Newfoundland & Labrador

BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

IN THE MATTER OF THE

2025-2026 GENERAL RATE APPLICATION

FILED BY

NEWFOUNDLAND POWER INC.

ORDER NO. P.U. 3(2025)

BEFORE:

Kevin Fagan
Chair and Chief Executive Officer

Dwanda Newman, LL.B.
Vice-Chair

John O'Brien, FCPA, FCA, CISA
Commissioner

NEWFOUNDLAND AND LABRADOR
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

ORDER NO. P.U. 3(2025)

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

IN THE MATTER OF an application by Newfoundland Power Inc. to establish customer electricity rates for 2025 and 2026.

BEFORE:

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1. DECISION SUMMARY

The Board does not accept the proposed overall average customer rate increase of 10.6% and directs Newfoundland Power to revise its proposals with respect to customer rates to be effective July 1, 2025, to reflect the determinations of the Board, addressing concerns in relation to rate increases and rate stability.

The Board directs that Newfoundland Power's revised proposals should reflect, among other things, the Board's findings with respect to reducing Operating Costs and a lower rate of return on equity than proposed.

Operating Costs

The Board directs Newfoundland Power to reduce its proposed Operating Costs by $2.0 million in 2025 and 2026 to reflect a productivity allowance to provide an incentive to Newfoundland Power to take additional measures to manage its costs and find efficiencies.

In addition to the productivity allowance, the Board directs Newfoundland Power to revise its proposals to exclude the costs associated with short-term incentive payments to the executive and directors.

Rate of Return on Equity

The Board does not accept the proposed increase in the rate of return on equity from 8.5% to 9.85% and directs Newfoundland Power to file a revised rate of return on rate base reflecting a rate of return on equity of 8.6%. The Board finds that Newfoundland Power's capital structure should continue to include a common equity component not exceeding 45%.

Balancing Cost and Reliability

The balance of cost and reliability was an important issue in this proceeding. The Board directs Newfoundland Power to develop a scope of work for the development of a strategic plan with respect to balancing cost and reliability, identifying issues and challenges that may have significant potential implications for its system and customers, such as electrification, climate change and aging infrastructure.

Regulatory Accounting Matters

The Board approves a number of revisions to Newfoundland Power's deferral accounts and the creation of a new deferral account to enable the recognition and amortization of costs over time periods consistent with regulatory principles.

Additional Reports to be filed

The Board directs Newfoundland Power to file additional reports/updates in relation to:

- Advanced Metering Infrastructure
- Its Load Research Study and the Rate Design Review
- Its supply cost recovery mechanisms
- Its Customer, Energy and Demand forecast methodology
- The method of calculating its rate of return on rate base
- Executive and director compensation

Compliance Application

The Board directs Newfoundland Power to file a compliance application to reflect the settlement agreements, the Board's determinations in this Decision and Order and in Order No. P.U. 16(2024) and Order No. P.U. 20(2024). This application will also reflect the flow-through of impacts associated with the revised wholesale rate from Hydro, as approved in Order No. P.U. 2(2025), and will incorporate the Rate Stabilization Account adjustment and Municipal Tax Adjustment Factor for July 1, 2025. Customer rate impacts will be determined following the review of the compliance application.

2. APPLICATION AND PROCEEDING

2.1. Application

Newfoundland Power Inc. ("Newfoundland Power") filed a general rate application with the Board of Commissioners of Public Utilities (the "Board") on November 9, 2023 requesting approval of Newfoundland Power's 2024 forecast average rate base and rate of return on rate base, as well as approval of Newfoundland Power's 2025 and 2026 Test Years revenue requirements.[1] On November 17, 2023, the Board directed Newfoundland Power to file a separate application for the 2024 rate of return and rate base proposals. On November 23, 2023, Newfoundland Power filed a 2024 Rate of Return on Rate Base Application.[2] On November 27, 2023 the Board further directed Newfoundland Power to file additional information with respect to its 2025/2026 General Rate Application.

On December 12, 2023 Newfoundland Power withdrew the 2025/2026 General Rate Application filed on November 9, 2023, and filed its 2025/2026 General Rate Application (the "Application"), which was revised in accordance with the directions of the Board. The Application proposed that the Board approve, among other things:

1. the amortization of a forecast 2024 revenue shortfall of approximately $6,722,000, and a forecast 2025 revenue shortfall of approximately $16,761,000, over a 30-month period, commencing July 1, 2025 and ending December 31, 2027;
2. rates, tolls, and charges and rules and regulations governing service, to be effective for all service provided on and after July 1, 2025, which result in an overall average increase in current customer rates of 5.5% and average increases in proposed customer rates by class as follows:

Rate Class	Average Increase
Domestic	5.5%
General Service 0-100kW (110 kVA)	5.5%
General Service 110-1000 kVA	5.4%
General Service 1000 kVA and Over	5.3%
Street and Area Lighting	5.9%

3. a rate of return on average rate base for 2025 of 7.40% in a range of 7.22% to 7.58% and for 2026 of 7.21% in a range of 7.03% to 7.39%;
4. a forecast average rate base for 2025 of $1,406,816,000 and for 2026 of $1,451,200,000;
5. a forecast revenue requirement from customer rates for 2025 of $768,770,000 and for 2026 of $789,602,000; and
6. the continued suspension of the automatic adjustment formula for setting the allowed rate of return on average rate base for Newfoundland Power in years subsequent to 2026.

[1] In Order No. P.U. 3(2022), the Board ordered Newfoundland Power to file its next general rate application no later than June 1, 2024.

[2] Newfoundland Power's 2024 Return on Rate Base Application was addressed through a separate process.

The Application was filed with comprehensive supporting materials which included written evidence, reports, and exhibits. Expert evidence for Newfoundland Power was prepared by James M. Coyne and John P. Trogonoski of Concentric Energy Advisors, Inc. in relation to cost of capital ("Concentric").

On December 13, 2023 Newfoundland Power filed the additional information requested by the Board.

2.2. Application Process

Notice of the Application and Pre-hearing Conference was published in newspapers throughout the province beginning on January 13, 2024.

A Pre-hearing Conference was held on February 1, 2024. In Order No. P.U. 5(2024) the Board identified intervenors, established procedural rules, and set the schedule for the proceeding.

Registered intervenors for the proceeding were the Government appointed Consumer Advocate, Dennis Browne, KC (the "Consumer Advocate"), Newfoundland and Labrador Hydro ("Hydro"), and the International Brotherhood of Electrical Workers, Local 1620 (the "IBEW").

On April 3, 2024 the Board entered, as part of the record in this proceeding, Hydro's 2023 Long-Term Load Forecast Report filed in the Reliability and Resource Adequacy Study Review.

On April 17, 2024 the Consumer Advocate filed expert evidence which included a report prepared by Dr. Laurence D. Booth of the Rotman School of Management, University of Toronto (the "Booth Report") and pre-filed evidence of consultant, C. Douglas Bowman.

On April 17, 2024 Newfoundland Power filed a report on executive compensation prepared by Wiclif Ma of Korn Ferry (CA) Ltd. (the "Korn Ferry Report").

On April 17, 2024 the Board's consultant, the Brattle Group (the "Brattle Group") filed its review of Newfoundland Power's load forecasting methodology (the "Brattle Group Load Forecasting Methodology Review"). On April 24, 2024 the Brattle Group filed its report on Newfoundland Power's Deferral Accounts (the "Brattle Group Deferral Accounts Report").

On April 24, 2024, Grant Thornton LLP ("Grant Thornton") filed a report with respect to its review of Newfoundland Power's pre-filed evidence (the "Grant Thornton Report"). On May 1, 2024 Grant Thornton filed a supplementary report (the "Grant Thornton Supplementary Report").

On May 11, 2024 notice of the hearing was published, inviting participation of interested parties or organizations.

Between May 21-24, 2024 the parties held settlement discussions, facilitated by Board Hearing Counsel.

On May 28, 2024 Newfoundland Power filed rebuttal evidence in response to the expert reports from the Brattle Group and C. Douglas Bowman, as well as rebuttal testimony prepared by Concentric.

On June 6, 2024, a settlement agreement between Newfoundland Power, the Consumer Advocate, Hydro, the IBEW, and Board Hearing Counsel was filed with the Board (the "Settlement Agreement"). The Settlement Agreement addressed a range of issues arising from the Application, including the automatic adjustment formula, matters of regulatory accounting, hearing costs, depreciation expense, and the Customer, Energy and Demand Forecast.

On June 12, 2024 a further settlement agreement was made between Newfoundland Power, Hydro, and the Consumer Advocate concerning the revision of Hydro's wholesale rate to Newfoundland Power (the "Wholesale Rate Agreement"). The Wholesale Rate Agreement detailed the agreement by Newfoundland Power and Hydro to apply to the Board to revise the wholesale rate charged by Hydro to Newfoundland Power effective January 1, 2025. It was agreed that Hydro would file its application on or about September 15, 2024, and that Newfoundland Power would file its flow-through application on the same date. The parties also agreed that the Board should order Newfoundland Power to rebase its power supply costs as part of its flow-through application.

A total of 759 Requests for Information ("RFIs") were filed and answered in the proceeding.

On June 13, 2024 the public hearing began as scheduled.[3] During the hearing the following witnesses testified:

<u>On behalf of Newfoundland Power:</u>
Gary Murray - President and Chief Executive Officer
Paige London - Vice President, Finance and Chief Financial Officer
James Coyne and John Trogonoski - Concentric Energy Advisors, Inc.
Wiclif Ma - Korn Ferry (CA) Ltd.
Byron Chubbs - Vice President, Engineering and Energy Supply
Michael Comerford - Director, Rates and Supply

<u>On behalf of the Consumer Advocate:</u>
Dr. Laurence D. Booth - Rotman School of Management, University of Toronto
C. Douglas Bowman - Regulatory Consultant

On July 9, 2024 the Board held a public participation day. One member of the public, Steve Kelland, attended and presented to the Board. The Board also received letters of comment from

[3] Testimony was heard June 13-14, 17-21, and 25-28, 2024.

the Island Industrial Customer Group,[4] the Canadian Federation of Independent Business, and eight members of the public.

On July 31, 2024 written submissions were filed by the Consumer Advocate and Hydro.

On August 8, 2024 Newfoundland Power filed a reply submission.

2.3. Revised Application Proposals

Newfoundland Power filed three additional applications with the Board while the Application was ongoing which had significant implications for the proposals in this Application.

On November 23, 2023 Newfoundland Power applied for approval of a 2024 forecast average rate base and rate of return on rate base and proposed an average 1.5% customer rate increase, effective July 1, 2024 and deferred cost recovery of a 2024 revenue shortfall of $6,722,000.[5] In Order No. P.U. 20(2024) the Board denied the proposed rate of return on rate base for 2024 and the proposed customer rate increase. The Board approved the recovery of a 2024 revenue shortfall associated with the approved rate of return on rate base through the use of the 2023 balance in the Excess Earning Account with the remaining shortfall to be deferred for future recovery through the rate stabilization account ("2024 Return on Rate Base Order").[6] The proposed revenue requirement for the 2025 and 2026 Test Years is impacted by this order.[7]

On June 12, 2024 Newfoundland Power applied for approval of a July 1, 2024 rate increase in the amount of 9.3% to reflect a change in the Rate Stabilization Account adjustment and a change in the Municipal Tax Adjustment Factor.[8] In Order No. P.U. 16(2024), the Board directed Newfoundland Power to reduce the customer rate increase to 7.0% and found that the unrecovered amount should remain in the Rate Stabilization Account for future recovery ("2024 RSA Order").[9] The Board's findings resulted in changes to the Rate Stabilization Account adjustment and the Municipal Tax Adjustment Factor, effective August 1, 2024, and did not have a material impact on the revenue requirement for the 2025 and 2026 Test Years.[10]

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[4] Corner Brook Pulp and Paper Limited, Braya Renewable Fuels (Newfoundland) LP, and Vale Newfoundland and Labrador Limited.

[5] In its 2022/2023 GRA Order, the Board required Newfoundland Power to file an application for approval of its 2024 forecast average rate base and rate of return on rate base.

[6] The findings in Order No. P.U. 20(2024) resulted in Newfoundland Power filing a compliance application, which was approved in Order No. P.U. 24(2024).

[7] Newfoundland Power Wholesale Rate Flow-Through Application, Response to PUB-NP-004, Attachment C, Footnote 4. Of the overall average customer rate impact of 10.6%, 1.4% is related to Order No. P.U. 20(2024).

[8] The principal purpose of the Rate Stabilization Adjustment is to ensure variations in Newfoundland Power's purchased power costs are recovered in a timely manner. In Order No. P.U. 17(1987), the Board ordered that municipal taxes be collected through a Municipal Tax Adjustment factor in the rates of Newfoundland on July 1st of each year.

[9] The findings in Order No. P.U. 16(2024) resulted in Newfoundland Power filing a compliance application, which was approved in Order No. P.U. 18(2024).

[10] Newfoundland Power Wholesale Rate Flow-Through Application, Response to PUB-NP-004, Footnote 1.

On September 16, 2024 Newfoundland Power and Hydro filed separate applications to revise Hydro's wholesale rate charged to Newfoundland Power, effective January 1, 2025. Order No. P.U. 2(2025) permits Newfoundland Power to flow-through supply and financial costs associated with the approval of a new Hydro wholesale rate effective January 1, 2025. ("Newfoundland Power Wholesale Rate Flow-through Order").[11] The proposed revenue requirement for the 2025 and 2026 Test Years is impacted as a result of this order.[12]

Newfoundland Power revised the proposals in the Application to reflect the 2024 Return on Rate Base Order, the 2024 RSA Order and the Newfoundland Power Wholesale Rate Flow-Through Order. Newfoundland Power's revised proposals include: [13]

1. the amortization of a forecast 2025 revenue shortfall of approximately $39,220,000, over a 30-month period, commencing July 1, 2025 and ending December 31, 2027;
2. rates, tolls, and charges and rules and regulations governing service, to be effective for all service provided on and after July 1, 2025, which result in an overall average increase in current customer rates of 10.6% and average increases in proposed customer rates by class as follows:

Proposed Average Customer Rate Increases by Class	
Rate Class	**Average Increase**
Domestic	10.7%
General Service 0-100kW (110 kVA)	10.6%
General Service 110-1000 kVA	10.4%
General Service 1000 kVA and Over	10.2%
Street and Area Lighting	12.2%

3. a rate of return on average rate base for 2025 of 7.34% in a range of 7.16% to 7.52% and for 2026 of 7.17% in a range of 6.99% to 7.35%;
4. a forecast average rate base for 2025 of $1,412,358,000 and for 2026 of $1,461,358,000; and
5. a forecast revenue requirement from customer rates for 2025 of $777,523,000 and for 2026 of $824,906,000.

[11] Order No. P.U. 1(2025) approves a new Wholesale rate to be charged to Newfoundland Power.
[12] Newfoundland Power Wholesale Rate Flow-Through Application, Response to PUB-NP-005, Table 1.
[13] Newfoundland Power Wholesale Rate Flow-Through Application, Response to PUB-NP-003, Attachment A.

A breakdown of the original and revised cost and rate impacts are set out in the table below.

Proposed Cost Increases and Average Customer Rate Increases Breakdown				
	Application[14]		Revised Proposals[15]	
	Amount ($millions)	Rate Increase (%)	Amount ($millions)	Rate Increase (%)
Change in Rate of Return on Rate Base and Depreciation	18.3	2.2	30.6	3.5
Operating costs	13.4	1.6	13.4	1.5
Amortization of the Revenue Shortfall and Hearing Costs	9.8	1.2	9.8	1.1
Sales growth	(8.9)	(1.1)	(8.9)	(1.0)
Increase in Return on Equity	13.0	1.6	13.0	1.5
Power Supply Costs	-	-	35.7	4.0
Total	**45.6**	**5.5**	**93.6**	**10.6**

References in this Decision and Order to application proposals, including revenue requirement, customer rate impacts, and credit metrics, unless otherwise noted, refer to the information provided in the revised proposals.[16]

3. SETTLEMENT AGREEMENT

The Settlement Agreement sets out the parties' agreement on the following issues:

- automatic adjustment formula;
- regulatory accounting matters; and
- the 2025 and 2026 Customer, Energy and Demand Forecast.

In considering the Settlement Agreement the Board must be satisfied that the recommendations are reasonable and consistent with the existing regulatory framework and legislation, with particular reference to the power policy of the province as set out in section 3 of the EPCA.

3.1. The Automatic Adjustment Formula

The parties agreed that, as proposed in the Application, the Board should approve the continued suspension of the use of an automatic adjustment formula for setting Newfoundland Power's allowed rate of return on equity between test years.

The use of an automatic adjustment formula was approved by the Board in 1998 to determine changes to Newfoundland Power's rate of return on equity between general rate applications

[14] PUB-NP-002.
[15] Newfoundland Power Wholesale Rate Flow-Through Application, PUB-NP-005.
[16] Newfoundland Power Wholesale Rate Flow-Through Application, PUB-NP-006.

based on forecast changes in long-term Canada bond yields. The Board first suspended the use of the automatic adjustment formula in 2011.[17] The formula has been suspended since that time, with the Board recognizing in its Order in relation to Newfoundland Power's 2013/2014 General Rate Application, that abnormally low bond yields had raised concerns about the operation of the formula in establishing a fair return for Newfoundland Power.[18] The Application notes that while bond yields have increased, there has been continued volatility in financial markets in recent years. The Application states that current economic conditions do not provide the stability necessary to establish a formula that can estimate a reasonable rate of return on equity between test years.[19]

The Board accepts the Settlement Agreement recommendation for the continued suspension of the automatic adjustment formula.

3.2. Regulatory Accounting

3.2.1. Clause II.9 of the Rate Stabilization Clause

The parties agreed that, as proposed in the Application, the Board should approve, for costs incurred commencing January 1, 2021, amendments to Clause II.9 of the Rate Stabilization Clause to allow for recovery of costs charged annually to the Electrification Cost Deferral Account.

The Board approved the creation of the Electrification Cost Deferral Account in Order No. P.U. 3(2022). At that time the Board did not approve the proposed amendments to Clause II.9 of the Rate Stabilization Clause, stating that the proposal should be considered as part of the utility's electrification application.[20] In Order No. P.U. 33(2022), in relation to Newfoundland Power's 2021 Electrification, Conservation and Demand Management Application, the Board agreed that a ten-year period to recover costs associated with electrification initiatives is appropriate and consistent with sound utility practice, current practices for Conservation Demand Management initiatives, and regulatory fairness principles. The Board also provided that Newfoundland Power may file for the necessary approvals with respect to the recovery of approved electrification costs.[21]

The Board accepts the Settlement Agreement recommendation that Clause II.9 of the Rate Stabilization Clause should be amended to allow for recovery of costs charged annually to the Electrification Cost Deferral Account for costs incurred commencing January 1, 2021.

[17] Order No. P.U. 25(2011).
[18] Order No. P.U. 13(2013), page 36.
[19] Application, Volume 1, pages 3-45 to 3-47.
[20] Order No. P.U. 3(2022) pages 9 to 11.
[21] Order No. P.U. 33(2022) page 18.

3.2.2. The Demand Management Incentive Account

The parties agreed that, as proposed in the Application, the Board should approve amendments to the definition of the Demand Management Incentive Account (the "DMI Account") effective January 1, 2025 to establish a threshold of +/- $500,000.

The Board approved the creation of the DMI Account in Order No. P.U. 32(2007) with a threshold from +/- 1% of test year wholesale demand charges. The DMI Account is intended to provide an incentive to Newfoundland Power to undertake reasonable initiatives to minimize peak demand. The DMI Account also isolates demand costs and, in conjunction with the Energy Supply Cost Variance, provides Newfoundland Power with the ability to recover its costs associated with variability in purchased power costs inherent in the demand and energy wholesale rate.[22] In Order No. P.U. 43(2009) the Board approved the continued use of the DMI Account. The Application states that since 2008, its ability to reduce its purchased power demand costs has become more limited. The demand rate has also increased by more than 40%, with risk of further increase. The Application notes that although the use of thresholds associated with supply cost mechanisms is not the norm in Canada, the Board has approved cost thresholds of +/- $500,000 associated with certain Hydro supply costs in the past.[23]

The Board accepts the Settlement Agreement recommendation to amend the Demand Management Incentive Account definition to establish a threshold of +/- $500,000 effective January 1, 2025.

