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May 14, 2024

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

Attention: Jo-Anne Galarneau
Executive Director and Board Secretary

Dear Ms. Galarneau:

Re: Newfoundland Power's 2024 Rate of Return on Rate Base Application

A. The Application

In Order No. P.U. 3 (2022), the Board of Commissioners of Public Utilities (the "Board") ordered Newfoundland Power Inc. ("Newfoundland Power" or the "Company") to file an application on or before November 15, 2023 for approval of the Company's 2024 forecast average rate base and rate of return on rate base maintaining the common equity ratio and return on common equity established for ratemaking purposes.

On November 9, 2023, the Company filed a *2025/2026 General Rate Application* which sought the approval of Newfoundland Power's 2024 forecast average rate base and rate of return on rate base.

By way of a letter dated November 17, 2023, the Board directed the Company to file a separate application relating to approval of its 2024 forecast average rate base and rate of return on rate base.

On November 23, 2023, Newfoundland Power filed an application for approval of the Company's 2024 forecast average rate base and rate of return on rate base (the "Application") made in compliance with Order No. P.U. 3 (2022) and the Board's direction of November 17, 2023.

The Application proposes that the Board approve an overall average increase in current customer rates of 1.5%, effective July 1, 2024, based upon:

(i) a forecast average rate base for 2024 of $1,360,058,000;

(ii) a rate of return on average rate base for 2024 of 6.85% in a range of 6.67% to 7.03%; and

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(iii) forecast revenue requirements from customer rates for 2024 of $711,080,000, representing a $11,835,000 increase to the ratemaking 2023 revenue requirement approved by the Board in Order No. P.U. 3 (2022), to reflect the revised 2024 forecast average rate base and rate of return on rate base.

Based on a customer rate implementation date of July 1, 2024, the proposals result in a forecast revenue shortfall in 2024 of $6,722,000. The Application proposes deferred cost recovery of the 2024 revenue shortfall, with its disposition being subject to a future order of the Board.

B. Regulatory Process

The Application has been subject to a comprehensive public written hearing process, summarized below.

- On November 28, 2023, Newfoundland Power filed additional information as requested by the Board in correspondence dated November 17, 2023.

- On December 21, 2023, the Company filed responses to 36 Requests for Information (“RFIs”) submitted by the Board, the Consumer Advocate and Newfoundland and Labrador Hydro (“Hydro”).

- On January 26, 2024, Newfoundland Power filed responses to an additional 27 RFIs filed by the parties. On February 9, 2024, the Company filed revisions to six of the RFIs to include requested 2023 actual financial data.

- On April 5, 2024, Grant Thornton LLP (“Grant Thornton”) filed a report on the Application (the “Grant Thornton Report”). On April 26, 2024, Grant Thornton responded to two RFIs submitted by the Consumer Advocate on the Grant Thornton Report.

- On May 7, 2024, Hydro and the Consumer Advocate filed comments on the Application (“Hydro’s Comments” and the “Consumer Advocate’s Comments,” respectively).

In its April 30, 2024 correspondence, the Board set today’s date for Newfoundland Power’s final comments associated with the Application.

Section C of this submission provides a summary of the justification of the Application. Section D provides Newfoundland Power’s reply to Hydro’s and the Consumer Advocate’s comments. Section E concludes the Company’s final comments on the Application.

C. Summary of Justification for the Application

The following summarizes the justification for the Board's approval of the Application.

The Application complies with Order No. P.U. 3 (2022) and is consistent with prior orders of the Board.

Newfoundland Power has proposed that the Board approve its 2024 forecast average rate base and rate of return on rate base, in compliance with Order No. P.U. 3 (2022). The Application follows the established approach for prior rate of return on rate base applications, including those approved by the Board for the 2015, 2018 and 2021 forecast years in Order Nos. P.U. 51 (2014), P.U. 41 (2017) and P.U. 36 (2020), respectively.

The Grant Thornton Report found that "*…nothing has come to our attention that would suggest that [the Application] is not in compliance with past Board Orders.*"[1] Further, Grant Thornton did not note any discrepancies in the clerical accuracy of the 2024 forecast average rate base, 2024 rate of return on regulated rate base, or 2024 regulated return on rate base calculations.

