057	-	93,057
19 Total expenses	619,489	-	619,489
20			
21 Net income (loss) before compliance adjustments	27,476	463	27,939
22 Compliance Adjustments	-	-	-
23 Net Income (loss) after compliance adjustments	27,476	463	27,939
24			
25 Retained earnings			
26 Balance at beginning of year	323,017	-	323,017
27 Opening adjustment - retained earnings	-	-	-
28 Dividends	-	-	-
29 Balance at end of year	350,493	463	350,956

**Increase to Target ROE and Revisions to ROE Rate Change Deferral Account and Excess Earnings Account Definitions
Schedule 1, Appendix A, Page 2 of 3**

**Newfoundland and Labrador Hydro
Financial Results and Forecasts
Rate of Return on Rate Base
(\$000s)**

	Rate Setting Test Year 2019	ROE Adjustment	Revised Rate Setting Test Year 2019
1 Property, plant, and equipment	2,240,847	-	2,240,847
2 add: accumulated depreciation (net of disposal & Removal pools)	446,385	-	446,385
3 less: work in progress	(12,512)	-	(12,512)
4 Capital assets in service	2,674,720	-	2,674,720
5 less: asset retirement obligation	(124)	-	(124)
6 add: contributions in aid of construction	(44,965)	-	(44,965)
7 less: accumulated depreciation	(446,385)	-	(446,385)
8 Capital assets - current year	2,183,246	-	2,183,246
9 Capital assets - previous year	2,083,554	-	2,083,554
10 Unadjusted capital assets - average	2,133,400	-	2,133,400
11 less: Average net assets excluded from rate base	(11,519)	-	(11,519)
12 Capital assets - average	2,121,881	-	2,121,881
13		-	
14 Working capital allowance	2,022	-	2,022
15 Fuel	57,150	-	57,150
16 Materials and supplies	32,884	-	32,884
17 Deferred charges	103,333	-	103,333
18		-	
19 Average rate base	2,317,270	-	2,317,270
20		-	
21 Net Income	27,476	463	27,939
22 add: Cost of service exclusions:		-	
23 Revenue Req. Cost of Service Exclusions	3,088	-	3,088
24 Interest. Cost of Service Exclusions	6,302	-	6,302
25 Regulated Interest	88,912	-	88,912
26 Return on rate base	125,778	463	126,241
27		-	
28 Rate of return on rate base	5.43%	0.02%	5.45%

**Newfoundland and Labrador Hydro
Financial Results and Forecasts
Capital Structure
(\$000s)¹**

	Rate Setting Test Year 2019	ROE Adjustment	Revised Rate Setting Test Year 2019
1 Regulated capital structure			
2 Long-term debt	1,794,947	-	1,794,947
3 Promissory notes	291,930	-	291,930
4 Promissory notes - related party	-	-	-
5 less: sinking funds	(223,976)	-	(223,976)
6 add: mark to market of sinking funds	40,738	-	40,738
7	1,903,639	-	1,903,639
8 Cost of service exclusions			
9 Non-regulated debt pool	(11,067)	-	(11,067)
10 Net regulated debt	1,892,572	-	1,892,572
11 Funded Asset retirement obligation	14,443	-	14,443
12 Employee future benefits	76,085	-	76,085
13 Contributed capital	100,000	-	100,000
14 Retained earnings cost of service exclusions	33,484	-	33,484
15 Retained earnings	350,493	463	350,956
16 Total	2,467,076	463	2,467,539
17			
18 Regulated capital structure (%)			
19 Debt	76.71%	-0.01%	76.70%
20 Asset retirement obligation	0.59%	0.00%	0.59%
21 Employee future benefits	3.08%	0.00%	3.08%
22 Equity	19.62%	0.02%	19.63%
23 Total	100.00%	-	100.00%
24			
25 Regulated average capital structure (%)			
26 Debt	76.80%	-0.01%	76.79%
27 Asset retirement obligation	0.61%	0.00%	0.61%
28 Employee future benefits	3.12%	0.00%	3.12%
29 Equity	19.48%	0.01%	19.48%
30 Total	100.0%	-	100.0%
31			
32 Weighted average cost of capital (WACC)			
33 Embedded cost of debt	4.91%	0.00%	4.91%
34 Asset retirement obligation	0.00%	0.00%	0.00%
35 Employee future benefits	0.00%	0.00%	0.00%
36 Equity	8.50%	0.10%	8.60%
37 WACC	5.430%	0.02%	5.45%

¹ Numbers may not add due to rounding.