3.2.3. Report on Supply Cost Recovery Mechanisms

The parties agreed that Newfoundland Power should file a report ahead of its next general rate application reviewing its supply cost mechanisms.

Utility supply costs are typically recovered through supply cost mechanisms. The main supply cost recovery mechanism used by Newfoundland Power is the Rate Stabilization Account ("RSA"), which includes recovery of the Energy Supply Cost Variance, the DMI Account and the Weather Normalization Reserve.[24] The report will include a review of the recommendations in the Brattle Group Deferral Accounts Report, as well as a jurisdictional review. Newfoundland Power will file the report with the Board on or before December 31, 2025.

The Board accepts the Settlement Agreement recommendation for Newfoundland Power to file a report reviewing its supply cost recovery mechanisms on or before December 31, 2025.

[22] Order No. P.U. 32(2007), pages 26 to 27.
[23] Application, Volume 1, page 3-55. See also Application, Volume 1, page 3-54, Footnote 148.
[24] Application, Volume 1, pages 3-39 to 3-40.

3.2.4. The Pension Capitalization Cost Deferral Account

The parties agreed that, as proposed in the Application, the Board should approve the proposed amendment to the definition of the Pension Capitalization Cost Deferral Account effective January 1, 2025, to cease charges to the account effective December 31, 2024.

In Order No. P.U. 3(2022) the Board approved the creation of the Pension Capitalization Cost Deferral Account. The deferral account offsets the income tax impact of the change in capitalizing pension costs, with amortization of the amounts over a five-year period, commencing January 1, 2023. The Application proposes amending the definition of the Pension Capitalization Deferral Account so that these amounts will no longer be charged to the account, effective December 31, 2024. Prior charges will continue to be amortized over a five-year period.[25]

The Board accepts the Settlement Agreement recommendation that the definition of the Pension Capitalization Cost Deferral Account should be amended effective January 1, 2025, to cease charges to the account, effective December 31, 2024.

3.2.5. The International Financial Reporting Standards Cost Deferral Account

The parties agreed that the Board should approve the creation and use of a deferral account to provide for the deferred recovery of actual costs incurred as a result of Newfoundland Power's conversion to International Financial Reporting Standards ("IFRS"). The parties further agreed that the Board should approve a decrease to the revenue requirement for 2025 and 2026 of $995,000 and $495,000, respectively, to reflect the use of the IFRS Cost Deferral Account. The IFRS Cost Deferral Account definition was attached to the Settlement Agreement.

The Application notes Newfoundland Power's upcoming conversion from U.S. generally accepted accounting principles ("U.S. GAAP") to IFRS. Newfoundland Power states that it currently uses U.S. GAAP; however, by 2027, it will be required to file its financial statements in accordance with IFRS.[26] Newfoundland Power's test year operating costs include $995,000 in 2025 and $495,000 in 2026 to reflect the anticipated costs for conversion from U.S. GAAP to IFRS.[27]

The Board accepts the Settlement Agreement recommendation for the creation and use of the International Financial Reporting Standards Cost Deferral Account and a reduction in the forecast revenue requirement for the 2025 and 2026 Test Years of $995,000 and $495,000, respectively.

[25] Application, Volume 1, pages 3-56 to 3-57.
[26] Application, Volume 1, page 2-33, Footnote 60.
[27] PUB-NP-022, Table 1.

3.2.6. Amortization of Hearing Costs

The parties agreed that, as proposed in the Application, the Board and the Consumer Advocate hearing costs should be recovered over a 30-month period commencing July 1, 2025 and ending December 31, 2027. For rate setting purposes, the parties agreed that the hearing costs shall be estimated at $1.0 million. The parties also agreed that any difference between actual costs and the estimated costs should be recovered or rebated through the RSA.[28]

The Board accepts the Settlement Agreement recommendation for the amortization of the Board and the Consumer Advocate hearing costs, in an amount up to $1.0 million, over the period of July 1, 2025 to December 31, 2027, with differences between actual and estimated hearing costs to be reflected in the Rate Stabilization Account.

3.2.7. Depreciation Expense

The parties agreed that, as proposed in the Application, the Board should approve the calculation of depreciation expense.

The Application proposes the approval of depreciation expenses for 2025 and 2026 in accordance with the methodology and rates outlined in the 2019 Depreciation Study.[29] In Order No. P.U. 3(2022), the Board approved Newfoundland Power's use of the depreciation rates and methodology as recommended in the 2019 Depreciation Study for the calculation of its depreciation expense with effect from January 1, 2022. The Application states that depreciation rates are typically reviewed every four to five years, with the next depreciation study expected to be completed in 2025 based on plant in service as of December 31, 2024.[30] Grant Thornton reviewed Newfoundland Power's forecast depreciation expenses of $83,143,000 for 2025 and $86,691,000 for 2026. Based on its review, Grant Thornton concluded that the depreciation rates used to calculate the proposed forecast for 2025 and 2026 agree to those recommended in the 2019 Depreciation Study and Newfoundland Power's pre-filed evidence, and that the depreciation expense, has been calculated in accordance with these depreciation rates.[31]

The Board accepts the Settlement Agreement recommendation for the proposed calculation of depreciation expense based on the rates in the 2019 Depreciation Study.

3.3. Customer, Energy and Demand Forecast

The parties agreed that, as proposed in the Application, the Board should approve the 2025 and 2026 Customer, Energy and Demand Forecast ("CED Forecast"). The parties also agreed that Newfoundland Power should engage an expert to conduct a review of the recommendations set

[28] Application, Volume 1, page 3-57.
[29] Application, Volume 1, pages 3-6 to 3-7.
[30] Application, Volume 1, page 3-7.
[31] Grant Thornton Report, pages 48 to 49.

out in the Brattle Group Load Forecasting Methodology Review and file the results of the review on or before December 31, 2025.

The Application includes a 2026 CED Forecast that indicates:

(i) an increase in the number of customers by 0.4% in 2025 and 0.3% in 2026;[32]
(ii) an increase in energy sales of approximately 0.8% in each of 2025 and 2026;[33] and
(iii) a decline in peak demand of approximately 0.7% in 2026.[34]

Grant Thornton reviewed the CED Forecast and determined that the overall forecast methodology used by Newfoundland Power is consistent with the 2022/2023 General Rate Application. The Brattle Group reviewed Newfoundland Power's load forecasting methodology and determined that the CED Forecast provided reasonable accuracy for the 2025/2026 General Rate Application. However, the Brattle Group noted that there were shortcomings in Newfoundland Power's forecasting approach, which were likely to negatively impact accuracy levels in the future. The Brattle Group offered a number of recommendations for Newfoundland Power to consider going forward.[35]

The Board accepts the Settlement Agreement recommendation in relation to the 2025 and 2026 Customer, Energy and Demand Forecast filed in the Application to be used in calculating the forecast revenue requirement for the 2025 and 2026 Test Years.

The Board accepts the Settlement Agreement recommendation for Newfoundland Power to file a report in relation to the Customer, Energy and Demand Forecast methodology including the review of the recommendations set out in the Brattle Group Load Forecasting Methodology Review, on or before December 31, 2025.

4. OPERATING COSTS

The Application seeks approval of Gross Operating Costs (Operating Costs) of $79.083 million for 2025 and $81.603 million for 2026. Operating Costs constitute 10% of the overall revenue requirement for 2026 of $824.517 million.[36]

Issues were raised in this proceeding with respect to the proposed increases in Operating Costs and executive compensation.

[32] Application, Volume 1, page 5-3.
[33] Application, Volume 1, page 5-4.
[34] Application, Volume 1, page 5-6, Table 5-4.
[35] Brattle Group Load Forecasting Methodology Review, pages 23 to 25.
[36] Newfoundland Power Wholesale Rate Flow-Through Application filed September 16, 2024, Schedule 1, Appendix C, page 2 of 2.

4.1. Operating Costs Increases

The proposed 2026 Operating Costs are approximately 18.3% higher than the 2023 Test Year Operating Costs reflected in current customer rates. The significant increase in Operating Costs was a focus for the Intervenors and the Board throughout the proceeding.

Submissions

The Consumer Advocate submitted that Newfoundland Power should be incentivized to aggressively reduce growth in operating expenses and recommended that the proposed 2025 and 2026 Operating Costs be reduced by $2.5 million and $5 million, respectively.[37] According to the Consumer Advocate, Newfoundland Power's senior management made no attempt to mitigate the significant rate increases of more than 20% facing customers over the next year and provided no direction to management to cut costs to only those absolutely necessary.[38] The Consumer Advocate noted that the growth in operating expenses proposed for 2025 and 2026 of 4% and 3.7%, respectively is higher than inflation and builds on significant growth in operating expenses of 7.3% in 2023 and 6.6% in 2024 which demonstrates weak cost control.[39] The Consumer Advocate also recommended that the proposed insurance costs be disallowed. According to the Consumer Advocate it is not clear that customers benefit from Newfoundland Power's participation in the Fortis Group insurance program and that insurance is obtained at the lowest cost.

Hydro submitted that in light of the substantial increase in Operating Costs and Newfoundland Power's evidence that it has taken no additional action to reduce costs for the proposed test years, it is appropriate for the Board to issue directives that will provide incentives to Newfoundland Power to manage costs and find efficiencies.[40] Hydro submitted that the evidence is not clear as to whether Newfoundland Power's Operating Costs have been managed in a reasonable way. Hydro referred to the significant increase in Operating Costs from the 2023 Test Year to 2026 Test Year. Hydro noted that while Newfoundland Power's Operating Costs had been declining from 2014 to 2018, they started to increase in 2019 and, after a decrease in 2020, the costs have continued to increase. Hydro noted that Newfoundland Power could not provide examples of specific actions to reduce costs or efficiencies that were implemented for the 2025 and 2026 test years, different than in previous general rate applications.

Newfoundland Power submitted that: (i) the proposed Operating Costs reasonably reflect expected costs in 2025 and 2026; (ii) the proposed Operating Costs appropriately balance costs and service; (iii) Grant Thornton did not identify any irregularities or inconsistencies in its review of the Operating Costs; and (iv) there is no basis in the evidence to indicate the Operating Costs

[37] Consumer Advocate Submission, pages 62 to 63.
[38] Consumer Advocate Submission, page 4.
[39] The Consumer Advocate Submission refers to operating costs and not gross operating costs. Operating costs include adjustments for recovery of approved deferral amounts and transfers to GEC.
[40] Newfoundland Hydro Submission, pages 8-9.

are unreasonable.[41] According to Newfoundland Power the evidence on the record provides justification for each cost included in the 2025 and 2026 forecasts and demonstrates how it operates in an efficient manner.[42]

According to Newfoundland Power it has demonstrated sound cost management as evidenced by various benchmarks, including (i) the gross operating cost per customer was reduced by approximately 9.5% on an inflation-adjusted basis from 2013-2023; (ii) the operating cost per customer of a U.S peer group increased by 15.1% over the same period; (iii) the operating cost per customer is forecast to decrease by 0.7% on an inflation adjusted basis between 2024 and 2026; (iv) labour costs are forecast to increase by 3.1% per year from 2022 to 2026, approximately 1% less than Newfoundland Power's internal labour inflation rate; and (v) Operating Costs per kWh have been relatively consistent over the last decade.[43] Newfoundland Power noted that the record provides more than two dozen examples of productivity improvements over the years and that the test year Operating Costs would have been higher without Newfoundland Power's approach to cost management.[44] Newfoundland Power also noted that the allowed range of return on rate base provides incentive to lower operating costs.[45]

Newfoundland Power submitted that the evidence adequately explains the reasons for the increases in Operating Costs.[46] Newfoundland Power noted that inflation was much higher than anticipated at the time of the last general rate application with an actual 17% increase for the period 2020-2023 compared to the 5.8% increase assumed at the time of the last general rate application.[47] According to Newfoundland Power its approach to cost management focuses on the effective deployment of human resources and use of operational technologies. Newfoundland Power submitted that the Board should assess forecast operating costs against recent actual and forecast costs as well as operating cost metrics similar to the approach that was taken when a productivity allowance was last imposed on a utility.[48] Newfoundland Power submitted that a reasonable level of operating efficiency is demonstrated for Labour Costs which increased by 1% less than its labour inflation rate for the 2022 to 2026 period.[49] In terms of Other Costs, Newfoundland Power submitted that inflationary pressure is the primary reason for the increase and that forecasts for insurance, consulting fees and computing equipment and software costs, exceed inflation due to market conditions. Newfoundland Power noted that while Other Costs are forecast to increase by 4.9% on an annual basis from 2022 to 2026, if insurance, other company fees and computing equipment and software costs, were excluded the forecast increase would be 1.3% per year.[50]

[41] Newfoundland Power Submission, page 43, lines 2-6 and lines 10-14 and page 46, lines 16-18.
[42] Newfoundland Power Submission, page 52, line 20 to page 53, line 3.
[43] Newfoundland Power Submission, page 45, lines 18 to page 46, line 8.
[44] Newfoundland Power submission, page 45, lines 4-12.
[45] Newfoundland Power submission, page 115, lines 8-9.
[46] Newfoundland Power submission, page 114, lines 13-16.
[47] Newfoundland Power Submission, page 44, lines 7-17.
[48] Newfoundland Power Submission, page 52, lines 5-7.
[49] Newfoundland Power Submission, page 48, lines 1-2.
[50] Newfoundland Power Submission, page 48, lines 11-15.

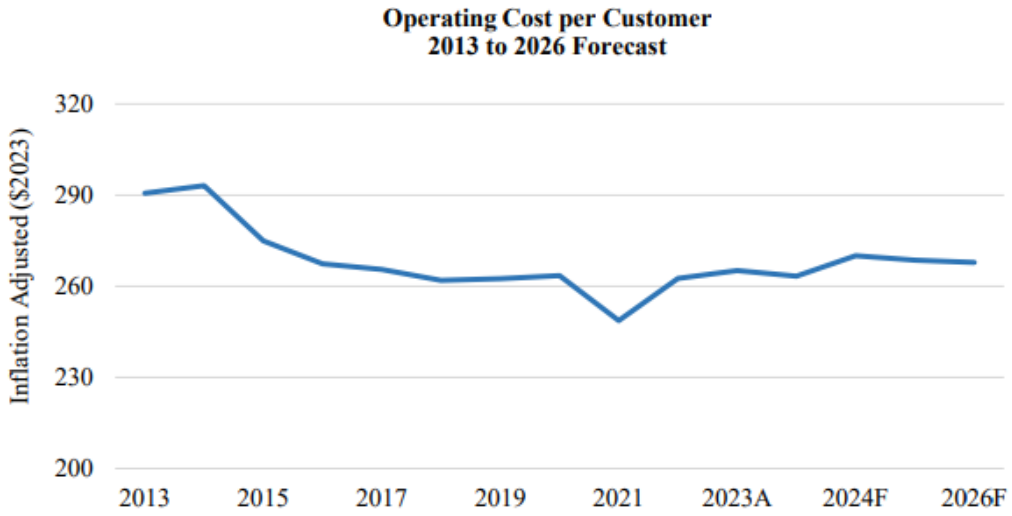
According to Newfoundland Power the Consumer Advocate's submission did not consider key evidence including; (i) the impact of market conditions causing certain costs to exceed inflation, such as insurance and computing equipment and software; (ii) operational requirements such as those related to vegetation management and the need for increased consulting fees; (iii) labour increases reflect collectively bargained wage increases which are comparable to other Atlantic utilities over the same period; and (iv) its cost performance metrics.[51] Newfoundland Power noted that the growth rates cited by the Consumer Advocate refer to operating costs and when gross operating costs are considered, the increase is 3.9% over the 2022 to 2026 period not 5.9% as stated in the Consumer Advocate's submission.[52] Newfoundland Power also submitted that the Consumer Advocate presented no evidence to show any proposed cost is unreasonable. In reply to Hydro, Newfoundland Power submitted that Hydro's analysis is based on a limited analysis of the proposed operating costs, provides no evidence that any specific cost is unreasonable and does not consider the legislative requirement that Newfoundland Power must have the opportunity to recover its reasonable costs.[53]

Board Decision

The increase in Newfoundland Power's Operating Costs was a significant issue in this proceeding. Operating Costs are generally considered to be the category of costs over which a utility has the most control, unlike other categories such as depreciation, interest and financing charges.[54] The proposed Operating Costs increase represents approximately 1.5% of the 10.6% overall customer rate increase associated with this Application.[55]

Newfoundland Power submitted that the evidence demonstrates that its costs management reflects an appropriate balance of cost and service and noted that its Operating Costs per customer decreased on an inflation-adjusted basis over the period 2013 to 2022. While the Board accepts that Newfoundland Power's Operating Costs per customer decreased for a number of years over the period 2013 to 2018, this downward trend has reversed. Since 2021 Newfoundland Power's Operating Costs have been increasing, on an inflation adjusted basis, as can be seen in the graph below.[56]

[51] Newfoundland Power Submission, page 88, line 8 to page 90, line 7.
[52] The increase is 3.7% excluding IFRS costs as agreed in the Settlement Agreement.
[53] Newfoundland Power Submission, page 114, lines 1-5.
[54] Transcript, June 17, 2024, page 79, lines 3-10.
[55] Newfoundland Power Wholesale Rate Flow-through Application, PUB-NP-005.
[56] NLH-NP-011.



Newfoundland Power explained that the forecast increase from 2023 to 2026 is due to overall inflationary pressures and higher than inflation pressures for certain costs due to market conditions and operational requirements. The Board acknowledges that inflation was higher in 2022 and 2023 than anticipated in Newfoundland Power's last general rate application, but notes that the Operating Costs set out in this graph are inflation-adjusted.[57]

The evidence shows that Newfoundland Power became aware in mid-2023 that its Operating Costs were tracking higher than 2023 Test Year. Despite this, no specific action was taken and no directive issued to managers to review and potentially reduce costs.[58] Newfoundland Power explained that the focus is always on least-cost and efficient operations as supported by past performance and it would have been difficult to take action mid-year.[59] Given the magnitude of the increases in 2023 costs, the Board would have expected that additional measures would have been taken to review and manage the cost increases. The Board notes that even with the higher operating costs in 2023 Newfoundland Power earned above the allowed range of return.[60] Because Newfoundland Power was in an excess earnings position in 2023, these higher operating costs served to reduce the amount of the excess earnings that were applied to the benefit of customers.

The Board acknowledges Newfoundland Power's position that the assessment of Operating Costs should take into account the 2023 actual costs and not the 2023 Test Year costs. While actual values have been used in the past there is not normally such a variance between test year values and actual costs.[61] The Board believes that in the circumstances it is appropriate to consider both the 2023 Test Year Operating Costs and the 2023 actual Operating Costs when assessing the reasonableness of the proposed 2025 and 2026 Test Year Operating Costs.

[57] PUB-NP-018 and Transcript, June 26, 2024, page 7, lines 12-20.
[58] Transcript, June 17, 2024, page 88, line 17 to page 89, line 6.
[59] Transcript, June 14, 2024, page 73, lines 4-21.
[60] Order No. P.U. 20(2024).
[61] PUB-NP-141, Attachment C.

Based on the evidence for 2025 and 2026, Newfoundland Power did not take specific targeted actions to review the forecast Operating Costs to identify measures to reduce the significant increases in these costs, despite the significant proposed increase in customer rates.[62] Newfoundland Power's approach with respect to the forecast increases in Operating Costs is particularly concerning for the Board given the proposed and anticipated customer rate increases and the potential for rate shock as a result of the current upward pressure on rates.