The proposed revisions to the 2023 ratemaking revenue requirement and customer rates are consistent with prior board orders and past regulatory practice.

The Application proposes an $11.8 million increase to the 2023 ratemaking revenue requirement, which reflects the 2024 forecast average rate base and rate of return on rate base proposed in the Application. Revising customer rates to collect the additional revenue requirement is consistent with Order No. P.U. 13 (2013) and past practice of the Board.

When return on rate base applications in their current format were first required by the Board in Order No. P.U. 13 (2013), the Board provided that the Company may file for approval of a revised *Schedule of Rates, Tolls and Charges* to reflect the revisions required by the order.[2] Prior to 2013, in years when the Company's return on rate base was established by use of the Automatic Adjustment Formula, the Board's practice was to revise customer rates when the forecast just and reasonable return on rate base was outside the range of return on rate base established by the Board.

Deferred cost recovery of the 2024 revenue shortfall of $6.7 million is also consistent with past practice of the Board.[3]

1 See the Grant Thornton Report, page 3.
2 See Order No. P.U. 13 (2013), page 57, lines 23-24.
3 See the response to Request for Information NLH-NP-015 and Newfoundland Power's *2025/2026 General Rate Application, 3.5 Regulatory Amortizations.*

***The Application is consistent with the* Public Utilities Act *and the* Electrical Power Control Act, 1994.**

The *Public Utilities Act* (the "Act") provides that a public utility is entitled to earn a just and reasonable return on its rate base in each year.[4] The *Electrical Power Control Act, 1994* ("EPCA") provides that customer rates approved by the Board should provide sufficient revenue for a utility to enable it to earn the just and reasonable return as construed under the Act so that it is able to achieve and maintain a sound credit rating in the financial markets of the world.[5]

Newfoundland Power's 2024 existing forecast (i.e. without approval of the Application proposals) provides for a revenue deficiency of $12.6 million.[6] The Company's 2024 existing forecast rate of return on rate base is 6.21%, which is 64 basis points below the 6.85% regulated rate of return on rate base established by the Application. This result is 46 basis points beyond the bottom of the ±18 basis point range established by the Board. Accordingly, cost recovery is required for the Company to have an opportunity to earn a just and reasonable return in 2024 in accordance with section 80 of the Act.

With cost recovery of the $11.8 million proposed in the Application, Newfoundland Power's 2024 rate of return on rate base is forecast to be 6.82%, three basis points lower than the 2024 regulated rate of return on rate base of 6.85%. This result is within the ±18 basis point range currently approved by the Board.

Cost recovery associated with the Application proposals is required to maintain the Company's sound credit rating as required by the EPCA. In its April 30, 2024 Credit Opinion on Newfoundland Power (the "Moody's Report"), Moody's Investor Services ("Moody's") states:

> *"The stable outlook reflects our expectation that the company will continue to recover its costs and earn its allowed returns in a timely fashion…"*[7]

Moody's also provided the following with respect to factors that could lead to a downgrade of Newfoundland Power's credit rating:

> *"A decline in regulatory support including for example delays in recovering costs or an inability to earn allowed returns."*[8]

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4 See section 80 of the Act.
5 See section 3(a)(iii) of the EPCA.
6 See the response to Request for Information PUB-NP-016.
7 See the Moody's Report, page 2, filed with the Board as part of the Company's *2025/2026 General Rate Application* on May 2, 2024.
8 Ibid.

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The Grant Thornton Report found that nothing had come to Grant Thornton's attention that would suggest that the Application is not in compliance with the methodology and approach referenced in sections 78 and 80 of the Act.[9]

D. Reply to Hydro's and the Consumer Advocate's Comments

The following section provides Newfoundland Power's reply to Hydro's and the Consumer Advocate's comments on the Application, as filed on May 7, 2024.

Reply to Hydro's Comments

In its comments on the Application, Hydro concludes that: *"…Newfoundland Power should continue to earn within the currently approved range, and approval should not be granted to update the average rate base outside of a test year."*[10] The "currently approved range" referred to by Hydro is Newfoundland Power's 2023 test year range of rate of return on rate base.