Attachment 1

ROE Rate Change Deferral Account Definition and Methodology





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May 15, 2018

The Board of Commissioners of Public Utilities
Prince Charles Building
120 Torbay Road, P.O. Box 21040
St. John's, NL
A1A 5B2 Canada

**Attention: Ms. Cheryl Blundon
Director Corporate Services & Board Secretary**

Dear Ms. Blundon:

Re: Return on Equity (ROE) Rate Change Deferral Account

Further to Newfoundland and Labrador Hydro's (Hydro's) 2017 General Rate Application (GRA) Settlement Agreement, enclosed please find one (1) original and thirteen (13) copies of Hydro's ROE Rate Change Deferral Account Definition.

Should you have any questions, please contact the undersigned.

Yours truly,

NEWFOUNDLAND AND LABRADOR HYDRO

A handwritten signature in blue ink, appearing to read "Geoffrey P. Young", written over a horizontal line.

Geoffrey P. Young,
Corporate Secretary & General Counsel
GPY/skc

cc: Gerard Hayes – Newfoundland Power Inc.
Paul Coxworthy – Stewart McKelvey
Denis J. Fleming – Cox & Palmer
ecc: Van Alexopolous – Iron Ore Company
Senwung Luk – Olthuis Kleer Townshend LLP

Dennis Browne, Q.C. – Browne Fitzgerald Morgan & Avis
Dean Porter – Poole Althouse
Benoit Pepin – Rio Tinto

Newfoundland and Labrador Hydro Return on Equity (ROE) Rate Change Deferral Account

Purpose

As per Board Order No. P.U. 49(2016), Newfoundland and Labrador Hydro's (Hydro's) target Return on Equity (ROE) percentage must be adjusted as required to equal the ROE approved for Newfoundland Power. The purpose of the ROE Rate Change Deferral Account is to defer recovery of the change in test year revenue requirement that will occur due to the customer rate implementation date differing from the effective date of the approved ROE percentage.

Methodology

As a result of changes in the ROE percentage between test years, the methodology originally filed as Sections 1 to 5 of Exhibit 12 to the 2017 GRA filing and included as Attachment 1 will be used in determining the change in revenue requirement by rate class and rate design.

Rate Implementation Process

The implementation process for changing customer rates that result from ROE revenue requirement adjustments shall include:

- a) an application by Hydro to change rates for Hydro Rural Labrador Interconnected and Labrador Interconnected Industrial Customers reflecting the allocated revised test year revenue requirement based on the effective date of revised test year ROE;
- b) proposals by Hydro to change rates for Newfoundland Power and Island Industrial Customers reflecting the revised test year ROE revenue requirements to accompany Hydro's applications to update the RSP adjustments.

Balance Accumulation

The annual ROE revenue requirement adjustments for Newfoundland Power and Island Industrial Customers reflecting the revised test year ROE percentage will be converted to monthly revenue requirement adjustments to be recorded in the ROE Rate Change Deferral Account for each month of delayed rate implementation.