Labour is the largest cost category of Newfoundland Power's Operating Costs, constituting 54% of the forecast 2026 Operating Costs. Labour Costs are forecast to increase by 13.1% from the 2023 Test Year to the 2026 Test Year.[63] The proposed Labour Costs are $42.079 million in 2025 and $43.882 million in 2026.[64] Newfoundland Power is forecasting an annual increase in Labour Costs of approximately 3.1% from actual Labour Costs over the 2022 to 2026 period. According to Newfoundland Power a reasonable level of operating efficiency is demonstrated for Labour Costs given that they are forecast to increase by 1% less than its internal labour inflation rate over the 2022 to 2026 period.[65] The Board notes that Newfoundland Power has a great deal of control of Labour Costs through its compensation policies and the management of its workforce. Based on the evidence the average base salary for all employees is forecast to increase by 13.3% from 2023 Forecast to 2026, from $96,722 to $109,584.[66] Further the evidence shows that the hourly wage rates for a number of Newfoundland Power job classifications are higher than those of other Atlantic Canadian utilities.[67] For the executive group and managerial employees the Board notes Newfoundland Power normally accepts the salary increases recommended by its consultants.[68] While the Labour Costs do not reflect the full amount associated with Newfoundland Power's internal labour inflation rate, based on the evidence it is not clear that Newfoundland Power took adequate measures to manage its Labour Costs considering the significant increases in Operating Costs and the significant upward pressure on customer rates.

Other Costs make up the remaining 46% of the proposed 2026 Operating Costs. These costs include non-labour costs such as insurance, computing equipment and software and vegetation management costs. Other Costs are forecast to increase by 25% from the 2023 Test Year to the 2026 Test Year.[69] The proposed Other Costs are $37.0 million in 2025 and $37.7 million in 2026.[70] Actual Other Costs in 2023 exceeded the 2023 Test Year by 12% with certain categories having significant increases. Increases in Other Costs include:

[62] Transcript, June 14, page 55, line 12-page 59, line 17; Transcript, June 14, 17, page 80, line 7-page page 83, line 22 and Transcript, June 27, page 61, line 9-page 64, line 19.
[63] PUB Information Request (ii), Schedule B, Attachment 5 for Test Year 2022 and 2023 and 2025 Forecast and 2026 Forecast.
[64] Application, Table 2-8, page 2-34 and lines 9-10.
[65] Application, page 2-31, Footnote 57.
[66] PUB-NP-031, Table 1.
[67] PUB-NP-031, Table 2.
[68] Transcript June 14, 2024, page 115, lines 5-22.
[69] NLH-NP-029, Attachment A.
[70] Application, Table 2-8, page 2-34.

- Insurance costs are forecast to increase by 25% from the 2023 Test Year to 2026 Test Year, from $2.4 million to $2.9 million in 2026.[71] The actual costs in 2023 were 3% higher than 2023 Test Year.[72] The evidence confirmed that the rates and coverage for 2023-2024 for Newfoundland Power are the best available in the current market conditions.[73] Newfoundland Power's insurance coverage is placed as part of the Fortis Group, which based on the evidence, achieves the greatest cost efficiency and the broadest coverage.[74] Based on the evidence, insurance costs increased consistent with general market trends and inflationary increases.

- Other Company Fees are forecast to increase by 82% from the 2023 Test Year to the 2026 Test Year, from $2.6 million to $4.2 million.[75] Actual costs in 2023 were 38% higher than 2023 Test Year, with the 2026 forecast being an increase of approximately 32% over the 2023 actual cost.[76] Other Company Fees primarily reflect costs associated with (i) regulatory proceedings; (ii) upcoming changes in accounting standards (now proposed to be deferred in the Settlement Agreement);[77] (iii) information technology; and (iv) other areas, such as engineering and human resources.[78] Fees paid for Information Technology services comprise the largest category of cost and are forecast to be $967,000 in 2026.[79] The 2026 Forecast for information technology consulting fees is 212% higher than the 2023 Test Year of $310,000.[80]

- Computing Equipment and Software Costs are forecast to increase by 46% from 2023 Test Year to 2026 Test Year, from $3.4 million to $5.0 million. Actual costs in 2023 were 7% higher than 2023 Test Year. The increase in computing equipment and software costs reflects forecast licensing and support for third-party hardware and software solutions.[81] Based on the evidence, the cost for technology is increasing beyond inflation with market demand for IT professionals and programmers driving costs for software and licensing fees and the cost of new technology solutions. The need to address increasing cybersecurity requirements is also driving costs.[82]

[71] PUB Information Request (ii), Schedule B, Attachment 5.
[72] NLH-NP-029, Attachment A.
[73] PUB-NP-018d) and Transcript, June 17, 2024, pages 5, line 4 to page 6, line 5; NLH-NP-021, Attachment A.
[74] Undertaking #3, Attachment A.
[75] Undertaking #10, after the reduction agreed in the Settlement Agreement.
[76] NLH-NP-029, Attachment A.
[77] As a result of the Settlement Agreement $0.495 million will be removed from the revenue requirement and set up for deferred recovery.
[78] PUB-NP-018f), page 3, and NLH-NP-028.
[79] Undertaking #10.
[80] PUB-NP-022.
[81] PUB-NP-018h).
[82] Transcript, June 27,2024, page 44, line 2 to page 45, line 17.

- Vegetation management costs are forecast to increase by 40.6% from 2023 Test Year to 2026 Test Year, from $2.4 million to $3.4 million.[83] Actual costs in 2023 were 36% higher than 2023 Test Year.[84] The increase is due to additional distribution and transmission vegetation management activity in the past three years and inflationary increases.[85] Based on the evidence work orders for planned vegetation management, customer tree trimming requests and the percentage of outage minutes due to tree contacts have increased in recent years.[86] Evidence with respect to the vegetation management costs of other utilities in Atlantic Canada showed Newfoundland Power's costs were consistent with these other utilities.[87]

- Education, training and employee fees are forecast to increase by 49% from 2023 Test Year to 2026 Test Year, from $0.4 million to $0.5 million. Actual 2023 costs were 59% higher than 2023 Test Year.[88] The increase in these costs was due to the return to normal levels of education and training following the lifting of public health restrictions during the Covid-19 pandemic and changes in workforce demographics.[89] To manage these costs Newfoundland Power utilizes free training, virtual education and internal facilitators.[90]

- Travel costs are forecast to increase by 36.6% from 2023 Test Year to 2026 Test Year, from $0.9 million to $1.2 million. Actual 2023 costs were 31% higher than the 2023 Test Year.[91] The increase in actual 2023 costs from the 2023 Test Year was explained on the basis of a return to a normal level of travel after the Covid-19 pandemic and inflationary pressures.[92] Newfoundland Power manages travel costs through the placement of employees at strategic locations, the use of virtual meetings, expense guidelines and a third-party management company.[93]

- Vehicle expenses are forecast to increase by 28% from the 2023 Test Year to 2026 Test Year, from $1.7 million to $2.2 million. Actual 2023 costs were 12% higher than 2023 Test Year.[94] The increase in vehicle expenses is due to higher fuel prices and increased maintenance costs.[95]

The Board accepts that inflationary pressure is a primary reason for the increase in the Other Costs category, but notes that the increases in several categories are much higher than the level

[83] PUB-Information Request (ii), Schedule B, Attachment 5.
[84] NLH-NP-029, Attachment A.
[85] PUB-NP-18 g) and Transcript, June 27, page 51, line 11 to page 53, line 24.
[86] PUB-NP-141 f), pages 5-6.
[87] PUB-NP-141 f), pages 7-8.
[88] NLH-NP-029, Attachment A.
[89] PUB-NP-018 e); As of 2023, 31% of employees had less than five years of experience, compared to 9% in 2020.
[90] PUB-NP-141 b).
[91] NLH-NP-029, Attachment A.
[92] PUB-NP-018 c).
[93] PUB-NP-141 a).
[94] NLH-NP-029, Attachment A.
[95] PUB-NP-018 a).

of inflation. The Board accepts the evidence that the increase in the forecast insurance costs is based on market factors outside of Newfoundland Power's control. The Board also accepts that the costs associated with information technology services and computing equipment and software have increased at rates higher than inflation, but finds the evidence to be unclear as to whether Newfoundland Power sought opportunities to better manage these costs. In addition, the Board is concerned about the increases in the other categories of Other Costs and the magnitude of the increases in Other Costs generally. Newfoundland Power has flexibility with respect to the timing and extent of some of the costs in this category, including vegetation management, education, training and employee fees, and travel costs. While the Board accepts inflationary increases and that there were additional cost pressures on certain categories of Other Costs, given the magnitude of the cost increases, the Board is not satisfied that reasonable efforts were made to manage Other Costs, to the extent possible.

The Board is required to balance the interests of Newfoundland Power in the recovery of prudent costs with the interests of customers who are to receive reliable service at the lowest possible cost, in an environmentally responsible manner. The Board notes that there is currently significant upward pressure on customer rates. The combined impact of the increases on overall customer rates is expected to be in excess of 20% over the 2024 to 2026 period. Increases of this amount are extraordinary and would normally be considered to constitute rate shock for customers.

Newfoundland Power is required to establish that its proposed 2025 and 2026 Operating Costs are reasonable. The Board is not satisfied that Newfoundland Power has met this burden of proof. The Board does not accept Newfoundland Power's reliance on cost decreases from 2013 to 2018 in assessing the proposed 2025 Test Year and 2026 Test Year Operating Costs. The Board is concerned that, Newfoundland Power took no specific additional actions to address the increasing Operating Costs in recent years. The Board is not satisfied that Newfoundland Power has demonstrated adequate management of its Operating Costs or that the proposed 2025 and 2026 Operating Costs are reasonable and should be fully recovered from customers. While the Labour Costs do not reflect the full amount associated with Newfoundland Power's own internal labour inflation rate, the Board is not satisfied that Newfoundland Power took adequate steps to manage its Labour Costs to find further reductions. In terms of its Other Costs, the Board accepts that there are factors driving increases in certain cost categories beyond the level of inflation. Nevertheless, based on the evidence, insufficient action was taken by Newfoundland Power to find ways to reduce the impact of these cost drivers and the upward pressure on its costs. The Board believes that a productivity allowance should be applied to incent Newfoundland Power to find additional efficiencies in its operations.

In determining the amount of the productivity allowance the Board notes that the 2025 Test Year Operating Costs are $10.1 million higher than 2023 Test Year costs, and $6.1 million higher than actual 2023 costs. For 2026 Test Year the Operating Costs are $12.7 million higher than 2023 Test Year costs and $8.6 million higher than actual 2023 costs. Based on the evidence the Board is satisfied that it is reasonable to expect that Newfoundland Power can achieve a reduction of $2.0 million in Operating Costs in each Test Year without impacting its obligation to provide

reliable service, through the effective management of its Labour Costs and Other Costs. The Board notes that a $2.0 million productivity allowance would require Newfoundland Power to reduce the proposed Operating Costs by approximately 2.5% in 2025 and 2026. The Board is satisfied that a productivity allowance of $2.0 million should be applied for the 2025 Test Year and the 2026 Test Year to provide an incentive to Newfoundland Power to take additional measures to manage costs and find efficiencies.

The Board finds that Newfoundland Power's proposed Operating Costs should be reduced by $2.0 million in the 2025 Test Year revenue requirement and in the 2026 Test Year revenue requirement.

4.2. Executive Compensation

Newfoundland Power has different compensation policies for its three separate employee groups, union, managers, and executive and directors.[96] Issues were raised in the proceeding in relation to Newfoundland Power's executive compensation, in terms of base salaries and short-term incentives as discussed below.

4.2.1. Base Salaries

The salary policy for the executive and directors is set to be competitive with the median salary paid by a group of Canadian Commercial Industrial companies.[97]

Submissions

The Consumer Advocate submitted that Newfoundland Power's executive compensation is excessive and recommended that 20% of executive base pay be disallowed and paid by the shareholder.[98] The Consumer Advocate submitted that Newfoundland Power executive salaries exceed the salaries of other utility executives and cited the executive salaries of three crown-owned electric utilities in Canada, as well as executive salaries for Nova Scotia Power which are established in accordance with legislation with the shareholder paying additional amounts.[99] The Consumer Advocate submitted that Newfoundland Power is not comparable to the companies in the Canadian Commercial Industrial group which includes only three Canadian electrical utilities, none of which are comparable to Newfoundland Power. According to the Consumer Advocate the private investor companies in the Canadian Commercial Industrial group face different challenges than a traditional regulated monopoly like Newfoundland Power which, under existing legislation, is assured a reasonable return.[100] The Consumer Advocate also stated that the assumption that Newfoundland Power competes in the Canadian commercial market

[96] PUB-NP-031.
[97] PUB-NP-031d).
[98] Consumer Advocate Submission, pages 67 and 70 to71.
[99] Consumer Advocate Submission, page 67, line 25 to page 68, line 14.
[100] Consumer Advocate Submission, page 65, lines 29-34.

to recruit executives is not correct as evidenced by the history of Newfoundland Power's hiring practices.[101]

Hydro submitted that the underlying assumptions for executive compensation appear to have not been fully analyzed for its appropriateness and applicability to Newfoundland Power's operating environment. Hydro questioned whether the Canadian Commercial Industrial group is the most appropriate comparator given the lack of utility representation and geographic representation of the included organizations.[102]

Newfoundland Power submitted that the Board has accepted the Canadian Commercial Industrial group as a reasonable comparator group for its executive since 1998 and that the Board has consistently determined that Newfoundland Power's executive compensation policies are reasonable.[103] Newfoundland Power noted the challenges associated with selecting a comparator group given the small number of investor-owned utilities and the view of its expert that crown-owned utilities should be excluded for comparison purposes as they have different funding and business models.[104] Newfoundland Power submitted that the correct test to apply is not whether the Canadian Commercial Industrial group is the most appropriate comparator but rather whether the comparator group is reasonable.[105] Newfoundland Power further submitted that no party presented evidence to show that the base salaries for executives forecast for 2025 and 2026 are unreasonable.[106]

In reply to the Consumer Advocate's recommended 20% reduction, Newfoundland Power submitted that the reduction is based on the compensation for the President and Chief Executive Officer at Hydro, and there is no information with respect to whether the role is equivalent to the same role at Newfoundland Power. Further Newfoundland Power noted that, in the opinion of the expert evidence, the compensation policy is not the same for crown-owned utilities as investor-owned utilities. Newfoundland Power pointed out that the Nova Scotia legislation referred to by the Consumer Advocate is not typical in Canada with regulators normally approving utility compensation practices and recovery in rates on the basis of whether they are reasonable and benefit customers. Newfoundland Power also submitted that there are a number of issues with the information referred to by the Consumer Advocate in his submission on the salaries of executives at certain crown-owned utilities, including the absence of evidence on the comparability of roles and the limited size of the comparator group.

[101] Consumer Advocate Submission, page 66.
[102] Newfoundland Hydro Submission, pages 9 to 10.
[103] Newfoundland Power submission, page 54, lines 8-18.
[104] Newfoundland Power Submission, page 116, line 5 to page 117, line 13.
[105] Newfoundland Power Submission, page 116, lines 5-15.
[106] Newfoundland Power Submission, page 94, lines 2-8.

Board Decision

The Canadian Commercial Industrial group has been used by Newfoundland Power in determining executive compensation since 1998.[107] This comparator group is comprised of 390 commercial industrial organizations across Canada, a number of which are involved in retail and motor vehicle operations.[108] Only three electrical utilities and three Atlantic Canadian organizations are included in the group and no Newfoundland and Labrador companies are included.[109] Newfoundland Power's consultant for executive and director compensation, Korn Ferry, found that it is reasonable for Newfoundland Power to use the Canadian Commercial Industrial Market as its comparator group and for it to use the median level of this comparator group as the basis for executive and director pay standards. It was Korn Ferry's opinion that Newfoundland Power's executive salaries are close to the market median.[110]

The Board notes that when Newfoundland Power first started using the Canadian Commercial Industrial group as the basis for executive compensation, additional information was also provided as to other comparators, including utilities, Atlantic Canadian companies and Newfoundland and Labrador companies.[111] This information was not provided in this proceeding.

The Board also notes that the Canadian Commercial Industrial group is not the comparator which is used by Newfoundland Power in determining compensation for its managerial and union employees. Managerial compensation and salary adjustments reflect compensation information from a number of peer groups, including Canadian organizations and utilities, Atlantic Canadian companies and Newfoundland and Labrador companies.[112] In addition, a different consultant, Wilson Towers Wyatt, is used in determining managerial compensation and this consultant used two comparator groups. One comparator included organizations from all industries nationally, excluding energy services and utility organizations, and the second was comprised of organizations in the energy services and utilities sectors, including crown-owned electrical utilities.[113] While compensation for union employees is based on collective agreements, the wage adjustments are generally negotiated in comparison to the wage rates paid by other electrical utilities in Atlantic Canada.[114]

Due to the different approaches taken by Newfoundland Power for each of the three employee groups, the salary adjustments are generally not the same. As set out in the table below, the

[107] PUB-NP-171.
[108] PUB-NP-171 (i).
[109] PUB-NP-173.
[110] Korn Ferry Report, page 4.
[111] PUB-NP-171; PUB Order No. P.U. 36(1998-1999), pages 34 to 36 and page 40.
[112] Transcript, June 17, 2024, page 92, line 4 to page 95, line 10.
[113] Transcript, June 17, 2024, page 11, line 4 to page 96, line 3.
[114] Transcript, June 14, 2024, page 82, lines 1-14.

adjustments for the executive and directors were higher than for the other groups in 2023 and 2024.[115]

Salary Adjustments		
	2023	**2024**
Union(clerical)[116]	2.0%	2.5%
Managers	2.0%	3.0%
Executive and Directors	3.6%	3.8%

Based on the evidence in this proceeding, the Board has concerns with respect to Newfoundland Power's approach to determining its salary adjustments for the executive and directors. The current approach resulted in salary adjustments which are higher for the executive and directors than for other employee groups. The evidence does not sufficiently explain why a different approach is taken for determining compensation for the executive and directors. It is not clear why different consultants are used and why different comparator groups are used. Newfoundland Power did not demonstrate why other comparators such as Canadian electric utilities, Atlantic or Newfoundland companies, are not used in determining executive and director compensation when they are used for the other employee groups. While some information on other possible comparators including crown-owned and Atlantic utilities, was provided by the Consumer Advocate, it was provided by way of submissions and as a result could not be tested through examination. The Board is not satisfied that the Canadian Commercial Industrial group continues to be a reasonable comparator for Newfoundland Power's executive and director compensation practices. The Board believes that Newfoundland Power should conduct a comprehensive review of executive and director compensation addressing the appropriate comparator groups as well as consistency between its employee groups and file a report with its next general rate application.

While the Board has concerns with respect to Newfoundland Power's approach to executive and director compensation, the Board will not reduce the 2025 and 2026 Test Year Operating Costs to reflect a reduction in base salary for executive and director compensation. The Board has determined that a productivity allowance should be applied to Newfoundland Power's Operating Costs, in part to reflect potential savings that Newfoundland Power may be able to achieve in the management of its Labour Costs. The Board will not implement a further reduction for the costs associated with Newfoundland Power's base salaries for the executive and directors at this time.

The Board finds that Newfoundland Power should file a report in relation to executive and director compensation with its next general rate application.

[115] The evidence does not indicate the 2025 and 2026 salary adjustments for the executive and directors or managers.

[116] PUB-NP-031 b). The craft collective agreement expired on June 30, 2022 and negotiations are ongoing.