Hydro's conclusion fails to recognize that Order No. P.U. 3 (2022) requires Newfoundland Power to file an application for approval of its 2024 forecast average rate base and rate of return on rate base. Suggesting that the Company use its 2023 range of rate of return on rate base for 2024 ignores the requirement imposed by the Board for the determination of a 2024 range.

Hydro's conclusion also fails to recognize prior orders of the Board which approved Newfoundland Power's rate of return on rate base applications for the 2015, 2018 and 2021 forecast years, respectively.[11] In each of those orders, the Board approved the Company's regulated rate of return on rate base for the *forecast year*, distinct from the preceding test year rate of return on rate base.

As an example, in Order No. P.U. 51 (2014), the Board approved Newfoundland Power's 2015 rate of return on rate base of 7.50% in a range of 7.32% to 7.68%.[12] This Order recognized that the 2014 test year rate of return on rate base, approved by the Board in the Company's prior general rate application, was not relevant to the 2015 year. Newfoundland Power's 2015 actual rate of return on rate base was assessed against the forecast rate of return on rate base approved in Order No. P.U. 51 (2014), not the 2014 test year rate of return on rate base.[13]

Newfoundland Power submits that Hydro's conclusion as outlined in its comments dated May 7, 2024 reflects a misunderstanding of the established practice for determining forecast rate of

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9 See the Grant Thornton Report, page 3.
10 See page 3 of Hydro's Comments.
11 See Order Nos. P.U. 51 (2014), P.U. 41 (2017) and P.U. 36 (2020).
12 See Order No. P.U. 51 (2014), page 2.
13 See *Annual Return 13: Return on Average Rate Base & Determination of Excess Earnings* for the 2015 year filed with the Board on April 1, 2016.

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return on rate base. As such, the Company submits that it is not relevant to the Board's consideration in making its determination on the Application.

Reply to the Consumer Advocate's Comments

The Consumer Advocate recommends that the Board deny the cost recovery proposed in the Application.[14] In support of its recommendation, the Consumer Advocate provides that it would be inappropriate to increase customer rates outside of a general rate application and emphasizes that without cost recovery, Newfoundland Power's 2024 forecast rate of return on rate base is 6.21%, which is within the 2023 test year range of return on rate base of 6.21% to 6.57%.[15]

Like Hydro, the Consumer Advocate disregards the Board's direction in Order No. P.U. 3 (2022) and the process established and upheld by prior orders of the Board for rate of return on rate base applications.[16] Further, the Consumer Advocate's Comments do not acknowledge the requirements of the Act and the EPCA,[17] or the Board's commentary in Order No. P.U. 13 (2013) with respect to the ability to revise customer rates resulting from rate of return on rate base applications.[18]

The Consumer Advocate also provides the following comments to support its recommendation:

> *"…Newfoundland Power is requesting a rate increase between regulatory cycles to ensure it realizes its approved rate of return on equity regardless of performance; e.g., failure to contain growth in costs."*[19]

and,

> *"The table makes it clear that, in effect, all of the proposed increases in the return on rate base…is to be accomplished through an increase in the Return on Equity. The overriding intent of the Application is to accomplish that increase in the return on equity by raising average customer rates by 1.5%."*[20]

Both statements are inaccurate. The Application only considers the change in the return on rate base component of Newfoundland Power's ratemaking revenue requirement.[21] The proposed $11,835,000 increase to the 2023 test year revenue requirement is comprised of: (i) a $8,555,000 increase in return on debt; (ii) a $2,296,000 increase in return on equity; and (iii) a $984,000

14 See the Consumer Advocate's Comments, recommendations one and two, page 14.
15 Ibid., pages 2 and 3.
16 See the discussion on page 5 of this submission.
17 See the discussion on page 4 of this submission.
18 See the discussion on page 3 of this submission.
19 See the Consumer Advocate's Comments, page 4.
20 Ibid, page 5.
21 This is in compliance with the Board's direction in Order No. P.U. 3 (2022).

increase in associated income taxes.[22] The Application proposals do not include any change in Newfoundland Power's other costs, such as operating costs or depreciation expense. Changes in these components of the Company's revenue requirement and customer rates are only considered in connection with a general rate application.