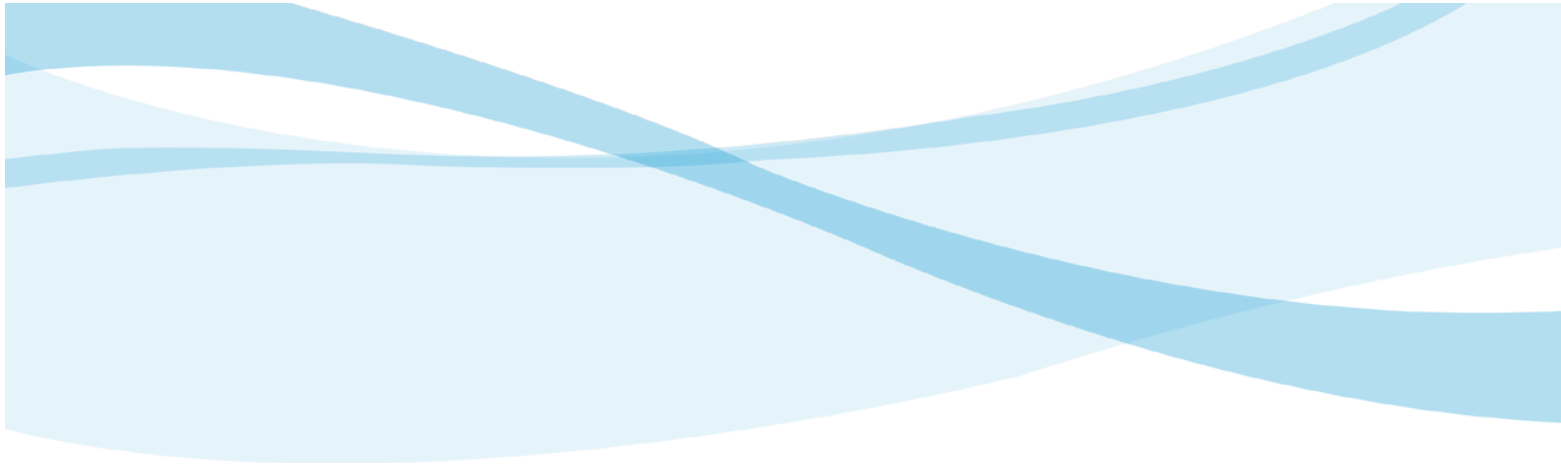
If the effective date of revised customer rates on the Labrador Interconnected System is subsequent to the effective date of the approved revised test year ROE, Hydro will record the test year revenue requirement impacts of delayed rate implementation in the ROE Rate Change Deferral Account.

Disposition

On June 30 of each year, the balance attributable to Newfoundland Power will be transferred to the Newfoundland Power RSP Current Plan balance for disposition through the RSP recovery adjustment for the subsequent 12 month period.

On December 31 of each year, the balance attributable to Island Industrial Customers will be transferred to the Island Industrial Customers RSP Current Plan balance for disposition through the Industrial Customer RSP recovery adjustment for the subsequent 12 month period.

Any balances related to Labrador Interconnected customers will be proposed for disposition at Hydro's next General Rate Application.



Automatic Return on Equity Adjustment

Newfoundland and Labrador Hydro

June 2017

A Report to the Board of Commissioners of Public Utilities

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7.0	Conclusion.....	5

1 **1.0 Overview**

2 In Board Order No. P.U. 49(2016), the Board of Commissioners of Public Utilities (the Board)
3 determined that Newfoundland and Labrador Hydro's (Hydro) target return on equity should be
4 subject to an adjustment process in the years between General Rate Applications (GRAs) so
5 that it continues to be the same as Newfoundland Power's return on equity. As such, it directed
6 Hydro to file a proposal in relation to an adjustment mechanism for its target return on equity.

7
8 This report provides an overview of the calculation of the adjustment to return on equity, the
9 allocation of the adjustment to various customers, the required adjustment to customer rates
10 to reflect the change in revenue requirement, and any process related matters to implement
11 the rate adjustment.

12

13 **2.0 Flow-through of Adjustment to Return on Equity**

14 **2.1 Adjustment to Return on Equity and Weighted Average Cost of Capital**

15 Upon the delivery of an order to change Newfoundland Power's rate of return on equity, Hydro
16 would be required to update its return on equity to be equal to that of Newfoundland Power.

17 This change would, in turn, cause a change in Hydro's weighted average cost of capital and
18 return on rate base. For illustrative purposes, Hydro's 2015 Test Year weighted average cost of
19 capital (WACC) for rate setting would reduce from 6.61% to 6.56% if the approved Test Year
20 return on equity was revised from 8.50% to 8.25%.

21

22 Appendix A to this report provides the calculation showing the impact on WACC and return on
23 rate base of 25 basis point reduction in the Test Year return on equity based on the illustrative
24 change in return on equity noted above.

25

26 **2.2 Adjustment to Revenue Requirement for Rate Setting**

27 To reflect a revised return on rate base in customer rates and ensure that Hydro's rates reflect
28 the same return on equity as Newfoundland Power would require Hydro to calculate a revised

1 Test Year revenue requirement for rate setting. Using the illustrative change in return on equity
2 noted in section 2.1, a reduction of 5 basis points in return on rate base would reduce Hydro's
3 revenue requirement to be recovered through customer rates by \$964,000, or approximately
4 0.17% of the approved 2015 Test Year revenue requirement from customer rates.