4.2.2. Short-Term Incentive Plans

Newfoundland Power gives incentive payments in addition to base salaries to the executive and directors group based on performance.[117] Newfoundland Power's short-term incentive plan for the executive and directors was an issue in this proceeding. The regulated total short-term incentive payments for executive and directors including the pay for performance payments for managers, are forecast to be $1.5 million for 2025 and 2026. These payments were $1.3 million in 2022 and were forecast to be $1.4 million in 2023.[118] The Test Year amounts are based on labour inflation rate increases of 3.8%, 4.45% and 4.5% for 2024, 2025 and 2026, respectively over the 2023 forecast.[119]

Submissions

The Consumer Advocate submitted that Newfoundland Power's short-term incentive plan is not designed to target benefits for customers but is designed to incentivize the executive to do what is best for the shareholders.[120] He submitted that achievement of targets for safety, reliability and customer satisfaction should not require a bonus as they are part of the responsibility of the utility. In the Consumer Advocate's view, a controllable operating costs target ignores other costs such as capital costs and may be an incentive for more capital expenditures which results in higher depreciation and finance costs.[121] The Consumer Advocate submitted that while having an incentive plan may be reasonable for the utility, it is not reasonable or fair that customers pay for it. The Consumer Advocate recommended that all payments under the short-term incentive plan for executives should be paid by the shareholder, not customers.[122]

Newfoundland Hydro did not make any submissions on Newfoundland Power's short-term incentive plan.

Newfoundland Power submitted that it is not reasonable to disallow short-term incentive payments given that the short-term incentive plan has been reviewed and approved in the past by the Board, is consistent with regulatory practice and the evidence demonstrates that the plan benefits customers.[123]

Board Decision

The Board has previously ruled that certain costs associated with Newfoundland Power's short-term incentive plan may not be recovered from customers. Newfoundland Power is not

[117] Newfoundland Power has a long-term incentive plan for the executive though the associated costs are not included in regulated costs.
[118] PUB-NP-033.
[119] PUB-NP-033, Footnote 1.
[120] Consumer advocate submission, page 70, lines 3-6.
[121] Consumer Advocate Submission, page 69, lines 11-38.
[122] Consumer Advocate submission, page 70, lines 24-29.
[123] Newfoundland Power Submission, page 91, lines 1-2 and page 93, line 3.

permitted to recover 50% of the costs associated with the earnings, regulatory performance and cash flows components of the plan.[124] Payments in excess of 100% of the target percentage payouts also cannot be recovered. The evidence in this proceeding raises issues as to whether the short-term incentive plan for the executive and directors, as currently designed, provides appropriate incentives and whether it is appropriate for the costs to be recovered from customers.

The Board notes that the short-term incentive plan for the executive and directors requires that a minimum return on equity be met before there are any payouts. The target rate of return on equity is 90% of the forecast rate of return which is almost always exceeded by Newfoundland Power.[125] It is not clear why this target minimum was chosen as compared to other targets which may have more clear benefits for customers.

Short-term incentives for the executive and directors are determined through an assessment of corporate and individual performance. Corporate performance has a weight of 70% for the President and CEO and the vice-presidents and 50% for directors. Corporate performance components are based on Newfoundland Power's performance relative to weighted targets. Objective targets are set for performance in each area of corporate performance except regulatory, which are subjective. The weights given to the corporate performance target are shown below.[126]

2024 Corporate STI Performance Targets - Weighting	
Financial	
Earnings	30%
Controllable Operating Cost per Customer	10%
Safety	
All Injury Frequency Rate	12%
Quality Leading Indicators	8%
Reliability	
SAIDI (Outage Duration Index)	15%
Customer Satisfaction	
% of Satisfied Customers (as measured by Customer Satisfaction Survey)	15%
Regulatory	
Regulatory Performance	10%

Individual performance has a weight of 30% for the President and CEO and the vice-presidents and 50% for directors. Individual personal performance targets are subjective and are intended to encourage performance in the individual's specific areas of responsibility and support

[124] The five categories included in the corporate component of Newfoundland Power's 2024 short-term incentive plan: financial which includes earnings with a weighting of 30% and controllable operating costs per customer with a weighting of 10%, safety with a weighting of 20%, reliability with a weighting of 15%, customer satisfaction with a weighting of 15% and regulatory with a weighting of 10%.

[125] PUB-NP-147.

[126] PUB-NP-032, Attachment A.

corporate performance.[127] As the short-term incentive plan reflects subjective regulatory and individual performance targets, it is difficult to ascertain the benefits for customers.

Corporate performance targets are based on performance in previous years and the business plan for the upcoming year. The targets for customer service, reliability and safety are based on the average of the target achieved in each category over a set period. Poor performance in a year when a target is not achieved is reflected in determining the target for the next year.[128] This is evident with respect to reliability as the non-achievement of the targets in 2020 and 2023 resulted in the determination of a lower 2024 target. While it is accepted that targets should be achievable in the circumstances, the Board believes that this method of determining targets which reflect unsuccessful years may not provide a sufficient incentive to maintain and improve performance.

The Board notes that Newfoundland Power did not achieve the targets for all categories in 2020, 2022 and 2023, but significant short term incentive payments to the executive and directors were made in those years.[129] In particular, payments were made despite the fact that there has been a continuing trend of increasing operating costs per customer in recent years. While Newfoundland Power is not entitled to recover all of the costs associated with its short-term incentive plan for the executive and directors, the costs that are recovered from customers are significant, as set out in the table below.

Executive and Director Short-Term Incentive Payments
2022 and 2023 Actual

	2022A		**2023A**	
Executives	**($)**	**(%)**	**($)**	**(%)**
President & CEO	221,000	51.2	269,000	57.4
VP Customer Operations	128,000	41.2	137,000	45.8
VP Engineering & Energy Supply	115,000	36.3	141,000	43.0
VP Finance & CFO	112,000	36.5	141,000	44.5
Directors	385,300	16.5	438,300	19.4
Total	**961,300**		**1,126,300**	
Regulated	780,821		783,346	
Non-Regulated	180,479		342,954	
Total	**961,300**		**1,126,300**	

Source: NLH-NP-114

Based on the evidence, the Board is not satisfied that the current design of Newfoundland Power's short-term incentive plan for the executive and directors provides sufficient benefits for customers to support inclusion of the associated costs in the revenue requirement to be recovered from customers in 2025 and 2026. The evidence does not support the chosen target

[127] PUB-NP-032, Attachments B and C.
[128] Transcripts, June 14, 2024, page 100, lines 15-22 and page 39, lines 1-6.
[129] PUB-NP-009, Attachment A for targets and NLH-NP-114 for payments.

categories, and weights given to these targets, the subjective targets set for regulatory and individual performance, the minimum target rate of return on equity, or the way the targets are established. Newfoundland Power has not met its burden of demonstrating the value of the short-term incentive plan for customers. The Board finds that the costs of the short-term incentive plan for the executive and directors should be excluded from regulated costs. Before proposing recovery of costs from customers in future applications Newfoundland Power should conduct a comprehensive review of its short-term incentive plan for the executive and directors to ensure appropriate benefits for customers.

The Board finds Newfoundland Power's proposed Operating Costs should be reduced to reflect the exclusion of the costs associated with short-term incentive payments to the executive and directors from the 2025 and the 2026 Test Year revenue requirement.

5. COST OF CAPITAL

The Application seeks approval of a rate of return on equity for 2025 and 2026 of 9.85% on a common equity component of 45%, an increase from the current rate of return on equity of 8.5% with a common equity ratio of 45%. The requested increase in rate of return on equity was estimated to result in an increase in return reflected in rates of approximately 29.5%, from $49.2 million in 2023 Test Year[130] to $63.7 million[131] in 2026 Test Year. This was estimated to increase customer rates by approximately 1.5%.[132]

5.1. Legislative and Policy Framework

The legislative framework in this province provides guidance on the determination of Newfoundland Power's return. Section 80(1) of the **Act** states that "a public utility is entitled to earn a just and reasonable return as determined by the board on the rate base as fixed and determined by the board." In carrying out its duties the Board is required by section 4 of the **EPCA** to observe the power policy of the province as set out in section 3 of the **EPCA** and to apply tests which are consistent with generally accepted public utility practices. Section 3 (a) (iii) of the **EPCA** provides that the rates to be charged for the supply of power should provide sufficient revenue to enable the utility to earn a just and reasonable return so that it is "able to achieve and maintain a sound credit rating in the financial markets of the world." Section 3(b) of the **EPCA** also provides that power should be delivered to consumers at the lowest possible cost, in an environmentally responsible manner, consistent with reliable service.

In accordance with accepted regulatory principles, Newfoundland Power is entitled to a fair return which is one that is: (i) commensurate with the return on investments of similar risk; (ii) sufficient to assure financial integrity; and (iii) sufficient to attract the necessary capital. All three requirements must be met and no one requirement takes precedence over the other two.

[130] Newfoundland Power Additional Information, Exhibit 3.
[131] Application, Exhibit 5, page 1 of 9.
[132] Newfoundland Power Wholesale Rate Application, PUB-NP-005.

Assessing the fair return involves an assessment of the rate of return on equity as well as the utility's capital structure.[133] The rate of return on equity and the common equity ratio for Newfoundland Power are both issues to be determined by the Board in this proceeding in setting the fair return.

5.2. Newfoundland Power's Risk Profile

An assessment of Newfoundland Power's risk profile is required for the Board's consideration of a fair return for Newfoundland Power. Newfoundland Power relies on the expert opinion of Concentric that it is an above average business risk Canadian utility, which is the same position Newfoundland Power and Concentric first took in 2016.

Concentic compared Newfoundland Power's business risk to five other Canadian investor-owned utilities and concluded that Newfoundland Power has above average business risk compared to these Canadian utilities with a number of factors contributing to its higher risk profile, including its small size, its dependence on one supplier, weaker macroeconomic and demographic trends in the Province, more weather and storm related risk and more power supply risk due to the cost of the Muskrat Falls Project and additional costs for supply that were not previously anticipated.[134] Concentric also concluded that Newfoundland Power has somewhat higher business risk than its proxy group of U.S. electric utility companies. Concentric also considered Newfoundland Power's financial risk and concluded that, with its 45% common equity ratio, it has comparable financial risk to that of its Canadian and U.S. electric utility proxy groups, based on an analysis of deemed equity ratios and key cash flow and interest coverage metrics.[135]

The Consumer Advocate's expert, Dr. Booth, expressed the opinion that Newfoundland Power continues to be an average business risk Canadian utility with lower than average financial risk. Dr. Booth explained that he considered the cost and reliability implications of the Muskrat Falls Project in assessing Newfoundland Power's business risk. In his opinion, it is ratepayers not Newfoundland Power that bear any risk with respect to cost pressures and the reliability concern is a short-run problem that will be resolved.[136] He further explained that, in his opinion, neither the Board nor Government would see the utility financially harmed due to the recovery of the Muskrat Falls Project costs.[137]

Newfoundland Power took the position that it is an above average risk utility and relies on the opinion of Concentric for this position. In its submission Newfoundland Power referred to its dependence on a single supplier, including the implications of the Muskrat Falls Project, the continued reliance on the Holyrood plant, and the need to construct new sources of capacity as key factors in its business risks.[138] Newfoundland Power submitted that while the Rate Mitigation

[133] Order Nos. P.U. 32(2007); P.U. 43(2009); P.U. 13(2003); P.U. 18(2016); and P.U. 2(2019).
[134] Concentric Report, page 78, lines 3-13.
[135] Concentric Report, page 83, lines 21-23.
[136] NP-CA-028.
[137] NP-CA-028 and Booth Report, page 100, lines 2-10.
[138] Newfoundland Power Submission, page 26, lines 6-9.

Plan provides a level of certainty on customer rates until 2030, the certainty is offset by the high overall cost of the project and increasing cost pressures associated with mitigating the Labrador Island Link's reliability. In Newfoundland Power's opinion, the Muskrat Falls Project continues to be a risk in the near-and-longer term.[139] Newfoundland Power acknowledged that its business risk is comparable to that existing at the time of the last general rate proceeding with no material change.

The Consumer Advocate and Hydro submitted that Newfoundland Power's business risk remains consistent with 2016 when the Board determined that Newfoundland Power was an average risk utilty, and if anything, the risk is lower now related to Muskrat Falls as it is in operation and there is more certainty on rate implications due to the Rate Mitigation Plan. Both the Consumer Advocate and Hydro submitted that the Rate Mitigation Plan has removed the uncertainty in the near term with respect to costs and rate impacts of the Muskrat Falls Project. Hydro also noted that Newfoundland Power has not factored reliability concerns into its forecast and that recent experience with the Labrador Island Link should alleviate reliabilty concerns.[140]

The Board notes that Newfoundland Power and Concentric submitted that it is an above average risk utility for essentially the same reasons as relied on in the 2016 general rate application. At that time the Board determined that Newfoundland Power continued to be an average risk Canadian utility, while acknowledging that there were risks for Newfoundland Power associated with the Muskrat Falls Project. The Board finds that the evidence demonstrates that Newfoundland Power's historic risks including, its small size, harsh operating environment, dependence on a single supplier, relatively weaker provincial economic conditions, service territory demographics and low growth potential, all remain essentially the same as when last reviewed with no material change. The Board concludes that while there continues to be risks for Newfoundland Power associated with the Muskrat Falls Project in terms of reliable supply and costs, this risk may have reduced to some degree since the last general rate proceeding. The Board notes that Moody's Investors Service (Moody's) still continues to view Newfoundland Power overall as having low risk. Both Moody's and DBRS Morningstar (DBRS) have maintained Newfoundland Power's credit rating with no downgrade due to business risks, including from any that may arise due to the Muskrat Falls Project.[141] In its most recent update in October 2024 Moody's noted it had changed Newfoundland Power's outlook from stable to negative without any change in its rating.[142]

The Board finds that Newfoundland Power's business risks have not materially changed since it was reviewed by the Board in 2016 and Newfoundland Power continues to be an average risk utility compared to other Canadian utilities.

[139] Newfoundland Power Submission, page 28, lines 1-10.
[140] Hydro Submission, pages 4 to 5.
[141] Moody's Report, April 30, 2024 and DBRS Report, Exhibit 4 (1st Revision) page 1.
[142] Newfoundland Power Wholesale Rate Flow-Through Application, PUB-NP-006.

5.3. Capital Structure

The Application stated that the Board's view of the appropriateness of the capital structure has remained consistent since it was first approved in 1996 and noted that the Board has acknowledged that a strong equity component is needed to mitigate the impact of Newfoundland Power's relatively small size and low growth potential.[143] In Concentric's opinion, the current deemed equity ratio of 45% remains the minimum appropriate level given its assessment of Newfoundland Power's relative financial and business risks. Concentric concluded that Newfoundland Power's small size and operating environment, the challenging demographic and macroeconomic trends in the Province, and the elevated business risk due to the Muskrat Falls Project all continue to support a higher common equity ratio than other investor-owned utilities in Canada. Concentric also noted that regulatory protections for Newfoundland Power to mitigate business risks are generally similar to those for the operating companies in its U.S. electric utility proxy group, and the financial risk of Newfoundland Power with 45% common equity is comparable to that of its Canadian and U. S. electric utility proxy groups.[144] Concentric also noted that while Newfoundland Power's equity ratio is above that of other Canadain investor-owned electric utilities, it remains well below its U.S. peers.[145]

Dr. Booth stated that a 45% common equity ratio for Newfoundland Power is excessive compared to its Canadian peers. He recommended, as he has previously, that an average common equity ratio of 40% should be implemented and that if an immediate drop to 40% is considered too big a shock, the change could be phased in or a 5% preferred shares component could be implemented. Dr. Booth acknowledged that his recommendation of 40% common equity with a rate of return on equity of 7.70%, if accepted by the Board, would raise concerns with the credit rating agencies.[146]

Newfoundland Power submitted that as there has been no material change in circumstances that would justify a change in its capital structure since its last General Rate Application, the Board should maintain its equity ratio of 45%. Newfoundland Power noted that Dr. Booth's evidence did not identify any change in its business risk and that, in Concentric's opinion, its business risks remain the same and that it has higher than average business risk relative to its peers. Newfoundland Power also noted that credit rating agencies regard its 45% common equity ratio as a key financial strength required to mitigate its financial and business risks and weak financial flexibility. Newfoundland Power further submitted that Dr. Booth's recommendation of a 40% equity ratio and an rate of return on equity of 7.7% would result in Newfoundland Power having limited ability to issue first mortgage bonds.[147]

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[143] Application, page 3-20, lines 5 to page 3-21, line 7.
[144] Concentric Report, page 83, lines 2-27.
[145] Transcript, June 18, 2024, page 10, line 2 to page 11, line 1.
[146] Transcript, June 21, 2024, page 85, lines 2-22.
[147] Newfoundland Power Submission, page 34, lines 7-21.

The Consumer Advocate submitted that the Board can and should maintain an approved equity ratio of 45% for Newfoundland Power while reducing the rate of return on equity to 8.15%.[148] The Consumer Advocate noted that with this recommendation Newfoundland Power's weighted cost of capital would be similar to that of Maritime Electric, Nova Scotia Power and the Canadian electric average shown in Concentric's evidence.[149] The Consumer Advocate noted Dr. Booth's recommendation to reduce the equity ratio to 40% to bring it in-line with the Canadian utility average and said there is no basis for the 5%-6% extra equity thickness of Newfoundland Power.[150] The Consumer Advocate also submitted that Newfoundland Power's credit metrics would not be destabilized by virtue of a modest reduction in its common equity ratio.[151]

Hydro made no submissions on changes to Newfoundland Power's capital structure.

The Board has accepted a capital structure of up to 45% common equity for Newfoundland Power since 1996. This common equity component was supported on the basis of Newfoundland Power's business risks including its small size relative to its peers and its low growth potential. These factors still exist and Dr. Booth, the Consumer Advocate and Hydro all submit that there has been no material change in Newfoundland Power's business risks. Neither the Consumer Advocate or Hydro submitted that Newfoundland Power's equity component should be reduced at this time.

The Board notes that Newfoundland Power's capital structure has consistently been recognized by the credit rating agencies as a strength which positively impacts its credit ratings. Moody's, in a recent report, stated:

> While the ROE remains relatively low, it is mitigated by one of the highest deemed equity levels in Canada that remains unchanged at 45%.[152]

DBRS in its recent report described Newfoundland Power's equity component as *Excellent*.[153] While Newfoundland Power's common equity component is higher than the allowed equity of other Canadian investor-owned utilities the Board notes that the allowed common equity was recently increased for Nova Scotia Power and Fortis BC.[154] The Board is satisfied that a common equity ratio of 45% continues to be reasonable for Newfoundland Power.

The Board finds that Newfoundland Power's common equity component for rate setting purposes for the 2025 and 2026 Test Years should not exceed 45%.

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[148] Consumer Advocate submission, page 60, lines 17-19.
[149] Consumer Advocate submission, page 57, lines 1-14.
[150] Consumer Advocate Submission, page 34, lines 11-14.
[151] Consumer Advocate Submission, page 35, lines 15-16.
[152] Moody's Report, April 30, 2024, page 4.
[153] DBRS Report, Exhibit 4 (1st Revision) page 8.
[154] Concentric Report, page 55, Figure 33; PUB-NP-122 and PUB-NP-067.

5.4. Rate of Return on Equity

Newfoundland Power requested approval of a rate of return on equity for the 2025 and 2026 test years of 9.85% with a capital structure that includes 45% common equity. Newfoundland Power's current rate of return on equity of 8.5% was first approved by the Board in 2016 and has been in place since, following settlements which were accepted by the Board in the general rate application proceedings in 2019 and 2022.[155] Newfoundland Power stated that it has been able to maintain its financial integrity since 2016 with a rate of return on equity of 8.5% and a 45% common equity component but the proposed increase in the rate of return on equity is required to maintain its financial integrity in 2025 and 2026.[156]

The Consumer Advocate recommended a rate of return on equity of 8.15% with a capital structure including common equity of 45%.[157] The Consumer Advocate's expert, Dr. Laurence Booth recommended a rate of return on equity of 7.70% with common equity of 40%.