The limited scope of the Application was recognized by the Chair of the Board during the pre-hearing conference for Newfoundland Power's *2025/2026 General Rate Application:*

> *"It's a single item review of costs that was approved by the Board to be when costs were outside of a certain range to come back with an application, so the review of that proceeding will be strictly on that matter alone and not on the overall cost management of the utility, so similar to the July 1st rate changes, but it would get due diligence and review and make sure it's complying with the Board's requirements before it's passed through."*[23]

The Consumer Advocate's Comments suggest how Newfoundland Power may be able to manage its \$12.6 million revenue deficiency in 2024 without cost recovery.[24] This includes reducing its operating, depreciation and finance costs, as well as the possibility of higher sales.

First, it is important to recognize the materiality of the Company's 2024 forecast revenue deficiency of \$12.6 million. Newfoundland Power's ±18 basis point range on rate of return on rate base translates, in dollars, to approximately ±\$3.6 million in 2024.[25] The Company's 2024 forecast revenue deficiency is 3.5 times larger than its range of return on rate base.[26] As such, an expectation for Newfoundland Power to manage its 2024 forecast revenue deficiency without cost recovery is not reasonable, nor is it consistent with the Act, the EPCA, or past practice of the Board.

Newfoundland Power's 2024 forecast operating costs reflect its work requirements in 2024, as well as inflationary cost pressures from 2023 levels.[27] While the Company has greater flexibility with its operating costs than with any other component of its revenue requirement, the overall impact of a reduction in operating costs is limited.[28] Further, there are annual risks to operating costs, which can result in actual operating costs being higher than forecast – for example, storm costs and higher than anticipated inflationary cost pressures.

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22 See Appendix C to the *2024 Rate of Return on Rate Base Report* filed with the Application.
23 See the transcript of the pre-hearing conference held on February 1, 2024 in relation to the Company's *2025/2026 General Rate Application*, page 20.
24 See pages 8 to 12 of the Consumer Advocate's Comments.
25 See Schedule B, page 2, Table 1 of Newfoundland Power's correspondence *Re: 2024 Rate of Return on Rate Base Application – Additional Information*, filed with the Board on November 28, 2023.
26 \$12.6 million ÷ \$3.6 million = 3.5 times.
27 See the response to Request for Information PUB-NP-013.
28 For example, 1% of 2024 forecast gross operating costs is \$768,380. See Attachment B to the response to Request for Information NLH-NP-011. This compares to a total 2024 forecast revenue deficiency of \$12.6 million.

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With respect to managing its depreciation and finance costs, the Consumer Advocate suggests that Newfoundland Power could reduce its 2024 capital expenditures. The Company's 2024 capital expenditures were approved by the Board in Order No. P.U. 2 (2024) and are necessary to provide customers with safe, reliable power in a least-cost manner. The Consumer Advocate acknowledges the limitations in Newfoundland Power's ability to reduce these costs in 2024.[29]

Finally, the Consumer Advocate suggests that the Company can expect sales growth in 2024 beyond that contained in its forecast.[30] As provided in the response to Request for Information PUB-NP-014, factors that led to an increase in actual sales in 2023 as compared to the 2023 test year forecast, such as government electrification initiatives, are now incorporated into Newfoundland Power's 2024 sales forecast.[31] In addition, population growth is expected to slow in 2024, and increases in electricity prices in 2023 and 2024 are expected to negatively impact sales in 2024.[32] Further, the Company's 2024 actual sales year-to-date are consistent with its 2024 sales forecast.[33]

In addition to denial of cost recovery, the Consumer Advocate recommends that the Board order Newfoundland Power to reduce its 2024 forecast average rate base by $1 million based on the Board's determinations in Order No. P.U. 2 (2024) (the "2024 CBA Order").[34]

The Application contains the best available information at the time of its filing. Due to the length of the public written hearing process, intervening events occur which may alter the underlying information contained in an application. These intervening events may result in required adjustments to application proposals, either upward or downward.[35]