5
6 The calculation of the revised Test Year revenue requirement was derived by updating the Test
7 Year rate of return on rate base (as provided in Appendix A) in the calculation of the revised
8 Test Year return on rate base. Finance schedules showing the derivation of the revised 2015
9 Test Year revenue requirement for rate setting reflecting the illustrative change from 8.50%
10 return on equity to 8.25% return on equity is provided in Appendix B.

11

12 **3.0 Allocation of Revised Revenue Requirement**

13 In order to allocate the return on equity adjustment amongst customer groups, Hydro would be
14 required to revise its approved Test Year cost of service for rate setting to reflect the revised
15 Test Year return on rate base. Doing so would provide revised Test Year revenue requirements
16 by class consistent with the approved cost of service methodology for the most recently
17 approved Test Year. As Hydro would be revising the approved Test Year cost of service study,
18 Hydro would submit a revised Test Year cost of service study for Board approval reflecting the
19 revised return on equity approved for Newfoundland Power.

20

21 Table 1 provides the impact of 25 basis point return on equity decrease on 2015 Test Year
22 revenue requirement by rate class.

Table 1
Allocation of Revised Revenue Requirement

Customer Group	Approved 2015 Test Year Revenue Requirement (\$000)	Revised 2015 Test Year Revenue Requirement (\$000)	Change (\$000)	Change (%)
Newfoundland Power – Incl. Rural Deficit	443,366	442,515	(851)	(0.19)
Island Industrial	34,829	34,776	(53)	(0.15)
Labrador Industrial	5,218	5,210	(8)	(0.15)
CFB Goose Bay Secondary	932	932	0	0.00
Hydro Rural Labrador Int. – Incl. Rural Deficit	20,169	20,117	(52)	(0.26)
Rural Revenues from Deficit Areas	60,851	60,851	0	0.00
Total	565,365	564,401	(964)	(0.17)

1 Table 1 allocates the reduced Rural Deficit of \$203,000 resulting from the reduction in the Test
2 Year return on rate base to Newfoundland Power and the Hydro Rural Labrador Interconnected
3 customers.

4

5 **4.0 Revisions to Customer Rates**

6 Hydro would follow the Board’s most recently approved rate design approach in computing
7 proposed rates to recover the revised Test Year revenue requirement.

8

9 For Newfoundland Power, the second block energy rate is currently set based on the Test Year
10 price of Holyrood fuel and the demand charge is negotiated. Therefore, Hydro would propose
11 that changes to the Test Year revenue requirement allocated to Newfoundland Power would be
12 applied through a change in the first block rate.

13

14 The Island Industrial Customers’ rates for demand, energy, and specifically assigned charges
15 currently are an output from the approved Test Year cost of service study. Hydro proposes to
16 use this same approach, using the Revised Test Year cost of service study, for Island Industrial

1 Customer rate design. For Hydro Rural Labrador Interconnected and Labrador Industrial
2 Transmissions customers, Hydro proposes to adjust customer rates by applying the percentage
3 change in Test Year revenue requirement for each class of service.

4
5 Hydro Rural rates would be required to change when Newfoundland Power's return changes to
6 ensure its customers receive the same rates as Newfoundland Power regardless of whether
7 Hydro changed its return on equity, so there would be no change in existing process for these
8 customers.

9
10 With an automatic update to Hydro's Test Year revenue requirement due to a change in the
11 return on equity from Newfoundland Power, the process for implementation of compliance
12 rates reflecting a Newfoundland Power GRA would be required to change. The compliance
13 application for Newfoundland Power would also need to reflect the revised supply cost from
14 Hydro as a result of any required change in the approved return on equity for Hydro. Therefore,
15 Hydro's compliance application in response to the establishment of a revised return on equity
16 would need to be filed prior to Newfoundland Power filing its application to establish customer
17 rates.

18

19 **5.0 Revisions to Excess Earnings Account Definition**

20 As Hydro's rate of return on rate base would be impacted by a change of return on equity,
21 Hydro would be required to revise its Excess Earnings Account definition to reflect the revised
22 rate of return on rate base.