5.4.1. Market Conditions

According to Newfoundland Power the evidence indicates a shift in economic and market conditions compared to those existing at the time of its last general rate application. Newfoundland Power noted that both Concentric and Dr. Booth provided evidence that interest rates, long-term Canada bond yields and beta estimates have all increased since 2021.[158] In Concentric's opinion there has been a "fundamental shift" in the economy and capital market conditions since it last provided expert evidence in Newfoundland Power's 2022/2023 General Rate Application with the cost of capital higher for all companies, including utilities.[159] The shift is, in their opinion, due in large part because the extended period of declining interest rates and low inflation has come to an end. They noted that stock market volatility is down while investor confidence has improved, although utility shares are down.[160] In Concentrics's opinion "equity investors no longer perceive utilities as safe havens during economic downturns or periods of market distress" and these companies are trading more like the broad markets.[161]

Dr. Booth also concluded that there is a "more favorable economic market" than when he testified previously in Newfoundland Power general rate application proceedings.[162] He noted that financial market conditions are close to normal and equity markets are roaring rather than weakening.[163]

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[155] Order No. P.U. 18(2016) and Order Nos P.U. 2(2019) and Order No. P.U. 3(2022) Amended No. 2.
[156] Application, page 3-1; NLH-NP-052; and, Transcript, June 17, 2024, page 106, line 4 to page 107, line 16.
[157] Consumer Advocate Submission, page 60, lines 17-19.
[158] Newfoundland Power Submission, page 27, lines 13-16.
[159] Concentric Report page 9, lines 17-23.
[160] Concentric Report, page 10, lines 3-10.
[161] Concentric Rebuttal, page 28, lines 8-11.
[162] Booth Report, page 1, line 22 to page 2, line 2.
[163] Booth Report, page 36, lines 1-10.

5.4.2. Proxy Groups and Use of U.S. Data

The fair return concept is based on the return required by investors in the capital markets. As Newfoundland Power is not publicly traded, it is necessary to establish a group of companies that are both publicly traded and comparable to Newfoundland Power's business and financial characteristics to serve as a "proxy" for the purpose of the fair return analysis.[164] The selection of the appropriate proxy companies tends to be controversial as no one company or group of companies has exactly the same business and financial profile.

Concentric used both Canadian and U.S. proxy group companies for its analysis. Concentric reviewed the macroeconomic and investment environment in Canada and the United States. According to Concentric the economic and business environments of both countries are highly integrated and exhibit strong correlation across a variety of metrics, including GDP growth and government bond yields and that from a business risk perspective, they are ranked closely when compared against other developed and developing countries. Concentric concluded that there are no fundamental dissimilarities between Canada and the U.S. that would cause a reasonable investor to have a materially different return expectation for a group of comparable risk utilities in the two countries.[165] Concentric noted that the Ontario Energy Board, the Regie de l'energie and the Canadian Energy Regulator have accepted the use of U.S. data and proxy groups and the British Columbia Utility Commission ("BCUC") and the Alberta Utilities Commission ("AUC") recently accepted the use of a North American proxy group without adjusting the U.S. data.[166]

Concentric developed three proxy groups for analysis purposes: a Canadian proxy group, a U.S. proxy group and a North American proxy group. In Concentrics's opinion, Newfoundland Power is more comparable with respect to business risk to the companies in the U.S. proxy group than those in its Canadian proxy group and has somewhat higher business risk than the U. S. utilities in its North American proxy group.[167] In Concentrics's opinion, the North American Electric proxy group is the most representative of Newfoundland Power and it therefore places greater weight on the results for that group.[168]

While Dr. Booth did not support the use of a U.S. proxy group to estimate the fair return for a Canadian utility, he noted that, given the small sample of Canadian regulated utilities traded in the capital markets, Canadian regulators do consider U.S. data. Dr. Booth stated that he regards estimates of returns for U.S. utilities as biased high when applied to Canadian regulated utilities for three reasons: (i) the U.S. returns are mainly from riskier holding companies rather than operating companies; (ii) U. S. financial markets exhibit more risk than Canadian markets and have generated higher risk premia in the past where the realized market risk premium since 1926 has been 1.71% higher in the U.S. than in Canada; and (iii) although the regulatory principles are

[164] Concentric Report, page 28, lines 24-27.
[165] Ibid., page 27, lines 13-22.
[166] Concentric Report, pages 32 and 33 and Concentric Rebuttal, page 16, line 19 to page 17, line 22.
[167] Concentric Report, pages 78 to 82.
[168] Concentric Report, page 3, lines 15-17.

the same in both countries, their implementation is different.[169] In his opinion, adjustments must be made to the U.S. data in the determination of the fair return for a Canadian utility. Dr. Booth noted that the need to make adjustments to U.S. data has been recognized by Canadian regulators.[170] Dr. Booth stated that he includes consideration of the U.S. market risk premium data as well as other sources of data to help inform his judgement of the appropriate market risk premium to use in his analysis.[171] Dr. Booth took exception to the U.S. companies chosen by Concentric as proxies for Newfoundland Power as, in his opinion, all are riskier holding companies and are not sufficiently comparable to Newfoundland Power to be considered as reasonable proxies.[172]

Newfoundland Power submitted that Concentric's use of proxy groups that include U.S. utilities and unadjusted U.S. data in making its recommendation on the rate of return on equity is consistent with regulatory precedent.[173]

The Consumer Advocate submitted that the use of unadjusted U.S. data is not reasonable as the U.S. utilities selected by Concentric in its proxy groups are riskier than Newfoundland Power and there are still significant differences between the U.S. and Canadian capital and financial markets such that a downward adjustment should be made if U.S. data is considered. The Consumer Advocate submitted that a downwards adjustment consistent with the Board's past practice of applying a downward adjustment of 50-100 basis points should be applied to U.S. data.[174]

Hydro made no submission on the proposed proxy groups but noted that the use of a North American proxy group without adjustment results in a return on equity that is the second highest of Canadian gas and electric utilities.[175]

The Board has previously accepted that the limited availability of Canadian data requires the use of U.S. data in certain circumstances and that the integration of Canadian and U.S. financial markets supports this approach, however, the Board has applied a downward adjustment of 50 -100 basis points to the U.S. data. In 2016 the Board stated:

> The Board accepts that the limited Canadian data may require the use of U.S. data in some circumstances, and also that integration of Canadian and U.S. financial markets may support this approach. However, the Board does not believe that the integration of these markets means that the U. S. utilities should be considered the same as Canadian utilities. While the Board acknowledges that other Canadian regulatory boards have recently determined that it is not necessary to adjust the U. S. utility data, the Board continues to believe that an adjustment is appropriate. The Board believes that there are differences in risk and associated returns between Canadian and U. S. utilities and is not satisfied that the results

[169] Booth Report, page 75, lines 6-26.
[170] Booth Report, page 85, lines 9-12.
[171] Booth Report, page 85, lines 16-22.
[172] Booth Report, page 78, lines 1-2.
[173] Newfoundland Power Submission, page 36, lines 6-14.
[174] Consumer Advocate Submission, page 38, lines 11-30.
[175] Hydro Submission, page 6, lines 7-14.

> from using U.S. data, in the form of a proxy group of companies, can be accepted without adjustment to account for these differences. In Order No. P.U. 13(2013) the Board accepted a downward adjustment of 50-100 basis points in relation to the U.S. utility results. Dr. Booth's evidence is that an adjustment in this range remains appropriate. [176]

This issue has been considered recently by both the BCUC and the AUC. The BCUC endorsed the reasonableness of using U.S. market data and proxy groups in light of the small sample size of Canadian comparators notwithstanding the jurisdictional differences [177] The BCUC accepted the use of U.S. data and stated that the weighting to be given was a matter of judgement in the Board's discretion.[178] The BCUC gave primary weighting to Concentric's North American proxy group. The AUC also considered the use of U.S. proxy companies and U.S. data in its consideration of the fair return due to the relatively limited number of Canadian publicly traded utilities, the prevalence of U.S. business operations among publicly traded Canadian utilities, investors' tendency to consider utility opportunities in both the U.S. and Canada, the globalization of the world economy and integration of North American capital markets.[179] The AUC determined that the U.S. comparators were sufficiently comparable for use in the rate of return on equity analysis but found the Alberta utilities were at the low end of risk present in the comparator groups. The AUC found that "a significant amount of judgement must be applied" when interpreting the data from the comparator groups when determining the return for Alberta utilities.[180]

The Board accepts that consideration of U.S. data, including the use of U.S. proxy companies' data, is appropriate in the consideration of a fair return for Newfoundland Power given the limited number of publicly traded Canadian utilities, the increasing integration of Canadian and U.S. markets, and the reality that Canadian investors look to both the Canadian and U. S. markets. The Board continues to believe that there are differences in risk and associated returns between Newfoundland Power and the companies in the proxy groups and between the U.S. and Canadian markets that must be recognized. The Board notes the recent BCUC and AUC decisions found that judgement must be exercised when considering data from the U.S. Having considered the evidence, the Board will consider U.S. data to help inform its judgement on the fair return. The Board believes that there are differences that require the use of discretion in considering the weighting to be given to U.S. data but will not specify a specific downward adjustment as it has in the past. The Board accepts that the use of U.S. data, including the inclusion of U.S. companies in proxy groups, is reasonable and will exercise its judgement in the weighting to be given to such data in determining the fair return for Newfoundland Power.

[176] Order P.U. No.18(2016), page 29, lines 16-27.
[177] Decision and Order G-236-23, dated September 5, 2023, pages 15 to 16.
[178] Ibid., page 16.
[179] Decision 27084-D02-2023, dated October 9, 2023, page 22, paragraph 103.
[180] Ibid., page 22, paragraph 104.

5.4.3. Methodologies for Determing the Rate of Return on Equity

A number of methodologies are used to estimate the appropriate rate of return on equity to be used for utility rate setting. The two most common methodologies considered by Canadian regulators are the Capital Asset Pricing Model (CAPM) and the Discounted Cash Flow (DCF) method.

Concentric relied on multiple methodologies in this proceeding to estimate the fair return for Newfoundland Power, including CAPM, DCF and the Bond Yield Plus Risk Premium(Risk Premium) methods. In its opinion no one model can exactly pinpoint the correct rate of return on equity, rather multiple tests should be considered. Concentric stated:

> Although each model brings a different perspective and adds depth to the analysis, each model has its own inherent limitations and should not be relied upon individually without corroboration from other approaches. Regardless of which analyses are used to estimate the investor-required ROE, analysts must apply informed judgement to assess the reasonableness of results and to determine the appropriate weighting to apply to results under prevailing capital market conditions.[181]

Concentric provided the estimated fair return for its three proxy groups using the Average CAPM, the DCF, both Constant Growth and Multi-Stage, and the Risk Premium methods.

According to Dr. Booth the CAPM model is the premier model for estimating the fair return for a utility and is the model used by most regulatory boards in Canada. He explained that it is widely used because it is "intuitively correct". It captures the time value of money with the long Canada bond yield as the risk-free rate and the risk value of money with the market risk premium. It also captures the tax value of money. Dr. Booth also completed a DCF analysis which he used to inform his judgment on the appropriate rate of return on equity to recommend for a utility. Dr. Booth also considers the views of independent third parties on the required returns.

CAPM

The CAPM method requires the determination of the risk-free rate, which reflects the return on an investment with no risk: the market risk premium, which reflects the return of the overall market; and the beta; which reflects the utility's risk relative to the overall market. In addition, it is common to include an adjustment for flotation costs and financing flexibility.

- Concentric estimated a risk-free rate of 3.52% for Canada and 3.98% for the U.S. In Concentric's opinion these estimates are low given the current 30-year bond yields.[182] Concentric's risk-free rates were lower in 2022, 2.54% for Canada and 3.0% for the U.S. Dr. Booth assumed the risk-free rate is 3.8% which he views as the " normal" forecast long-term Canada bond yield. In his opinion Canada is getting closer to normal in the

[181] Concentric Report, page 34, lines 1-6.
[182] Concentric Report, page 43, line 2 to page 44, line 2.

capital markets than in past Newfoundland Power rate proceedings.[183] Dr. Booth's risk-free rate was the same in 2022, as he estimated a forecast long Canada Bond Yield of 3.07 but added an adjustment of a 0.8.

- Concentric's market risk premium is 6.39% which is based on the average of the Canadian historical market risk premium of 5.62% and the U.S. of 7.17%.[184] Concentric presented the historical and forward-looking market risk premium for Canada and the U.S. but relied on the historical market risk analysis in its recommendation to "temper" the results.[185] Concentric's market risk premium was higher in 2022.[186] Dr. Booth estimated a market risk premium of 5.5% to 6.0%. Dr. Booth used the historical approach, based on capital market history from 1926 to 2023, to estimate the market risk premium which he estimated to be 4.87% in Canada and 6.58% in the U.S. Dr. Booth also considered the results of the Fernandez survey of expected market risk premiums and analyses completed by third parties of the market risk premium to inform his judgement of the appropriate market risk premium.[187] In 2022 Dr. Booth estimated a lower market risk premium of 5.0% - 6.0%.
- Concentric estimated a beta of .86. Concentric used adjusted betas as in its opinion empirical studies have shown that that an individual company's beta is more likely than not to move toward the market average of 1.0 over time.[188] Concentric's betas were .78 and .87 for the Canadian proxy group, .89 for the U.S. proxy group and .86 and .87 for the North American proxy group.[189] In 2022 Concentric's beta was slightly higher at .88. Dr. Booth placed slightly higher weight on the most recent beta estimates and judged a range of .50 -.60 to be reasonable. Dr. Booth did not use adjusted betas. In his opinion, utility betas do not tend towards 1.0 but towards their grand mean. He estimated the beta using five years of monthly data and looked to other estimates including, individual companies, the U.S. instead of the TSX as a market proxy, estimates from third parties, and a sample of U.S. gas and electric utilities.[190] In 2022 Dr. Booth's beta was lower at .45 - .55.
- Both Concentric and Dr. Booth included an adjustment for flotation costs and financial flexibility of 0.50%.

Concentric's CAPM analysis resulted in a return of 9.57% for the Canadian proxy group, 10.15% for the U.S. proxy group and 9.86% for the North American proxy group.[191] In Concentric's opinion the North American proxy group is the most representative of Newfoundland Power so it places greater weight on the results for that group. Concentric based its recommendation on the return on equity on the more conservative historical market risk premium analysis. In 2022

[183] Booth Report, page 3, lines 19-25.
[184] Concentric Report, Exhibit JMC-8.2.
[185] Concentric Report, page 46, lines 4-22.
[186] 2022-2023 Newfoundland Power General Rate Application, Volume III, Cost of Capital: Mr. James Coyne, Concentric Energy Advisories Inc., page 45.
[187] Booth Report, page 42, lines 1-13 and page 44, lines 3-6.
[188] Concentric Report, page 44, lines 4-11.
[189] Concentric Report, Exhibit JMC - 8.2, pages 1 to 2 and page 44, Figure 27.
[190] Booth Report, page 44, line 11 to page 45, line 24.
[191] Concentric Report, Exhibit JMC - 8.2, pages 1 and 2.

Concentric's historical CAPM results were higher at 10.43% for the Canadian proxy group, 10.91% for the U.S. proxy group, and 10.56% for the North American proxy group.

Dr. Booth's overall conditional CAPM estimate is a rate of return on equity of 7.70% within a range of 7.28% to 8.13%. Dr. Booth included a credit risk adjustment of 0.23% to account for what he regards as a too low an estimate due to the current slight slowdown in the capital markets.[192] In 2022 Dr. Booth's CAPM result was lower at 7.37% in a range of 6.77%-7.97% with a credit risk adjustment of 0.15% to 0.30%.

DCF Method

Concentric's DCF results, including the adjustment for flotation costs and financial flexibility, resulted in a return of 10.17% for the Canadian proxy group, 9.38% for the U.S, proxy group and 9.42% for the North American proxy group.[193] Concentric used the Constant Growth and the Multi-Stage DCF models to estimate the rate of return on equity for each of its three proxy groups. The Constant Growth model assumes a constant average growth rate for earnings and dividends, a stable dividend payout ratio, a constant price-to-earnings multiple and a discount rate greater than the expected growth rate. Concentric relied on the earnings growth estimates from four different sources with no adjustment for analyst bias. In Concentric's opinion concerns as to bias in constant growth estimates are not a valid concern and projected analyst growth rates are reasonable by historical standards. Concentric noted that historically dividends have tracked reasonably well with earnings growth so that earnings growth is a reasonable proxy for dividend growth. The Multi-Stage DCF method used by Concentric tempers the assumption of constant growth with a three-stage approach based on near-term, transitional and long-term growth rates.[194] Concentric relied on the Multi-Stage DCF analysis in making its recommendation on the return for Newfoundland Power. In 2022 Concentric's Multi-stage DCF results were 10.86% for Canada, 9.48% for the U.S., and 9.44% for North American proxy groups.

Dr. Booth completed a DCF analysis of the overall Canadian and U.S. stock markets and testified that he uses the DCF analysis as a check in terms of what is a reasonable rate of return to recommend.[195] Dr. Booth's DCF results ranged from 8.1% to 8.75% for the Canadian market and 6.84% to 9.6% for the U.S. Market which would also require a flotation cost adjustment.[196] In Dr. Booth's opinion, these results are not appropriate to use by themselves in estimating the fair return. He explained that these results are "simple estimates using average numbers" and are presented to show that while the DCF and CAPM estimates are consistent over long periods of time, they both have problems when used mechanically during periods of high and low bond yields.[197] In Dr. Booth's opinion any DCF estimate relying on short run earnings growth is biased

[192] Booth Report, page 48, line 17 to page 49, line 12.
[193] Concentric Report, page 85, Figure 43.
[194] Concentric Report, page 39, lines 1-28.
[195] Transcript, June 21, 2024, page 7, line 16 to page 8, line 9.
[196] Booth Report, page 53 and page 72.
[197] Booth Report, page 58, lines 21-24.

high and as well, there is inherent bias in analysts' forecasts. In his view, while the Multi-Stage method does moderate this bias it is still present in the model.[198]

Risk Premium Method

Concentric's Risk Premium method results ranged from 10.26% to 10.44%. Concentric used a regression analysis with historical authorized returns from U.S. electric utilities to estimate the equity risk premium. Concentric used data from 1992-2023 from 717 integrated U.S. electric utilities and the U.S. government 30-year treasury yield to perform the analysis. Concentric explained that it had to rely on U.S. data as there aren't sufficient Canadian return on equity decisions to develop a meaningful regression analysis.[199]

Dr. Booth did not use the Risk Premium method.

5.4.4. Expert Recommendations on Rate of Return on Equity

Concentric recommended that Newfoundland Power's cost of equity be set at 9.85% with common equity of 45%.[200] In 2022 Concentric recommended a rate of return on equity of 9.8%. Concentric relied on the results of three methodologies to estimate a fair return for Newfoundland Power for the 2025 and 2026 Test Years. According to Concentric judgement is required in the selection of the models, the weighting to be given the models, the selection of the input data and the interpretation of the results. Concentric stated that it minimizes the role of judgement by using market data rather than its judgment for inputs into the various models.[201] Concentric recommended what it called a "conservative estimate" based on the Multi-stage DCF, CAPM with a historical market risk premium and the Risk Premium model. In Concentric's opinion the North American proxy group is the most comparable to Newfoundland Power. Concentric stated:

> Regardless of which analyses are used to estimate the investor-required ROE, analysts must apply informed judgement to assess the reasonableness of results and to determine the appropriate weighting to apply to results under prevailing capital market conditions.[202]

[198] Booth Report, page 52, lines 16-22 to page 53, lines 1-2.
[199] Concentric Report, page 50.
[200] Concentric Report, page 4, lines 1-12.
[201] Transcript, June 19, 2024, pages 8 to 10.
[202] Concentric Report, page 34, lines 4-6.

Concentric's results are shown below.

Concentric's Rate of Return on Equity Results			
	CANADIAN UTILITY PROXY GROUP	**U.S. ELECTRIC PROXY GROUP**	**NORTH AMERCIAN ELECTRIC PROXY GROUP**
MULTI-STAGE DCF	10.17%	9.38%	9.42%
HISTORICAL CAPM	9.57%	10.15%	9.86%
RISK PREMIUM		10.26%	10.26%
AVERAGE	**9.87%**	**9.93%**	**9.85%**

Source: Concentric Report, page 4, Figure 2.

