

1 Q. **Reference: Cost Relationship to Changes in Newfoundland Power’s Return on Equity**

2 Please confirm and explain if a change in the return on equity set for Newfoundland Power will
3 impact the costs incurred by Hydro under the Muskrat Falls agreements, specifically the
4 purchased power expense of Hydro, including a reference to any relevant contractual terms.

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7 A. There are no impacts on costs incurred by Newfoundland and Labrador Hydro (“Hydro”) with
8 respect to the Muskrat Falls Hydroelectric Generating Station or the Labrador Transmission
9 Assets pursuant to the Muskrat Falls Power Purchase Agreement¹ should there be a change in
10 the Return on Equity (“ROE”) set for Newfoundland Power Inc. (“Newfoundland Power”).

11 Any change in the ROE set for Newfoundland Power will impact the Rate of Return on Equity
12 (“RROE”) as defined by the Transmission Funding Agreement (“TFA”).² This will change the
13 prospective annual return on the undepreciated capital assets and the undepreciated sustaining
14 costs included in the TFA payments by Hydro, in accordance with the following contract terms:

- 15 ● The TFA between Labrador-Island Link Limited Partnership (“Partnership”), Labrador-
16 Island Link Operating Corporation (“Opco”), and Hydro is the agreement that obligates
17 Hydro to pay for the usage of the Labrador-Island Link (“LIL”) and associated assets
18 owned by the Partnership.
- 19 ● Under Article 3 of the TFA,³ Hydro is required to make payments which are comprised
20 of, amongst other things, the payment of rent to Opco. Rent includes, amongst other
21 things, the payment of an annual return on any undepreciated capital assets associated
22 with the LIL, as well as any undepreciated sustaining costs.

¹ “Power Purchase Agreement,” Newfoundland and Labrador Hydro and Muskrat Falls Corporation, November 29, 2013.

² “Transmission Funding Agreement,” Labrador-Island Link Limited Partnership, Labrador-Island Link Operating Corporation, and Newfoundland and Labrador Hydro, November 29, 2013.

³ *Supra*, f.n. 2, Article 3 at pp. 23–27 of 57.

- 1 • The annual rate of return is calculated by applying an annual return on the sum of the
2 undepreciated capital asset plus undepreciated sustaining costs. The annual rate of
3 return is determined by calculating:
- 4 a) The actual annual cost of the debt owed by the Partnership as a percentage; plus
5 b) The RROE⁴ applicable from time to time, averaged as appropriate and subject to a
6 minimum value to achieve the debt service coverage ratio agreed in the financing
7 documents.
- 8 both weighted according to the debt-to-equity ratio to determine the appropriate rate.
- 9 • The RROE to be earned by the Partnership in respect of any Fiscal Year shall be
10 determined in accordance with the following principles and shall be changed
11 whenever a reference rate of return is made effective by the PUB or other
12 Authorized Authority, with the prior reference rate of return applying during the
13 part of the Fiscal Year before the change and the new reference rate of return
14 applying during the portion of the Fiscal Year after the change:
- 15 i. If during such Fiscal Year there is only one privately-owned regulated
16 electrical utility in NL, the RROE shall be equal to the rate of after tax-
17 return on equity approved by the PUB in respect of such utility for such
18 Fiscal Year; and
- 19 ii. If during such Fiscal Year there is more than one privately-owned
20 regulated electrical utility in NL, the RROE shall be the average of the
21 rates of after-tax return on equity approved by the PUB in respect of all
22 such utilities for such Fiscal Year.⁵
- 23 In conclusion, any change to the ROE set for Newfoundland Power would impact the costs
24 incurred by Hydro under the TFA. For further information, please refer to Hydro's response to
25 PUB-NLH-003 of this proceeding.

⁴ RROE means an annual after-tax rate of return expressed as a percentage to be earned by the Partnership. The rate of return shall be calculated in accordance with regulatory accounting principles as applied by the Board of Commissioners of Public Utilities ("Board of PUB") or other Authorized Authority as defined by the Partnership TFA.

⁵ *Supra*, f.n. 2, Article 3, Clause 3.9 at p. 27 of 57.