23 **6.0 Implementation Process**

24 Hydro proposes that it would file an automatic adjustment application with the Board within 10
25 business days following the publication of a Board Order approving Newfoundland Power's
26 return on equity. Hydro's application would include the following:

- 27 • Revised Test Year weighted average cost of capital and rate of return on rate base to
28 reflect return on equity equal to that approved for Newfoundland Power;

- 1 • Finance schedules providing revised requirement from customer rates;
- 2 • Revised test year cost of service study identifying change in revenue requirement by
- 3 customer class;
- 4 • Derivation of revised customer rates;
- 5 • Revised Excess Earnings Account Definition; and
- 6 • Proposed revised schedule of rates, toll and charges.

7

8 **7.0 Conclusion**

9 Board Order No. P.U. 49(2016) directed Hydro to file a proposal in relation to an adjustment
10 mechanism for its target return on equity to reflect any future changes to Newfoundland
11 Power’s approved target return on equity for rate setting.¹ Hydro submits that the proposal
12 outlined in this document addresses the Board’s order and provides a reasonable approach by
13 which Hydro can ensure its Test Year return on equity reflected in customer rates remains the
14 same as that of Newfoundland Power.

¹ Page 24 of Order No. P.U. 49(2016).

*ROE Rate Change Deferral Account, Attachment 1
2017 GRA, Exhibit 12 - Automatic Return on Equity Adjustment
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**Appendix A
Page 1 of 1**

Sample Calculation of Revised Weighted Average Cost of Capital

Regulated Average Capital Structure	Test Year (%)
Debt	74.2
Asset retirement obligation	0.6
Employee future benefits	3.9
Equity	21.2
Total	100.0

Weighted Average Cost of Capital¹	Test Year (%)	Revised (%)
Embedded cost of debt	6.47	6.47
Asset retirement obligation	0.00	0.00
Employee future benefits	0.00	0.00
Equity	8.50	8.25
Weighted Average Cost of Capital	6.61	6.56

¹ Hydro's rate of return on rate base is equal to its approved weighted average cost of capital.

*ROE Rate Change Deferral Account, Attachment 1
2017 GRA, Exhibit 12 - Automatic Return on Equity Adjustment
Page 9 of 11*

**Appendix B
Page 1 of 3**

**Sample Finance Schedules
Newfoundland and Labrador Hydro
Financial Results and Forecasts
Statement of Income and Retained Earnings
(\$000s)**

	<u>Rate Setting</u> Test Year	<u>Automatic ROE</u> <u>Adjustment</u> (Year)	<u>Revised Rate</u> <u>Setting</u> Test Year
1 Revenue			
2 Energy sales	564,002	(964)	563,038
3 Revenue deficiency	-	-	-
4 Other revenue	2,508	-	2,508
5 Total revenue	<u>566,510</u>	<u>(964)</u>	<u>565,546</u>
6			
7 Expenses			
8 Operating expenses	131,350	-	131,350
9 Other Income and expense	4,074	-	4,074
10 Fuels	187,464	-	187,464
11 Power purchases	62,827	-	62,827
12 Amortization	63,230	-	63,230
13 Accretion of asset retirement obligation	748	-	748
14 Interest	89,453	-	89,453
15 Total expenses	<u>539,145</u>	<u>-</u>	<u>539,145</u>
16			
17 Net income	<u>27,364</u>	<u>(964)</u>	<u>26,400</u>
18			
19 Retained earnings			
20 Balance at beginning of year	259,556	-	259,556
21 Opening adjustment - retained earnings	-	-	-
22 Dividends	-	-	-
23 Balance at end of year	<u>286,920</u>	<u>(964)</u>	<u>285,956</u>

*ROE Rate Change Deferral Account, Attachment 1
2017 GRA, Exhibit 12 - Automatic Return on Equity Adjustment
Page 10 of 11*

**Appendix B
Page 2 of 3**

**Sample Finance Schedules
Newfoundland and Labrador Hydro
Financial Results and Forecasts
Rate of Return on Rate Base
(\$000s)**