Dr. Booth recommended a rate of return on equity of 7.70% in a range of 7.28% - 8.13% with a common equity ratio of 40%.[203] In 2022 Dr. Booth recommended a rate of return on equity of 7.5%. Dr. Booth relied primarily on the CAPM method with DCF analysis performed to test the reasonableness of his adjusted CAPM results. He also considered the forecast of third parties to help inform his judgement on the appropriate market risk premium and the appropriate beta to use in his estimate of the appropriate rate of return on equity to recommend for Newfoundland Power.[204] Dr. Booth acknowledged the role that judgement plays in the determination of his opinion. He stated that he considers the opinions of third parties in informing his judgement on the market risk premium, and that he uses judgement in the determination of the appropriate beta and the application of a credit risk adjustment.[205] Dr. Booth's overall CAPM fair return estimates are shown below.

Dr. Booth's Rate of Return on Equity Results		
	Low	**High**
Forecast long Canada bond yield	3.80	3.80
Credit risk adjustment	0.23	0.23
Utility risk premium	2.75	3.60
Adjustment to ROE	0.50	0.50
Estimate	**7.28**	**8.13**

Source: Booth Report, page 49.

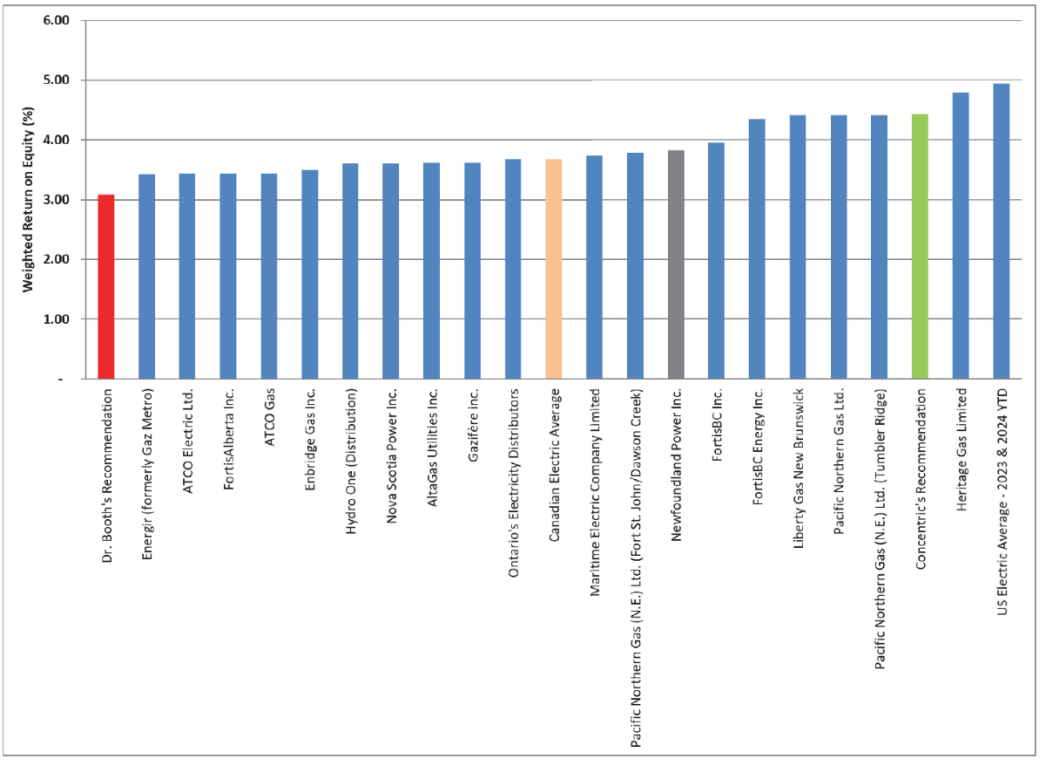
5.4.5. Other Allowed Utility Returns

The fair return standard requires that the return authorized for Newfoundland Power is commensurate with the return on investments of similar risk. As a result, it is useful to look at

[203] Booth Report, page 49, lines 1-13; page 72; page 112, line 21 to page 113, line 8.
[204] Booth Report, page 42, line 15 to page 44, line 6; page 45, lines 3-14 and page 72.
[205] Transcript, June 20, 2024, page 207, line 8 to page 208, line 10.

how Newfoundland Power's weighted rate of return on equity compares to other investor-owned electrical utilities. Both Concentric and Dr. Booth included this type of analysis in providing their opinions. The following figure, prepared by Concentric and updated during the hearing, illustrates Newfoundland Power's weighted rate of return on equity in comparison to other electric and gas utilities in Canada and the U.S.[206]

Weighted ROE for Canadian IOUs



Source: Undertaking #6.

Newfoundland Power's weighted rate of return on equity is just slightly above the average in the chart. Acceptance of Dr. Booth's recommendation would result in Newfoundland Power having the lowest weighted rate of return of Canadian investor-owned electric utilities while acceptance of Concentric's recommendations would result in Newfoundland Power having the highest weighted rate of return on equity of investor-owned electric utilities in Canada.

5.4.6. Credit Ratings and First Mortgage Bond Considerations

The fair return standard requires that Newfoundland Power's fair return must be sufficient to assure its financial integrity and to attract necessary capital. As a result, the implications on Newfoundland Power's credit ratings must also be considered in determining a rate of return on equity. Newfoundland Power maintains an investment grade credit rating from two rating agencies: Moody's Investors Service ("Moody's") and DBRS Morningstar ("DBRS").

[206] Undertaking #6. The weighted return on equity is the product of the return on equity multiplied by the common equity ratio.

Newfoundland Power has a credit rating of Baa1 from Moody's. In its April 2024 report Moody's stated that Newfoundland Power's outlook was stable.[207] It described Newfoundland Power as having "low business risk as a primarily electric transmission and distribution cost-of-service regulated utility" with its 45% equity capital among the highest in Canada. Its credit strengths were described as being low risk, the existence of a supportive regulatory environment and its track record of achieving allowed returns. Its credit challenges were described as the growth in power cost deferrals, weak cash flow metrics which were forecast to improve and increased risk of delayed cost recovery as costs associated with the Muskrat Falls Project add to rate pressures. Moody's explained that temporary weak financial metrics were caused by the under-recovery of power costs in 2023 which are expected to be recovered under existing approved cost recovery mechanisms. Moody's stated that an upgrade in Newfoundland Power's credit rating is unlikely without further clarity on the timing, size and implications of rate increases related to Muskrat Falls, and if its Cash Flow from Operations ("CFO") pre-working capital ("W/C") to debt metric is forecast to be sustained above 18% or if Newfoundland Power sees an improvement in its regulatory framework. Factors that could lead to a downgrade were said to be a decline in regulatory support, including delays in recovering costs or an inability to earn allowed returns and CFO pre W/C to debt sustained below 14%. Moody's issued an update in October 2024 noting that it had changed Newfoundland Power's outlook from stable to negative without any change to its Baa1 issuer rating and A2 first mortgage bond rating.[208] Moody's explained that the negative outlook reflects delays in cost recovery that have adversely affected Newfoundland Power's financial performance and credit profile and are likely to persist for the next several years given regulatory concerns about the pace of rate increases.

DBRS gives Newfoundland Power an "A" credit rating.[209] In a 2024 report DBRS stated that all trends for Newfoundland Power remain stable, including stable regulated electricity operations, a reasonable regulatory framework and steady key credit metrics. DBRS noted there had been no material changes to Newfoundland Power's business risks in the past year and that DBRS considers the greatest uncertainty to be a potential rate shock related to the Muskrat Falls project which risk it will continue to monitor. DBRS described Newfoundland Power's strengths as a stable and supportive regulatory environment, a solid financial profile, and a stable customer base. Its challenges were said to be uncertainty about rate shock due to the Muskrat Falls Project, weak economic outlook and limited population growth and reliance on a single supplier. In an October 2024 update DBRS confirmed the Issuer Rating and First Mortgage Bonds rating of Newfoundland Power at "A" with stable trends but noted that it remains concerned about current rate pressures and that future rate increases for recovery of Newfoundland Power's costs may be more challenging. DBRS stated that it may lower its score on the Energy Cost Recovery and Capital and Operating Costs Recoveries considerations if the recovery of purchased power costs and other costs of service continue to be delayed into future and ongoing rate cases.[210]

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[207] Moody's Report, dated April 30, 2024, pages 1 to 2.
[208] Newfoundland Power Wholesale Rate Flow-Though Application, PUB-NP-006.
[209] Exhibit 4 (1st Revision), DBRS Report, dated October 13, 2023, pages 1 to 2.
[210] Newfoundland Power Wholesale Rate Flow-Though Application, PUB-NP-006.

Evidence was filed that illustrated the impact on Newfoundland Power's credit metrics for proforma 2026 financial results of various rate of return on equity and common equity components.[211] Based on the evidence the CFO/Debt coverage metric has the highest weighting of Moody's credit metrics.[212] Assuming a rate of return on equity ranging from 8.25% to 9.25% and a 45% common equity component, Newfoundland Power's CFO/Debt coverage metric would range from 17.1% to 17.9%[213] which is within the range of 16% to 18% required by Moody's to maintain Newfoundland Power's current credit rating. Based on this, Concentrics's recommendations of 9.85% with 45% equity would result in a CFO/Debt coverage metric of 18.4% in excess of that required to maintain Newfoundland Power's credit rating. Dr. Booth acknowledged that his recommendations of a return of 7.7% return with a common equity of 40% would raise concerns for the credit rating agencies.[214] Newfoundland Power's currently approved 8.5% rate of return on equity and 45% common equity component produces a CFO/Debt coverage metric of 17.3% which is also within the range set out by Moody's.[215] According to evidence provided in Newfoundland Power's subsequently filed Wholesale Rate Flow-Through Application, the 2026 Test Year forecast credit metrics may be impacted by a change in the assumption of full recovery of its costs on July 1, 2025 and of amounts in the RSA within one year.[216]

Newfoundland Power submitted that consideration must also be given to the other factors considered by the rating agencies, including the regulatory framework and the ability to recover costs since the maintenance of its credit rating is influenced not only by credit metrics but by other factors which are qualitative.[217] Both Moody's and DBRS have noted the importance of a supportive regulatory regime.[218] According to Newfoundland Power:

> It is clear that the credit rating agencies consider the existing supportive regulatory environment as a credit strength of Newfoundland Power. Further, both rating agencies recognize the Company's longstanding 45% common equity component of its capital structure as a key credit strength. A reduction in the 45% common equity ratio could result in a re-evaluation of regulatory support by the rating agencies.[219]

Newfoundland Power's Vice-President of Finance and Chief Financial Officer, Ms. London testified:

> So, from my perspective any common equity below 45 percent would cause me concern, and when we look at return on equity, returns have been increasing across Canada and in assessing the overall comparability of returns, anything below 8.5 percent would certainly

[211] PUB-NP-061.
[212] Transcript, June 17, 2024, page 122, lines 2-11.
[213] PUB-NP-061, Table 5.
[214] Transcript, June 21, 2024, page 76, lines 12 to page 77, line 5.
[215] PUB-NP-061, Table 5.
[216] Newfoundland Power Wholesale Rate Flow-Though Application, PUB-NP-006.
[217] Newfoundland Power Submission, pages 29 to 30.
[218] Exhibit 4 (1st Revision), Moody's Report, April 30, 2024.
[219] PUB-NP-063 (1st Revision).

> cause me concern, but returns have been increasing as well. So, I think that's something that needs to be considered.[220]

Newfoundland Power's First Mortgage Trust Deed that secures its first mortgage bonds requires an earnings test interest coverage of 2.0 times or higher for it to issue additional bonds. Evidence was filed that shows the impact on the earnings test interest coverage at various rates of return on equity and common equity ratios. This evidence shows that at 45% common equity and rate of return on equity varying from 8.25% to 9.85%, the earnings test interest coverage would be satisfied. The earnings test interest coverage at 45% common equity and a rate of return on equity of 8.5% would be 2.32 and 2.19 times for its first mortgage bonds in 2026 and 2027 respectively. The earnings test interest coverage has ranged from 2.18 to 2.41 times for the past six issues with an average of 2.31 times.[221] Ms. London testified that to have a reasonable degree of flexibility 2.2 would provide sufficient flexibility.[222]

5.4.7. Submissions

Newfoundland Power submitted that the proposed increase in the rate of return on equity to 9.85% is based on Concentric's recommendation and on market dynamics that have changed significantly since 2021. It also reflects the fact that returns for Canadian investor-owned utilities have generally increased since 2021 with allowed returns, excluding Newfoundland Power, ranging from 9.0% to 9.65%, an increase from the range of 8.5% to 9.35% at the time of the last general rate proceeding. Newfoundland Power noted that Dr. Booth's recommendation of 7.70% rate of return on equity is 80 basis points below Newfoundland Power's existing return, which is currently the lowest authorized rate of return for any investor-owned regulated Canadian utility and is 130 basis points lower than the authorized rate of return of any other investor-owned Canadian utility.[223]

According to Newfoundland Power Concentric's recommendation of 9.85% satisfies the requirements of the fair return standard. Newfoundland Power submitted that Concentric's use of multiple methods to determine the cost of capital ensures that the return estimates that are considered include all relevant information that investors consider. It is also consistent with the approach used by Canadian regulators. It also noted that the Risk Premium Method used by Concentric but not Dr. Booth had recently been considered by the BCUC.[224]

Newfoundland Power submitted that Dr. Booth's recommendation of a 7.7% rate of return on equity with 40% common equity does not satisfy the fair return standard. This recommendation does not reflect a return comparable to other investor-owned Canadian electric utilities, is inconsistent with the maintenance of its creditworthiness and would impair future access to

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[220] Transcript, June 17, 2024, page 133, lines 7-15.
[221] PUB-NP-064.
[222] Transcript, June 17, 2024, page 134, line 16 to page 135, line 7.
[223] Newfoundland Power Submission, page 35, lines 4-17 and page 39, lines 2-5.
[224] Newfoundland Power Submission, page 38.

least cost financing.[225] In Newfoundland Power's view there are issues with Dr. Booth's CAPM analysis, including Dr. Booth's use of unadjusted betas. It submitted that the use of unadjusted betas is unreasonable with the range of beta coefficients used by Dr. Booth based on his subjective judgement only. It further submitted that while Dr. Booth has increased the range of betas he uses in his CAPM analysis since 2021, they are not based on current market data for companies that are comparable in risk to Newfoundland Power. Newfoundland Power noted that Concentric uses Blume-adjusted betas in its CAPM analysis with the betas based on objective market data from Bloomberg and Value Line.[226] According to Newfoundland Power Dr. Booth's reference to the Fernandez survey to inform his estimate of the market risk premium in his CAPM analysis is flawed as the survey is biased to those who use it and it is not clear from the responses how the participants derived their market risk premiums or for what purpose.[227] With respect to the DCF analysis, Newfoundland Power submitted that Dr. Booth's DCF analysis has limited value as much of it is based on historical data and does not provide a forward-looking estimate for the return.[228] Newfoundland Power noted that when Dr. Booth used forecast earnings and sustainable growth rates in his DCF analysis a similar result to Concentric's was produced when an adjustment is made for flotation costs.[229]

The Consumer Advocate submitted that the Board can and should maintain an approved equity ratio of 45% and recommended a rate of return on equity of 8.15%.[230] This would provide a weighted cost of capital within the range of other Canadian electric utilities, including Maritime Electric, Nova Scotia Power and the Canadian electric utilities average.[231] The Consumer Advocate also referred to the estimates of a pension actuary on the equity market returns to support his recommendation.[232] The Consumer Advocate submitted that the Board should adopt a practical approach that is fair to Newfoundland Power and its customers and noted that the experts' recommendations varied from a low of 7.7% to as high at 9.85%, a gap of 215 basis points. The Consumer Advocate submitted that Newfoundland Power's proposals for its return on equity and its common equity ratio would cause it to become "potentially relatively most profitable Canadian electric utility."[233] However, partial acceptance of Dr. Booth's recommendations could occur without its weighted cost of capital being significantly altered relative to other Canadian electric utilities.[234]

With respect to the use of appropriate methodologies to estimate the fair return, the Consumer Advocate referred to the Board's 2016 order which gave primary consideration to the CAPM method along with other evidence. He also referred to Dr. Booth's evidence that the DCF method

[225] Newfoundland Power Submission, page 42, lines 12-19.
[226] Newfoundland Power Submission, page 41, line 14 to page 42, line 10.
[227] Newfoundland Power Submission, page 41, lines 6-12.
[228] Newfoundland Power Submission, page 40, lines 1-8 and line 25 to page 41, line 4.
[229] Newfoundland Power submission, page 40, lines 1-5.
[230] Consumer Advocate Submission, pages 60, lines 17-19.
[231] Consumer Advocate Submission, page 56, line 40 to page 57, line 14.
[232] Consumer Advocate Submission, page 57, line 19 to page 58, line 14.
[233] Consumer Advocate Submission, page 53, lines 32-38.
[234] Consumer advocate Submission, page 54, lines 34-37.

should be rejected as a method to estimate the fair return and summarized Dr. Booth's concerns about using the constant growth DCF method given the existence of analysts' bias and the assumption that growth goes on in perpetuity. The Consumer Advocate noted that while the Multi-Stage DCF method also has the same issue of analysts' bias, in Dr. Booth's opinion, it is to a lesser degree. Dr. Booth only uses the DCF method to help inform his judgement on the fair return after he makes adjustments for analysts' bias and uses growth rates at sustainable levels.[235] The Consumer Advocate submitted that Dr. Booth's approach to, and, his estimate of beta is well founded.[236]

In its reply Newfoundland Power noted that the Consumer's Advocate's submission on the fair return is different than his own expert, it relies on a simple mathematical exercise using only two Canadian utilities data which is not a reasonable proxy group and its comparison to pension returns to estimate a utility's return is not supported by the evidence.[237] Newfoundland Power stated the method used by the Consumer Advocate to support his recommendation on the fair return does not recognize the foundational basis of a utility's capital structure and rate of return on equity. According to Newfoundland Power the Consumer Advocate does not provide a sufficient analysis of Newfoundland Power's risk profile relative to other comparable utilities and takes an approach unfounded in regulatory practice.[238]

Hydro submitted that Newfoundland Power has not demonstrated that an increase in its return is necessary to meet the fair return standard or that the existing return does not already meet the fair return standard.[239] According to Hydro the use of the North American Proxy Group, without any adjustment, results in a proposed return for Newfoundland Power that is the second highest weighted return of Canadian electric and gas investor-owned utilities while its current weighted return with its authorized return of 8.5% and common equity ratio of 45% is already above the Canadian electric average.[240] Hydro noted that an increased return for Newfoundland Power would impact Hydro's revenue requirement, inclusive of payments made to cover Muskrat Falls Project costs under the Transmission Funding agreement, and this is a material fact in considering the impact of the proposals in the Application on customers. It submitted that the Board has the jurisdiction to balance Newfoundland Power's right to earn a fair return with the overall impact on customers.[241]

In reply Newfoundland Power submitted that Hydro has a conflict of interest with respect to Newfoundland Power's return on equity as it receives the same return on equity by virtue of an Order- in-Council and as such, the Board should consider Hydro's direct interest before giving any weight to Hydro's submissions.[242] Newfoundland Power further submitted that

[235] Consumer Advocate Submission, page 40, lines 30-38.
[236] Consumer Advocate Submission, page 53, line 28.
[237] Newfoundland Power Submission, page 66, lines 9-17.
[238] Newfoundland Power Submission, page 69, lines 8-13.
[239] Hydro Submission, page 8, lines 1-3.
[240] Hydro Submission, page 6, lines 7-15.
[241] Hydro Submission, page 7, lines 9-11 and lines 25-27.
[242] Newfoundland Power Submission, page 107, lines 11-15.

consideration of the interests of third parties such as the impact on Hydro of an increased return for Newfoundland Power is not consistent with the fair return standard or the stand-alone principle.[243]

5.4.8. Board Decision Rate of Return on Equity

The determination of a fair return for Newfoundland Power for the 2025 and 2026 Test Years was a significant issue in this proceeding. Newfoundland Power proposed that the currently approved rate of return on equity of 8.5% be increased to 9.85%. The Consumer Advocate recommended that the return be reduced to 8.15%.

