

1 **Section 3: Finance/Fair Return**
2

3 **Q. Further to PUB-NP-060, PUB-NP-061 and PUB-NP-062 above would any of the**
4 **credit metrics at the different returns on equity and equity components in the**
5 **capital structure have impacts on Newfoundland Power’s ability to maintain its**
6 **creditworthiness and its ability to maintain a sound credit rating?**
7

8 **A. A. Credit Ratings**
9

10 The maintenance of Newfoundland Power’s creditworthiness and its ability to maintain a
11 sound credit rating is not solely a matter of credit metrics.
12

13 The Company’s credit ratings are determined by Moody’s Investor Services (“Moody’s”)
14 and DBRS Morningstar (“DBRS”).¹ As each of the current credit ratings from Moody’s
15 and DBRS indicates, Newfoundland Power’s credit ratings are substantially influenced
16 by factors other than credit metrics.
17

18 Moody’s, for example, attributes 60% of its rating to: (i) the regulatory framework,
19 including legislation and the consistency and predictability of regulation; (ii) the ability to
20 recover costs and earn returns, including the timeliness of recovery of costs and
21 sufficiency of rates and returns; and (iii) diversification, including market position and
22 generation and fuel diversity. Moody’s explains:
23

24 *“For rate-regulated utilities, which typically operate as a monopoly, the*
25 *regulatory environment and how the utility adapts to that environment are the*
26 *most important credit considerations.”²*
27

28 In its most recent rating report for Newfoundland Power, Moody’s stated:
29

30 *“We view the Newfoundland and Labrador Board of Commissioners of Public*
31 *Utilities (PUB) as one of the more supportive regulators in Canada because*
32 *regulatory decisions are timely and balanced, deferral accounts reduce risks from*
33 *factors beyond management’s control and NPI’s 45% equity capital is among the*
34 *highest authorized levels in Canada.”³*
35

36 DBRS completes both a business risk assessment (“BRA”) and financial risk assessment
37 as part of its rating methodology. For regulated utilities, DBRS states:
38

39 *“The quality of the regulatory regime is typically the most important BRA factor,*
40 *as it lays the foundation for utilities’ earning capacity, cost recovery mechanisms,*
41 *and capital structure. A supportive regulatory framework contributes to stable*

¹ See the 2025/2026 General Rate Application, Volume 1, Application, Company Evidence and Exhibits, Exhibit 4.

² See Moody’s, *Regulated Electric and Gas Utilities, Rating Methodology*, June 23, 2017, page 6. This is provided as Attachment A in response to Request for Information CA-NP-081.

³ See the 2025/2026 General Rate Application, Volume 1, Application, Company Evidence and Exhibits, Exhibit 4, Moody’s, page 1.

1 *cash flow and earnings, underpinned by a fair rate of return and a full and timely*
2 *recovery of costs.”⁴*
3

4 In its most recent rating report, DBRS recognized the Company’s stable and supportive
5 regulatory environment and strong financial profile as key credit strengths.⁵ Further,
6 DBRS stated: “*Newfoundland Power has maintained a solid financial profile,*
7 *underpinned by its reasonable financial leverage and stable cash flow.*”⁶
8

9 It is clear that the credit rating agencies consider the existing supportive regulatory
10 environment as a credit strength for Newfoundland Power. Further, both rating agencies
11 recognize the Company’s longstanding 45% common equity component of its capital
12 structure as a key credit strength. A reduction in the 45% common equity ratio could
13 result in a re-evaluation of regulatory support by the rating agencies.
14

15 **B. Credit Metrics**

16 Both Moody’s and DBRS consider various credit metrics as part of their credit rating
17 methodologies. Moody’s assessment of financial strength primarily relies on the debt to
18 capitalization financial metric and various cash flow metrics.⁷ DBRS considers the debt
19 to capitalization financial metric in combination with cash flow and interest coverage
20 credit metrics.⁸
21

22 Moody’s 12 to 18-month forward view reflects a constant debt to capitalization financial
23 metric.⁹ A reduction in the Company’s 45% common equity ratio, as outlined in the
24 scenarios in Request for Information PUB-NP-061, would increase the debt to
25 capitalization financial metric and could result in a re-evaluation of financial strength by
26 Moody’s when assessing the Company’s rating outlook.¹⁰
27