	<u>Rate Setting</u> Test Year	<u>Automatic ROE</u> <u>Adjustment</u> (Year)	<u>Revised Rate</u> <u>Setting</u> Test Year
1 Property, plant, and equipment	1,882,883	-	1,882,883
2 add: accumulated depreciation	204,001	-	204,001
3 add: contributions in aid of construction	17,936	-	17,936
5 less: work in progress	(240,977)	-	(240,977)
6 Capital assets in service	<u>1,863,843</u>	-	<u>1,863,843</u>
7 less: asset retirement obligation	(12,169)	-	(12,169)
8 less: contributions in aid of construction	(17,936)	-	(17,936)
9 less: accumulated depreciation	(203,834)	-	(203,834)
10 Capital assets - current year	<u>1,629,904</u>	-	<u>1,629,904</u>
11 Capital assets - previous year	<u>1,610,437</u>	-	<u>1,610,437</u>
12 Unadjusted capital assets - average	1,620,170	-	1,620,170
13 less: Average net assets not in use	(7,318)	-	(7,318)
14 Capital assets - average	<u>1,612,852</u>	-	<u>1,612,852</u>
15			
16 Cash working capital allowance	7,037	-	7,037
17 Fuel	47,398	-	47,398
18 Materials and supplies	27,402	-	27,402
19 Deferred charges	95,132	-	95,132
20 less: Deferred Charges not in use	(4,467)	-	(4,467)
21			-
22 Average rate base	<u><u>1,785,353</u></u>	-	<u><u>1,785,353</u></u>
23			
24 Unadjusted return on regulated equity	27,364	(964)	26,400
25 add: Cost of service exclusions	1,177	-	1,177
26 Interest	89,453	-	89,453
27 Return on rate base	<u><u>117,994</u></u>	<u><u>(964)</u></u>	<u><u>117,030</u></u>
28			
29 Rate of return on rate base	<u><u>6.61%</u></u>	<u><u>-0.05%</u></u>	<u><u>6.56%</u></u>

*ROE Rate Change Deferral Account, Attachment 1
2017 GRA, Exhibit 12 - Automatic Return on Equity Adjustment
Page 11 of 11*

**Appendix B
Page 3 of 3**

**Sample Finance Schedules
Newfoundland and Labrador Hydro
Financial Results and Forecasts
Capital Structure
(\$000s)**

	<u>Rate Setting</u> Test Year	<u>Automatic ROE</u> <u>Adjustment</u> (Year)	<u>Revised Rate</u> <u>Setting</u> Test Year
1 Regulated capital structure			
2 Long-term debt	1,649,544	-	1,649,544
3 Promissory notes	-	-	-
4 Promissory notes - related party	-	-	-
5 less: sinking funds	(238,850)	-	(238,850)
6 add: mark to market of sinking funds	31,071	-	31,071
7	<u>1,441,765</u>	-	<u>1,441,765</u>
8 Cost of service exclusions	-	-	-
9 Non-regulated debt pool	(8,187)	-	(8,187)
10 Net regulated debt	1,433,578	-	1,433,578
11 Asset retirement obligation	20,740	-	20,740
12 less: unfunded asset retirement obligation	(8,493)	-	(8,493)
13 Employee future benefits	72,454	-	72,454
14 Contributed capital	100,000	-	100,000
15 Retained earnings cost of service exclusions	2,154	-	2,154
16 Retained earnings	286,920	(964)	285,956
17 Total	<u>1,907,353</u>	<u>(964)</u>	<u>1,906,389</u>
18			
19 Regulated capital structure (%)			
20 Debt	75.2%	-	75.2%
21 Asset retirement obligation	0.6%	-	0.6%
22 Employee future benefits	3.8%	-	3.8%
23 Equity	20.4%	-	20.4%
24 Total	<u>100.0%</u>	<u>-</u>	<u>100.0%</u>
25			
26 Regulated average capital structure (%)			
27 Debt	74.2%	-	74.2%
28 Asset retirement obligation	0.6%	-	0.6%
29 Employee future benefits	3.9%	-	3.9%
30 Equity	21.2%	-	21.2%
31 Total	<u>100.0%</u>	<u>-</u>	<u>100.0%</u>
32			
33 Weighted average cost of capital (WACC)			
34 Embedded cost of debt	6.47%	-	6.47%
35 Asset retirement obligation	0.00%	-	0.00%
36 Employee future benefits	0.00%	-	0.00%
37 Equity	8.50%	-0.25%	8.25%
38 WACC	<u>6.61%</u>		<u>6.56%</u>

Attachment 2

ROE Rate Change Deferral Account Definition
(Proposed Amendments)



Newfoundland and Labrador Hydro Return on Equity (ROE) Rate Change Deferral Account

Purpose

As per Board Order No. P.U. 49(2016), Newfoundland and Labrador Hydro's (Hydro's) target Return on Equity (ROE) percentage must be adjusted as required to equal the ROE approved for Newfoundland Power. The purpose of the ROE Rate Change Deferral Account is to defer recovery of the change in test year revenue requirement that will occur due to the customer rate implementation date differing from the effective date of the approved ROE percentage.