The Board is required to make a determination as to a fair return for Newfoundland Power. In making this assessment the Board must exercise its discretion to determine the return which is commensurate with returns on investments of similar risk, assures Newfoundland Power's financial integrity and allows Newfoundland Power to attract the necessary capital. Setting a fair return is an exercise of judgement which involves the consideration of all of the evidence in the circumstances, including the recommendations of the experts, the results of various methodologies, credit metrics and financing requirements and the allowed returns of other investor-owned utilities.

While the experts did not agree as to the fair return for Newfoundland Power, they agreed that the market overall had improved since Newfoundland Power's last general rate application and, in Concentric's opinion, the risk of utilities relative to the overall market has increased. Both Concentric and Dr. Booth recommended returns higher than they recommended in Newfoundland Power's last general rate application. Dr. Booth increased the recommended rate of return on equity from 7.5% to 7.7% and Concentric increased it from 9.8% to 9.85%. In reaching their conclusions the experts exercised their judgement considering the result of various methodologies and other sources of related information. While CAPM and DCF analyses were used by both Concentric and Dr. Booth, they differed on a number of inputs and the purposes for which they were used. Concentric relied on the historical CAPM, the DCF method, and a Risk Premium analysis to support its recommendation. Dr. Booth relied primarily on CAPM, and used a DCF analysis and the opinions of third parties to inform his judgement on the reasonableness of his recommended rate of return on equity.

In terms of the CAPM analysis, the expert's results were very different but a number of the elements used in the analysis were similar. Both experts recommended flotation costs of 0.50% and the risk-free rates were similar. Their market risk premium ranged from 5.5% to 6.39%. While Dr. Booths market risk premium was on the lower end of the range, he added a credit risk adjustment of 0.23%. The Board notes that both experts reflect higher values for many of the

[243] Newfoundland Power Submission, page 113, lines 9-14.

factors in the CAPM analysis in this proceeding than in Newfoundland Power's last general rate application.[244]

The most significant difference in the CAPM analysis of the two experts relates to the beta which measures the risk of the utility relative to the overall market. Concentric used a beta which was much higher than used by Dr. Booth. Dr. Booth's beta was .50 to .60, whereas Concentric's beta was .86. Concentric used an adjusted beta while Dr. Booth did not. Concentric was of the view that Dr. Booth's beta fails to appropriately take into account the increased level of risk of utilities relative to the market that has occurred.[245] Concentric noted that unadjusted betas currently are higher than used by Dr. Booth.[246] Whether betas should be adjusted tends to be controversial for Canadian utility regulators. Recently the BCUC has accepted the use of adjusted betas.[247] While the AUC found that both raw and unadjusted betas provide useful information with respect to utility risk.[248] The Board agrees that both raw and adjusted betas provide useful information that should be considered in the overall determination of a fair return.

In 2016 the Board found that beta of .6 was reasonable in determining Newfoundland Power's costs of capital.[249] The Board accepts that the risk of a utility relative to the overall market has increased since that time. Dr. Booth used a higher beta than he used in Newfoundland Power's last general rate application.[250] While Concentric agreed that the risk of a utility relative to the overall market has increased, it did not increase the beta used in this proceeding.[251] The Board notes that there is a large range in the betas recently accepted by other regulators. The AUC has recently accepted a beta in the range of .45 to.75 while the BCUC has accepted a beta in the range of .80 to .89.[252] The Board believes that a beta in the range of .5 to .6 as suggested by Dr. Booth may not be sufficient to reflect the risk of the utility relative to the overall market. At the same time the Board believes that Concentric's beta of .86 is too high. Considering all of the evidence the Board believes that a beta of .70 appropriately reflects the risk of a utility relative to the market at this time. The Board notes if a beta of .7 is used in a CAPM analysis assuming other factors which are supported by the evidence, including a risk-free rate of 3.8%, a market risk premium of 6.0% and flotation costs of .50%, the result would be a rate of return on equity of 8.5%.[253]

[244] Dr. Booth's CAPM analysis reflects higher values for the market risk premium, beta and credit risk adjustment and Concentric's analysis reflects a higher risk-free rate.
[245] Concentric Rebuttal, page 4, lines 10-16.
[246] Concentric Rebuttal, page 29, Figure 5.
[247] BCUC Decision and Order G-236-23, dated September 5, 2023, page 75.
[248] AUC Decision, 27084-D02-2023, pages 28 to 29, paragraphs 128-132.
[249] Newfoundland Power's allowed return on equity was agreed in a settlement agreement which was accepted by the Board.
[250] Dr. Booth used a beta in the range of .45 to .55 in Newfoundland Power's last general rate application.
[251] Concentric's beta was .88 in Newfoundland Power's last general rate application.
[252] BCUC Decision and OrderG-236-23 dated September 5, 2023, pages 72 and 75.
[253] 3.8% + (6.0% x .7) + 0.5%.

While the Board has in the past given primary weighting to the CAPM results, it has also looked to the results of the DCF method in informing its judgment of a fair return.[254] The Board has in the past expressed concerns with the use of analysts' forecasts in the DCF analysis but has given some consideration to the Multi-Stage DCF results.[255] Concentic's DCF results in this proceeding were 9.42%, based on the Multi-Stage DCF analysis for its North American Proxy Group. While Dr. Booth does not rely on the DCF results, the results were used to inform his judgment on the fair return on equity. Dr. Booth's DCF results ranged from 8.1% to 8.75% for the Canadian market and 6.84% to 9.60% for the U.S. market.[256] The Board continues to believe that it is appropriate to give less weight to the DCF results but looks to the results in exercising its discretion as to a fair return. The Board believes that the DCF analysis may suggest results which are equal to or slightly higher than 8.5%.

The Board notes that Concentric also conducted a Risk Premium analysis; Dr. Booth did not. The Risk Premium method is less commonly relied on by regulators than the CAPM and DCF methods. The AUC recently rejected the use of this method but it was accepted by the BCUC.[257] The Board has in the past determined that it would not use the Risk Premium method as it is largely based on U.S. data which is unadjusted and analysts' growth forecasts.[258] The Board continues to have concerns with the Risk Premium method and, as a result, places little or no weight on Concentric's Risk Premium analysis. The Board notes that removing the Risk Premium results from Concentric's average of the North American Proxy Group would reduce Concentric's results from 9.85% to 9.64%.

In setting a fair return for Newfoundland Power the Board has a broad discretion. It is widely accepted that there are a range of returns which may be considered reasonable for a utility in a given set of circumstances. Concentric recommended a rate of return on equity for Newfoundland Power of 9.85%, while Dr. Booth recommended 7.70%, and the Consumer Advocate recommended 8.15%. Newfoundland Power's allowed rate of return on equity has been 8.5% for rate making purposes since 2016 and the Board accepts the evidence that the risk of utilities relative to the market has recently increased. Both Concentric and Dr. Booth recommended rates of return in this proceeding that are higher than in Newfoundland Power's last general rate application and the CAPM analysis of both experts reflects higher values for many of the factors in the model. While the CAPM results calculated by the Board using alternate values suggest a rate of return on equity in the order of 8.5%, the Board believes that the DCF analysis evidence may suggest a somewhat higher return.

In addition to the recommendations of the experts and the results of the various models used, the evidence as to the allowed returns of other utilities and Newfoundland Power's credit metrics is of assistance to the Board in exercising its judgement as to a fair return for

[254] Order No. P.U. 18(2016), pages 27 and 39.
[255] Order No. P.U. 18(2016), pages 27 and 39.
[256] Booth Report, page 53, lines 11-12 and 15-17.
[257] Decision 27084-d02-2023, dated October 9, 2023, page 36, paragraph 165 to page 37, paragraph 166; and, Decision and Order G-236-23, dated September 5, 2023, page 117.
[258] Order No. P.U. 13(2013), page 27.

Newfoundland Power. Newfoundland Power's current rate of return on equity of 8.5% is just above the Canadian electric average. Concentric's recommendation would place Newfoundland Power near the top of utility returns and Dr. Booth's recommendation would place Newfoundland Power at the bottom.

Based on the evidence, with a rate of return on equity of between 8.25% to 9.25% and a common equity ratio of 45% Newfoundland Power would achieve the credit metrics in the 2025 and 2026 Test Years required to maintain its current credit rating and to satisfy the earnings test interest coverage in its First Mortgage Trust Deed. Despite this the Board accepts that there are also qualitative factors that are considered by the credit rating agencies. For example concerns with respect to regulatory support given rate pressures and potential changes in Newfoundland Power's cost recovery could have implications for Newfoundland Power's credit metrics and may impact the views of the credit rating agencies.[259] Based on the evidence with respect to the credit metrics and the opinions of the credit rating agencies the Board is concerned that a rate of return on equity of 8.5% may not be sufficient for Newfoundland Power to achieve the credit metrics necessary to maintain its credit rating and to satisfy its First Mortgage bond requirements. The Board notes the evidence of Newfoundland Power's Vice-President of Finance and Chief Financial Officer that she would be concerned about a rate of return on equity below 8.5%.[260]

The Board is satisfied that a fair return for Newfoundland Power for the 2025 and 2026 Test Years should be slightly higher than the rate of return that was approved for 2022 and 2023 in its last general rate application. The Board believes that a rate of return on equity of 8.6% is reasonable for Newfoundland Power considering the recommendations of the experts, the results of the CAPM and DCF analysis, the allowed returns of other investor-owned utilities and Newfoundland Power's credit metrics. The Board finds that a rate of return on equity of 8.6% with a common equity component of 45% would be commensurate with returns on investments of similar risk and would be sufficient to assure financial integrity and attract necessary capital and is a fair return for Newfoundland Power for the 2025 and 2026 Test Years. The Board finds that, for the 2025 and 2026 Test Years, a rate of return on common equity of 8.6%, with a common equity component of 45%, will provide Newfoundland Power, with the opportunity to earn a just and reasonable return on rate base consistent with the fair return principle and the provision of service at the lowest possible cost in an environmentally responsible manner.

The Board finds that a rate of return on common equity of 8.6%, with a common equity component not to exceed 45% should be used in calculating the rate of return on rate base for the 2025 and 2026 Test Years.

[259] Newfoundland Power's Wholesale Rate Flow-Through Application, PUB-NP-006.
[260] Transcript, June 17, 2024, page 133, lines 7-15.

6. RATE BASE AND RATE OF RETURN ON RATE BASE

There were a number of issues raised relating to rate base and rate of return on rate base.

6.1. Forecast Average Rate Base and Rate of Return on Rate Base for 2025 and 2026

The Application when initially filed on December 12, 2023 proposed a forecast average rate base of $1,406,816,000 for 2025 and $1,451,200,000 for 2026. The proposed rate of return on rate base was 7.40% for 2025 and 7.21% for 2026.

Grant Thornton reviewed the calculation of the return on rate base and average rate base proposed in the December 2023 filing and concluded that the proposed average rate base accurately reflects Newfoundland Power's proposals with respect to regulatory deferral accounts and updated calculations related to rate base allowances.[261] Grant Thornton also stated that it did not note any discrepancies in the clerical accuracy of the proposed 2025 and 2026 return on average rate base calculation. Grant Thornton noted that the weighted average cost of capital ("WACC") and the rate of return on rate base did not agree and referenced Newfoundland Power's explanation that differences in invested capital and rate base can cause this.[262] The primary reason was explained to relate to the cash working capital allowance. Grant Thornton recommended that a review be undertaken of the methodology used to determine the cash working capital allowance in rate base to evaluate whether it requires a revision. Grant Thornton commented that recent significant differences may be resolved with the adoption of a new wholesale rate and recommended that a review of the cash working capital allowance be undertaken after the introduction of a new wholesale rate.[263]

Newfoundland Power submitted that the proposed 2025 and 2026 average rate base should be approved, subject to any adjustments arising from the Board's determinations with respect to the Application. Newfoundland Power explained that the differences between the calculation of average rate base and invested capital are related to construction work in progress, materials and supplies and cash working capital amounts. According to Newfoundland Power the differences increased in recent years, related to power purchased costs. Newfoundland Power stated "A new wholesale rate will significantly reduce the volatility in purchase power costs and likely reduce the differences in rate base and invested capital".[264] Newfoundland Power said it planned to review the calculation of cash working capital in rate base following the implementation of a new wholesale rate.

As already discussed in Section 2, following the filing of submissions in this proceeding Newfoundland Power filed an application to flow-through the impacts of the new wholesale rate approved for Hydro.[265] Newfoundland Power's Wholesale Rate Flow-Through Application

[261] Grant Thornton Report, dated April 24, 2024, pages 6 and 68.
[262] Grant Thornton Report, dated April 24, 2024, page 56.
[263] Grant Thornton Report, dated May 1, 2024, page 20, lines 26-42.
[264] Newfoundland Power Submission, page 59.
[265] Order No. P.U. 1(2025).

revised a number of the proposals in this Application to reflect the impacts of the new wholesale rate and also Order No. P.U. 16(2024) and Order No. P.U. 20(2024). The revised proposals include a forecast average rate base of $1,412,358,000 for 2025 and $1,461,358,000 for 2026 and a revised rate of return on rate base of 7.34% for 2025 and 7.17% for 2026. Newfoundland Power's Wholesale Rate Flow-Through Application was approved in Order No. P.U. 2(2025).

The Board notes that the calculation of Newfoundland Power's forecast average rate base and rate of return on rate base for 2025 and 2026 will be impacted by the determinations in this Decision and Order. As a result, Newfoundland Power will be required to file a revised forecast average rate base and rate of return on rate base for the 2025 and 2026 Test Years as a part of its compliance application in this proceeding.

In terms of the issue raised with respect to differences between average rate base and invested capital, the Board notes that this has been an issue for Newfoundland Power in past proceedings. When the issue arose in Newfoundland Power's 2003-2004 general rate application the Board determined that Newfoundland Power should move toward the adoption of the Asset Rate Base Method ("ARBM") for determining return on rate base.[266] Under the ARBM the return on rate base would normally be determined by applying WACC to the forecast average rate base. The Board notes that the use of ARBM to determine return on rate base is a simple transparent approach which is consistent with the legislative scheme and is used by Hydro. The Board acknowledges that where there are differences in average rate base and average invested capital, this may create differences in the rate of return on rate base. When the Board approved the transition to the ARBM for Newfoundland Power in 2008 the differences between average rate base and invested capital were addressed by Newfoundland Power and agreed by the parties in a settlement agreement.[267] More recently Newfoundland Power made adjustments for the 2022 and 2023 Test Years to align average invested capital and average rate base so that the proposed return on rate base was approximately equal to the return calculated by applying the WACC to average rate base.[268] While the differences in average rate base and invested capital most often did not result in significant impacts for Newfoundland Power's rate of return on rate base, the difference became more significant in 2024.[269]

Based on the evidence, the new wholesale rate recently approved for Newfoundland Power should significantly reduce the differences between average rate base and invested capital for the 2025 and 2026 Test Years. As a result, it is expected that Newfoundland Power's proposed rate of return on rate base may equal WACC in the compliance filing. If this is not the case, and the compliance application proposes a rate of return on rate base which is not equal to WACC, information should be provided to assist in the Board's evaluation of the proposed rate of return on rate base. This information should include an explanation of the differences between the proposed rate of return on rate base and WACC, a reconciliation of the differences between

[266] Order No. P.U. 19(2003).
[267] Order No. P.U. 32(2007).
[268] Grant Thornton Report, dated May 1, 2024, page 20.
[269] Order No. P.U. 20(2024).

average rate base and invested capital and options which may be available to address material differences for the 2025 and 2026 Test Years. This information should address why the proposed rate of return should be approved as opposed to the rate of return calculated using WACC.

In terms of the approach which is to be taken in the calculation of Newfoundland Power's rate of return on rate base in the future, the Board believes that this is an important issue that should be resolved prior to Newfoundland Power's next general rate application. The Board notes that Grant Thornton recommended that a review be undertaken of the methodology used to include the cash working capital allowance in rate base after the introduction of a new wholesale rate. Further, Newfoundland Power stated that it planned to review the calculation of cash working capital in rate base following the implementation of the new wholesale rate. As a result, the Board believes that Newfoundland Power should file a report in relation to its use of the ARBM and differences in the calculation of the rate of return on rate base that result from differences in average rate base and invested capital, including the cash working capital allowance as well as other allowances, and potential changes which may be considered to address this matter, including deferral account changes.

The Board finds that Newfoundland Power should revise its calculation of its forecast average rate base and rate of return on rate base for the 2025 and 2026 Test Years to reflect the recommendations of the settlement agreements, the determinations of the Board in this Decision and Order and in Order No. P.U. 16(2024), Order No. P.U. 20(2024) and Order No. P.U. 2(2025), including a rate of return on common equity of 8.6% and a common equity component not to exceed 45%.

The Board finds that if the proposed rate of return on rate base for the 2025 and 2026 Test Years does not equal the Weighted Average Cost of Capital, Newfoundland Power should file additional evidence in relation to the calculation of the proposed rate of return on rate base as part of its compliance application.

The Board also finds that Newfoundland Power should file a report by February 15, 2026 with respect to the calculation of the rate of return on rate base and the Asset Rate Base Method addressing differences in average rate base and invested capital, including the cash working capital allowance as well as other allowances, and potential changes which may be considered.

6.2. Range of Rate of Return on Rate Base for 2025 and 2026

The Consumer Advocate submitted that the range for Newfoundland Power's rate of return on rate base should be reduced to +/-6 basis points, given the long history of Newfoundland Power earning more than its authorized return. The Consumer Advocate also submitted that any contributions to the Excess Earnings Account should be capped at the point where further contributions would cause Newfoundland Power's return on equity to be less than the allowed

return.[270] Dr. Booth recommended that any excess earned above the return on equity should be shared 50/50 with rate payers but he did not complete an analysis relating to the practice in other jurisdictions to support this recommendation.[271]

Newfoundland Power submitted that its range is within the scope of ranges approved for electric utilities in Canada and it encourages efficiency.[272] Newfoundland Power referred to Concentric's evidence that it would typically recommend a range somewhat larger to make sure it is strong enough to be effective as an incentive for the utility to find efficiencies.[273] Newfoundland Power submitted that there is no evidence on the record to indicate that the current range of return on rate base is unreasonable. Newfoundland Power noted that while Dr. Booth had recommended 50/50 earnings sharing mechanism, he had not completed any analysis to support the recommendation.

The Board notes that Newfoundland Power's current range in the rate of return on rate base has been in place since 1999.[274] Newfoundland Power's rate of return on rate base currently reflects a range of +/- 18 basis points.[275] Newfoundland Power is entitled to earn a rate of return within this range, and any return in excess of this range is transferred to its Excess Earnings Account. The disposition of excess earnings is determined by the Board which has normally found that it is to be applied to the benefit of customers. The Board finds that there is insufficient evidence to implement a 50/50 sharing of earnings as recommended by Dr. Booth. The Board is satisfied that the current range in the rate of return on rate base is reasonable and provides an incentive to Newfoundland Power to find efficiencies. At the same time, it ensures that earnings above the range must be placed in the Excess Earnings Account to be addressed by the Board. The Board is satisfied that the evidence in this proceeding supports the continuation of the current range in the rate of return on rate base.

The Board finds that the range for the rate of return on rate base of +/- 18 basis points should not be changed at this time.

6.3. Rate of Return on Rate Base for 2027

The Application proposed two test years, 2025 and 2026, and does not address Newfoundland Power's rate of return for 2027.