In the case of this Application, two intervening events occurred subsequent to the filing of the Application: (i) the 2024 CBA Order was issued by the Board, approving a capital budget of $1 million less than proposed by the Company in its *2024 Capital Budget Application*; and (ii) Newfoundland Power's 2023 fiscal year concluded. The Company's 2023 year-end financials provide that its 2023 actual rate base was $1,312.9 million,[36] which is $0.8 million higher than the

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29 See Consumer Advocate's Comments, page 8.
30 See Consumer Advocate's Comments, pages 10-11.
31 See the response to Request for Information of PUB-NP-014, part f).
32 Ibid.
33 Compared to the sales forecast underpinning the 2024 financial forecast included in the Application, actual sales are 0.7% lower on a total basis, year-to-date, April 30, 2024. Domestic sales are consistent with the forecast (a 0.0% variance), while commercial and street lighting sales are 2.0% and 0.2% lower than forecast, respectively. Approximately 45% of Newfoundland Power's sales occur in the first four months of the year, due to the colder weather during that timeframe.
34 See page 15 of the Consumer Advocate's comments, recommendation three.
35 This is typically resolved through a compliance application following an order by the Board.
36 See *Annual Return 3: Computation of Average Rate Base* for the 2023 year filed with the Board on March 28, 2024.

2023 forecast rate base of $1,312.1 million used to determine the 2024 forecast average rate base in the Application.[37]

If the 2024 forecast average rate base was revised for both the 2024 CBA Order and the 2023 actual rate base, it would be roughly $0.3 million higher.[38] In Newfoundland Power's view, this is not a material amount and therefore no revision to the 2024 forecast average rate base proposed in the Application is necessary.

Finally, the Consumer Advocate recommends that the Board deal with the disposition of the 2023 excess earnings separately from this Application.[39] Newfoundland Power's Application does not contain any proposals associated with the disposition of the 2023 excess earnings balance, as the Application was filed prior to the 2023 fiscal year end, when amounts were not known. Accordingly, the Company takes no particular exception to the Consumer Advocate's recommendation on this matter.

Newfoundland Power does observe that the Board considered options of how to dispose of the 2023 excess earnings balance in Requests for Information PUB-NP-007 and PUB-NP-019 (1st Revision). As such, in the Company's view, it would be reasonable for the Board to provide its direction on the disposition of the 2023 excess earnings balance in its order on this Application.

E. Conclusion

The Application complies with Order No. P.U. 3 (2022) and is consistent with the established approach of the Board and its prior orders. The proposed revisions to the 2023 ratemaking revenue requirement and customer rates are consistent with section 80 of the Act, section 3(a)(iii) of the EPCA, prior board orders and past regulatory practice.

The conclusions and recommendations of both Hydro and the Consumer Advocate disregard the Board's direction in Order No. P.U. 3 (2022). Further, the comments of both parties fail to recognize the legislative requirement that customer rates should yield revenue that is sufficient for Newfoundland Power to have an opportunity to earn a just and reasonable return.

Accordingly, the Company requests that the Application be approved as filed to allow for the implementation of the proposed customer rates on July 1, 2024.

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37 See Appendix A to the *2024 Rate of Return on Rate Base Report* filed with the Application.

38 The $0.8 million higher rate base in 2023 would result in a full year impact to the 2024 average rate base calculation. The $1 million lower rate base in 2024 would result in a half year, or a $0.5 million, impact to the 2024 average rate base calculation. The net impact to the 2024 average rate base calculation is therefore a $0.3 million increase.

39 See the Consumer Advocate's Comments, recommendation four, page 15.

Newfoundland Power notes that as of the date of this submission, only six weeks remain before the proposed July 1, 2024 implementation date. In order to revise its customer rates on July 1, 2024, the Company would require direction from the Board on or about May 31, 2024. If direction is not received by that timeframe, the Company submits that implementing the customer rate change at the next possible date (e.g. August 1st or September 1st) is reasonable.

If you have any questions, please contact the undersigned.

Yours truly,

Lindsay Hollett

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