28 Both Moody’s and DBRS consider the Company’s 45% common equity ratio and cash
29 flow to debt coverage credit metric in their commentary on the Company’s rating
30 outlook.
31

32 In considering the ratings outlook for Newfoundland Power, Moody’s states:
33

34 *“The stable outlook reflects the PUB’s regulation of NPI which we consider*
35 *credit supportive. We expect the regulatory environment to remain supportive,*
36 *with the company maintaining a suite of timely recovery mechanisms, along with*
37

⁴ See DBRS, *Global Methodology for Rating Companies in the Regulated Utility and Independent Power Producer Industries*, January 2024, Page 5 of 28. This is provided as Attachment A in response to Request for Information CA-NP-082.

⁵ See the *2025/2026 General Rate Application, Volume 1, Application, Company Evidence and Exhibits, Exhibit 4, DBRS*, Page 2 of 14.

⁶ *Ibid*, DBRS, Page 2 of 14.

⁷ *Ibid*, Moody’s, page 9.

⁸ *Ibid*, DBRS, Page 2 of 14.

⁹ *Ibid*, Moody’s, page 9.

¹⁰ Conversely, an increase in the Company’s 45% common equity ratio, as outlined in the scenarios in Request for Information PUB-NP-062, could be viewed as a credit positive by Moody’s.

1 *our view that relatively stable cash flow generation and the capital structure of*
2 *NPI will generate sustained CFO pre-WC to debt in the 16-18% range.”¹¹*
3

4 Newfoundland Power’s cash flow metrics since 2020 have fluctuated, largely due to the
5 operation of the Energy Supply Cost Variance (“ESCV”) and the current wholesale rate
6 structure.¹² This cash flow volatility is expected to decrease following implementation of
7 a revised wholesale rate for Newfoundland Power reflecting commissioning of the
8 Muskrat Falls Project.
9

10 As provided in the response to Request for Information PUB-NP-060, rates of return on
11 equity (“ROEs”) ranging from 8.25% to 9.85% with a 45% common equity ratio,
12 excluding the impact of ESCV, generate cash flow to debt coverage consistent with the
13 range that Moody’s expects for Newfoundland Power.¹³
14

15 **C. Conclusion**

16

17 Newfoundland Power maintains investment grade credit ratings from Moody’s and
18 DBRS. These ratings reflect the supportive regulatory environment and the Company’s
19 stable financial performance, both of which are fundamentally supported by
20 Newfoundland Power’s longstanding capital structure that includes 45% common equity.
21 This has contributed to the Company’s continued access to capital markets on reasonable
22 terms.
23

24 In Newfoundland Power’s view, reducing the 45% common equity ratio represents a risk
25 to maintaining its existing credit ratings.
26

27 Further, in determining an appropriate ROE for the Company, the Board is guided by the
28 fair return standard. In Order P.U. 18 (2016), the Board stated:
29

30 *“In Order No. P.U. 43(2009) and in Order No. P.U. 13(2013), its most recent*
31 *Order on this issue, the Board stated that ‘to be considered fair the return must be*
32 *commensurate with the return on investments of similar risk and sufficient to*
33 *assure financial integrity and to attract necessary capital.’ This statement, which*
34 *reflects accepted regulatory principles, concisely captures the requirements that*
35 *must be met to determine a fair return. All three requirements must be met and no*
36 *one requirement takes precedence over the other two.”¹⁴*

¹¹ Ibid, Moody’s, page 2.

¹² Ibid, Moody’s, page 4. Moody’s states, “Financial metrics may fluctuate, however the variability is primarily a function of changes in long term regulatory assets and liabilities that is unlikely to be sustained over time...”

¹³ See also Table 5 in the response to Request for Information PUB-NP-061. Further, as provided in Table 5 in the response to Request for Information PUB-NP-061, excluding the impact of ESCV, ROEs ranging from 8.25% to 9.85% with equity components ranging from 45% to 50% generate cash flow to debt coverage within, or above, the range that Moody’s expects for Newfoundland Power.

¹⁴ See Order No. P.U. 18 (2016), page 10, line 44 to page 11, line 4.