Methodology

As a result of changes in the ROE percentage between test years, the methodology originally filed as Sections 1 to 5 of Exhibit 12 to the 2017 GRA filing and included as Attachment 1 will be used in determining the change in revenue requirement by rate class and rate design.

Rate Implementation Process

The implementation process for changing customer rates that result from ROE revenue requirement adjustments shall include:

- a) an application by Hydro to change rates for Hydro Rural Labrador Interconnected and Labrador Interconnected Industrial Customers reflecting the allocated revised test year revenue requirement based on the effective date of revised test year ROE;
- b) proposals by Hydro to change rates for Newfoundland Power and Island Industrial Customers reflecting the revised test year ROE revenue requirements to accompany Hydro's applications for the July 1 rate adjustments.

Balance Accumulation

The annual ROE revenue requirement adjustments for Newfoundland Power and Island Industrial Customers reflecting the revised test year ROE percentage will be converted to monthly revenue requirement adjustments to be recorded in the ROE Rate Change Deferral Account for each month of delayed rate implementation.

If the effective date of revised customer rates on the Labrador Interconnected System is subsequent to the effective date of the approved revised test year ROE, Hydro will record the test year revenue requirement impacts of delayed rate implementation in the ROE Rate Change Deferral Account.

Disposition

On March 31 of each year, the balance attributable to Newfoundland Power will be transferred to the Utility Customer Balance in the Supply Cost Variance Deferral Account (SCVDA) for disposition according to the rules approved for this account.

On March 31 of each year, the balance attributable to Island Industrial Customers will be transferred to the Industrial Customers Balance in the SCVDA for disposition according to the rules approved for this account.

Any balances related to Labrador Interconnected customers will be proposed for disposition at Hydro's next General Rate Application.

Attachment 3

Excess Earnings Account Definition (Proposed Amendments)



**Newfoundland and Labrador Hydro
Excess Earnings Account**

Definition of Excess Earnings Account

This account shall be credited with excess earnings in the event the result of the following formula is greater than zero:

$$A - (B \times C)$$

Where:

- A = Actual return on rate base, calculated as net interest expense, plus net income, plus cost of service exclusions
- B = Actual average rate base, December 31
- C = Upper limit of return on rate base, defined as Test Year Return on Rate Base + 20 basis points

The disposition of any balance in the account is to be determined by the Board.

The upper limit return on rate base for 2018 and 2019 are presented in the following table.

	2018	2019	2019 Revised
Approved Return on Rate Base	5.50%	5.43%	5.45%
Upper Limit Range	0.20%	0.20%	0.20%
Upper Limit Return on Rate Base	5.70%	5.63%	5.65%

Affidavit



IN THE MATTER OF the *Electrical Power Control Act, 1994*, SNL 1994, Chapter E-5.1 (“EPCA”) and the *Public Utilities Act*, RSNL 1990, Chapter P-47 (“Act”), and regulations thereunder; and

IN THE MATTER OF an application by Newfoundland and Labrador Hydro (“Hydro”) for an Order approving Hydro’s target return on equity (“ROE”) and revisions to Hydro’s ROE Rate Change Deferral Account and Excess Earnings Account definitions pursuant to Sections 58 and 80 of the Act.

AFFIDAVIT

I, Dana Pope, of St. John’s in the province of Newfoundland and Labrador, make oath and say as follows:

- 1) I am Vice President, Regulatory Affairs and Stakeholder Relations for Newfoundland and Labrador Hydro, the applicant named in the attached application.
- 2) I have read and understand the foregoing application.
- 3) To the best of my knowledge, information, and belief, all of the matters, facts, and things set out in this application are true.

SWORN at St. John’s in the province of Newfoundland and Labrador this 29th day of January 2025, before me:



Barrister, Newfoundland and Labrador
Witnessed through the use of audio-visual technology
in accordance with the *Commissioners for Oaths Act*
and *Commissioners for Oaths Regulations*



Dana Pope, CPA (CA), MBA