The parties did not file any submissions with respect to Newfoundland Power's rate of return on rate base for 2027.

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[270] Consumer Advocate Submission, page 59, lines 11-20.
[271] Transcript, June 20, 2024, page 143, line 12 to page 144, line 15; Dr. Booth Report, page 3, lines 7-9.
[272] Newfoundland Power Submission, page 85.
[273] Ibid., page 86.
[274] Order No. P.U. 36(1998-99).
[275] This results in an implied range of +/- 40 basis points on the return on equity.

The Board notes that it is regulatory practice for Newfoundland Power to file a general rate application every three years. In recent general rate applications Newfoundland Power has proposed two test years and has been directed to file a subsequent application to address its rate of return on rate base for the third year.[276] This direction required Newfoundland Power to file an application for approval of a revised forecast average rate base and rate of return on rate base for the non-test year(s) following the test year(s). Previously Newfoundland Power's rate of return on rate base for non-test years was established using an automatic adjustment formula which adjusted its return on equity but maintained other test year variables.

In relation to whether it is necessary to issue a direction for 2027, Concentric stated "a three-year period of reliance on a ROE in today's markets is reasonable. So my view is that it should not be necessary to revisit that until year four."[277] Dr. Booth testified:

> My position is simply that if you're on a three-year GRA, two years are determined and you got that third year. What do you do with the third year? Now, I know- do you just extend it? In which case, why not say it's a three-year ROE. Or if you have an automatic formula, my recommendation would be to keep it the same unless the forecast long Canada rate goes above 3.8 percent.[278]

Based on the evidence of the experts the Board accepts that it is reasonable to maintain the rate of return on equity of 8.6% for 2027. The Board is satisfied that based on the evidence in this proceeding it is not necessary to direct Newfoundland Power to file an application for a new rate of return for 2027. The Board will require Newfoundland Power to file information with respect to changes in its forecast cost of debt and forecast average rate base for 2027. This update should provide a calculation of the proforma rate of return on rate base for 2027 using WACC updated to reflect the 2027 forecast cost of debt and the approved rate of return on equity of 8.6%, applied to the forecast 2027 average rate base. The Board will review this information in considering whether changes are required to allow Newfoundland Power the opportunity to earn a fair return for 2027.

The Board finds that Newfoundland Power should file information relating to its forecast cost of debt, forecast average rate base and proforma rate of return on rate base for 2027, on or before September 15, 2026.

7. COST OF SERVICE AND RATE DESIGN

There were a number of issues raised during the hearing relating to cost of service and rate design, including:

- Ongoing Load Research and Rate Design Studies
- Cost Recovery for Customers at Transmission Voltage
- Proposed Rate Design Changes

[276] See for example Order No. P.U. 3(2022), page 20.
[277] Transcript, June 19, 2024, page 125.
[278] Transcript, June 21, 2024, page 74.

- Street and Area Lighting
- Advanced Metering Infrastructure

7.1. Ongoing Load Research and Rate Design Studies

The Consumer Advocate submitted that it is not clear that Newfoundland Power is giving the ongoing Load Research Study and the Rate Design Review the priority they deserve and recommended that the Board direct Newfoundland Power to give these studies high priority.[279]

Newfoundland Power submitted that the Consumer Advocate's recommendation is consistent with its ongoing efforts.[280] Newfoundland Power agreed to conduct a Load Research Study and a Rate Design Review as a part of the settlement agreement in its last general rate application. Newfoundland Power commenced the Load Research Study in 2023 and explained that the study was delayed due to delays procuring the necessary meters due to supply chain issues. Once the meters are in place, Newfoundland Power stated that customer load data will be collected for the 2024-2025 and 2025-2026 winter seasons. The Rate Design Review is also ongoing with a consultant retained and a Phase One Report circulated to the parties in April 2024. Phase Two is scheduled to be completed in 2025 and is dependent on the finalization of updated supply costs associated with the Muskrat Falls Project and the updated customer load research.[281]

The Board believes that both the Load Research Study and the Rate Design Review are critical studies that need to be completed in a timely manner to provide the necessary information to ensure effective and efficient rate structures for the Island Interconnected system. Newfoundland Power currently reports annually with respect to these studies as part of its annual returns filed on April 1 each year. Given the criticality of these studies and the fact that they remain ongoing since the last general rate application, the Board believes that Newfoundland Power should report more frequently in relation to the status of these studies, at least every six months.

The Board finds Newfoundland Power should provide updates every six months on the status of its Load Research Study and Rate Design Review, on or before April 1, as part of its annual return and also on September 30 each year.

7.2. Cost Recovery for Customers at Transmission Voltage

During this proceeding issues were raised with respect to the treatment of customers that are connected to the transmission system including a new rate class and transmission asset contribution policy.

[279] Consumer Advocate Submission, page 73, line 29 to page 74, line 6.
[280] Newfoundland Power Submission, page 97, lines 5-6.
[281] PUB-NP-169.

7.2.1. New Rate Class

The Consumer Advocate recommended that the Board direct Newfoundland Power to work with him to establish a new General Service customer rate class for customers served from the transmission system, to adjust the cost of service for General Service Rate 2.4 customers to reflect the proposed new General Service 2.5 customer group and to make the necessary amendments to the Rules and policies.[282] The Consumer Advocate refers to two mines and Memorial University ("MUN") as customers that are served from the transmission system that would be in the new general service rate class. The Consumer Advocate also submitted that the Board should direct Newfoundland Power to undertake a study to determine whether MUN is a public utility.

Newfoundland Power, in its submission, referred to the Load Research Study and Rate Design Review that is currently underway and submitted that the results of these studies will establish whether the addition of any new customer rate classes is appropriate and making changes at this time would be premature.[283] Newfoundland Power submitted that the issue of whether MUN is a public utility is outside the scope of this proceeding and is not to be determined by Newfoundland Power.

The Board has previously provided comments with respect to the rate design for MUN and stated:

> A review of the rates charged to MUN may be appropriate when more information is known about the anticipated changes in its load profile and when the ongoing rate design review by Newfoundland Power is complete.[284]

The Board expects that the Rate Design Review currently underway will include an evaluation of the reasonableness of the existing rate structure and cost recovery for MUN and other customers primarily served by transmission assets. The Board continues to believe that the issues raised with respect to MUN should not be addressed until completion of the Rate Design Review.

The Board finds that a new General Service customer rate class should not be established at this time.

7.2.2. Transmission Asset Contribution Policy

The Consumer Advocate submitted that the Contribution in Aid of Construction ("CIAC') Policy needs to be revised with respect to transmission asset investments for new connections and upgrades to ensure that the new customer pays all costs where the connection benefits only that customer. The Consumer Advocate's expert, Mr. Douglas Bowman did not have a concern

[282] Consumer Advocate Submission, page 78, lines 9-26.
[283] Newfoundland Power Submission, page 97, line 15 to page 98, line 3.
[284] Order No. P.U. 2(2024), (Reasons for Decision), page 13, lines 13-15.

with the CIAC Policy applying to distribution extensions and upgrades but did not agree with applying the policy to transmission assets. Mr. Bowman recommended an approach consistent with how Hydro treats Industrial customers when transmission assets are required to serve a single customer.[285]

Newfoundland Power stated that the existing CIAC policy and schedule of rates, rules and regulations currently ensure that the costs of assets that benefit only one customer, including connection assets, are recovered from the benefiting customer, either through rates or a separate contribution.[286] Newfoundland Power also stated the cost of service ensures that costs associated with specific transmission and substation assets associated with an individual customer, and that are recovered through rates charged to the customer, are specifically assigned to the customer's rate class.

The Board notes there are differences in the approach of Newfoundland Power and Hydro with respect to the requirement for contributions for transmission assets. For Hydro, the capital and operating cost of transmission assets dedicated to serving a single customer are recovered from the customer benefitting from the dedicated assets.[287] Newfoundland Power assesses the requirement for contributions as per the CIAC policy. Hydro also has a Labrador Network Additions Policy which sets out the approach followed when upgrades are required to common transmission assets.[288] The contribution policy for transmission assets should provide that transmission investments that primarily benefit a single customer are recovered from that customer. The Board believes it would be beneficial for Newfoundland Power to conduct a review of its approach to recovering the costs of transmission assets. This review should be completed as part of its ongoing Rate Design Review.

The Board finds that Newfoundland Power should address its general service contribution policy for transmission assets as part of its ongoing Rate Design Review.

7.3. Proposed Rate Design Changes

The Consumer Advocate recommended that the Board direct Newfoundland Power to work with him to alter the charges in (i) the existing rate structures and (ii) in the current optional rates to better reflect marginal costs in revised rates. He submitted that it is important to reflect trends in marginal costs in rates, that it is not necessary to undertake a comprehensive review when changes are only being made to the charges within the existing rate designs and that the only concern is that changes should not cause excessive rate impacts for customers.[289]

[285] Transcript, June 28, 2024, page 86, lines 3-13.
[286] Newfoundland Power Rebuttal Evidence, dated May 28, 2024, page 25, lines 15-18.
[287] CA-NLH-003.
[288] The Labrador Network Additions Policy was approved by the Board in Order No. P.U. 7(2021).
[289] Consumer Advocate Submission, page 79, lines 10-21 and page 80, lines 23-37.

Newfoundland Power submitted that revising customer rates in the manner recommended by the Consumer Advocate is not appropriate at this time.[290] Newfoundland Power stated that completing a comprehensive review of rates is necessary before customer rates are changed to ensure any new rate designs consider all factors and that there is input from customers.[291] Any new rate designs should reflect established regulatory principles, are acceptable to customers and have no unintended consequences. The ongoing Rate Design Review includes an analysis of customer rate alternatives, customer rate impacts, cost of service implications, and engagement with stakeholders.[292] Newfoundland Power stated its committed to working with the Consumer Advocate on these issues as part of the ongoing review.[293]

The Board accepts that changes in marginal costs are an important consideration when proposing revised customer rates. The Board acknowledges that it may in certain circumstances be reasonable to vary the percentage rate change in a general rate application even when the cost recovery ratios by rate class are within the targeted range. However, the Board believes that, given the material changes in system marginal costs as a result of interconnection with the North American grid, it is preferable to complete the ongoing Rate Design Review prior to making modifications to rate designs to better reflect marginal costs. This approach will ensure appropriate consideration of the issues and implications for customers associated with potential rate design changes and that all parties are fully informed of the potential customer impacts.

The Board finds that Newfoundland Power should not be directed to incorporate rate design changes at this time.

7.4. Street and Area Lighting

The Consumer Advocate recommended that the Street and Area Lighting class receive an above average increase in rates. The Consumer Advocate submitted that while it is acceptable to have revenue to cost ratios stemming from the cost of service study that are within a range of 90% to 110%, there is no reason why a customer class that has received a significant cost reduction should not pay 100% of the cost of supply.[294] The Consumer Advocate's expert, Mr. Douglas Bowman, questioned the appropriateness of the revenue-to-cost ratio for the Street and Area Lighting class. He stated in his evidence that "It is not clear why this customer class is not paying the full cost of supply given the significant savings the class is receiving as a result of the LED Street Light Replacement Plan".[295]

Newfoundland Power submitted that the Consumer Advocate's recommendation has limited scope as it does not address other classes, including the Domestic Customer class which also has

[290] Newfoundland Power Submission, page 98, lines 20-21.
[291] Newfoundland Power submission, page 99, lines 1-23.
[292] Newfoundland Power Rebuttal Evidence, dated May 28, 2024, page 20, lines 6-15.
[293] Newfoundland Power Rebuttal Evidence, dated May 28, 2024, page 21, lines 5-7.
[294] Consumer Advocate Submission, page 78, lines 30-41.
[295] Pre-Filed Evidence of C. Douglas Bowman, dated April 17, 2024, page 28, lines 15-17.

a revenue-to-cost ratio of less than 100% and further, it does not address the past practice which permits revenue-to cost ratios within a range of 90% to 110%.[296]

The Application proposed that approximately the same percentage rate increase be applied to each customer rate class. This approach reflects that the revenue-to-cost ratios used are within a range of 90% to 110%. This approach has been accepted by the Board as a means of achieving fairness in rate design without undue cross-subsidization among the various classes.[297] In this Application, the proposed revenue-to cost-ratios range from 96.5% for Domestic Customers to 107.9 % for General Service 0-100kW with Street and Area Lighting proposed at 97.2%.[298] The revenue-to-cost ratio for Street and Area Lighting decreased in the 2022 Cost of Service Study used as the basis for the rates proposed from the previous 2019 Cost of Service Study due to the proforma revenue reduction of $1.3 million related to the LED Replacement Plan which impacts the revenue-to-cost ratio by approximately 8%.[299] Newfoundland Power stated that its proposed approach to the Street and Area Lighting customer class is within accepted bounds and a revenue-to-cost ratio of 97.2% does not warrant applying a higher than average increase to that customer class.[300]

The Board accepts that the proposed rate increase for Street and Area Lighting class is within the normal range and is reasonable at this time. It is expected that the reasonableness of the Street and Area Lighting rate design and cost recovery will be addressed in the Rate Design Review currently underway.

The Board finds that Newfoundland Power should not be directed to make changes to the proposed rate increases for the Street and Area Lighting class at this time.

7.5. Advanced Metering Infrastructure

The Consumer Advocate recommended that the Board direct Newfoundland Power to complete a study by the end of 2024 on all the costs and benefits of Advanced Metering Infrastructure ("AMI"). He submitted that a comprehensive cost benefit study of AMI has not been done with previous reviews considering load shifting and demand response only and not all the potential benefits.[301] The Consumer Advocate's expert, Mr. Douglas Bowman, stated that Newfoundland Power's current metering system is "effectively obsolete" with AMI now the metering system of choice. He further stated that the penetration of smart meters in Canada will reach 94% over the next six years.[302] Mr. Bowman indicated that shifting load is only one of the benefits of the

[296] Newfoundland Power Submission, page 98, lines 10-14.
[297] Application, page 5-8, lines 1-4 and Order No. P.U. 7(1996-1997).
[298] Application, page 5-7, Table 5-5.
[299] CA-NP-261 c).
[300] Newfoundland Power Rebuttal Evidence, page 22, line 17 to page 23, lines 1- 5.
[301] Consumer Advocate Submission, page 81, lines 17-42.
[302] Pre-filed Evidence, C. Douglas Bowman, dated April 17, 2024, page 39, lines 7-19.

implementation of AMI.[303] Mr. Bowman recommended the Board order that a study on smart meters be done on the potential benefits because they're just too good to ignore.[304]

Newfoundland Power submitted that a direction to complete a separate cost benefit study of AMI at this time is not necessary and would disrupt the current efforts to determine the least-cost options to manage demand on the Island Interconnected system.[305] Newfoundland Power stated that its current metering system is not obsolete as major manufacturers continue to sell and support the existing technology and it is still used by numerous electric utilities, including Hydro and Manitoba Hydro. Mr. Chubbs, Vice President, Engineering and Energy Supply, indicated the existing Automatic Meter Reading ("AMR") system cost approximately $25 million and will provide savings of approximately $2.4 million per year over 18 years and while AMI would have provided some additional savings, AMI would require an approximate $100 million investment. Mr. Chubbs indicated AMR was implemented because it was least-cost for customers at the time and he still believes AMR continues to be least cost for customers.[306]

Newfoundland Power stated that while it recognizes that AMI can provide a range of benefits, the benefits vary by jurisdiction.[307] It noted that it had completed periodic analyses over the last decade to determine when AMI technology may become cost effective. It recently has engaged a third-party consultant to complete a market potential study that will study demand response, including dynamic rate design, with the results of this updated work to be used to produce a revised cost benefit analysis of AMI technology. The next step would be guided by the results of the revised analysis.[308] Mr. Chubbs indicated discarding AMR well before the end of its useful life and replacing it with AMI will further increase cost for customers as the customers would be required to fund the cost of the early discontinuance of AMR and the full cost of AMI implementation. He indicated it would be more cost-effective to implement AMI closer to the time that AMI would provide benefits to implement rate options such as dynamic rates or other initiatives for peak demand shifting. Mr. Chubbs also indicated delaying AMI installation until around 2030 would maximize the benefits for the existing AMR system over the estimated average AMR lifecycle and enable the future benefits of deferred generation additions through peak load shifting to help support justifying the cost of transition to AMI.[309]

Newfoundland Power indicated it is preparing to model the costs and benefits associated with implementation of AMI technology.[310] While the use of AMI has become more common at

[303] Transcript, June 28, page 46, lines 9-11.
[304] Transcript, June 28, page 47, lines 21-25.
[305] Newfoundland Power Submission, page 100, lines 1-17.
[306] Transcript, June 26, 2024, pages 120 to 121.
[307] In response to CA-NP-034(c), Newfoundland Power indicated the benefits of AMI technology can include: the ability to remotely read meters, automatic outage detection and management; the ability to remotely connect or disconnect service to customers; monitoring power quality; implementation of demand response programs such as Time-Of-Use ("TOU") rates; enablement of distributed energy generation; and the ability to provide customers personalized energy-saving tips and recommendations.
[308] Newfoundland Power Rebuttal Evidence, page 48, line 9 to page 49, line 13.
[309] Transcript, June 26, pages 128 to 131.
[310] CA-NP-034(f).

Canadian electric utilities, government funding has been provided in some jurisdictions to reduce customer rate impacts.[311] Newfoundland Power applied for AMI funding assistance to the federal government and the provincial government in 2021 and 2023, respectively. However, neither application was approved.[312]

While the Board believes smart metering through AMI implementation could provide additional benefits to customers beyond what is currently being provided by AMR, the evidence does not support a change at this time. Newfoundland Power has been reviewing AMI implementation and is advancing studies that will help quantify the potential benefits of AMI implementation. Newfoundland Power should continue this work and keep the Board and the parties advised of the progress on this matter.

The Board finds that Newfoundland Power should not be directed to provide a cost benefit analysis with respect to Advanced Metering Infrastructure implementation at this time.

The Board finds that Newfoundland Power should file an update on its review of the implementation of Advanced Metering Infrastructure as part of its 2026 Capital Budget Application.

8. BALANCING COST AND RELIABILITY

The Board is responsible for ensuring the delivery of power at the lowest possible cost, in an environmentally responsible manner, consistent with reliable service. The balance of cost and reliability is fundamental to the provision of least-cost power and was a central issue in this proceeding. This issue was part of the Board's considerations with respect to the proposed Operating Costs discussed in Section 4. It was also raised in the context of Newfoundland Power's reliability targets and distribution planning as discussed below.

8.1. Reliability Targets

The Consumer Advocate submitted that Newfoundland Power's reliability is now too high and that this imposes additional unnecessary costs for customers. According to the Consumer Advocate the growth in costs is largely driven by capital spending.[313] The Consumer Advocate submitted that Newfoundland Power has not demonstrated that providing service with reliability higher than the Canadian average is least-cost or that customers place a value on this increased level of reliability.[314] The Consumer Advocate submitted that the Board should direct Newfoundland Power to target a reliability level that is consistent with the Canadian average or that in the alternative, Newfoundland Power should be required to submit a report that its current level of reliability is consistent with the provision of least-cost service.

[311] CA-NP-034(d).
[312] CA-NP-250.
[313] Consumer Advocate Submission, page 69 and Transcript, June 13, 2024, pages 33 to 34.
[314] Over the period 2003 to 2023 Newfoundland Power's outage frequency was similar to the Canadian average while the duration of its outages was better than average.

Newfoundland Power submitted that in its view it is providing an appropriate level of reliability for customers and at least-cost. Newfoundland Power stated:

> Challenges such as aging infrastructure, more frequent weather events, uncertainties in supply reliability, and growing public reliance on electrification highlight the need to maintain system reliability levels comparable to those experienced by customers over the past decade. The Company submits that intentionally reducing system reliability is imprudent. Furthermore, reducing capital or operating budgets to achieve a specific reliability metric would undermine the Company's ability to maintain current reliability levels, increase pressure on customer rates, and conflict with the goal of providing least-cost, reliable service to customers.[315]

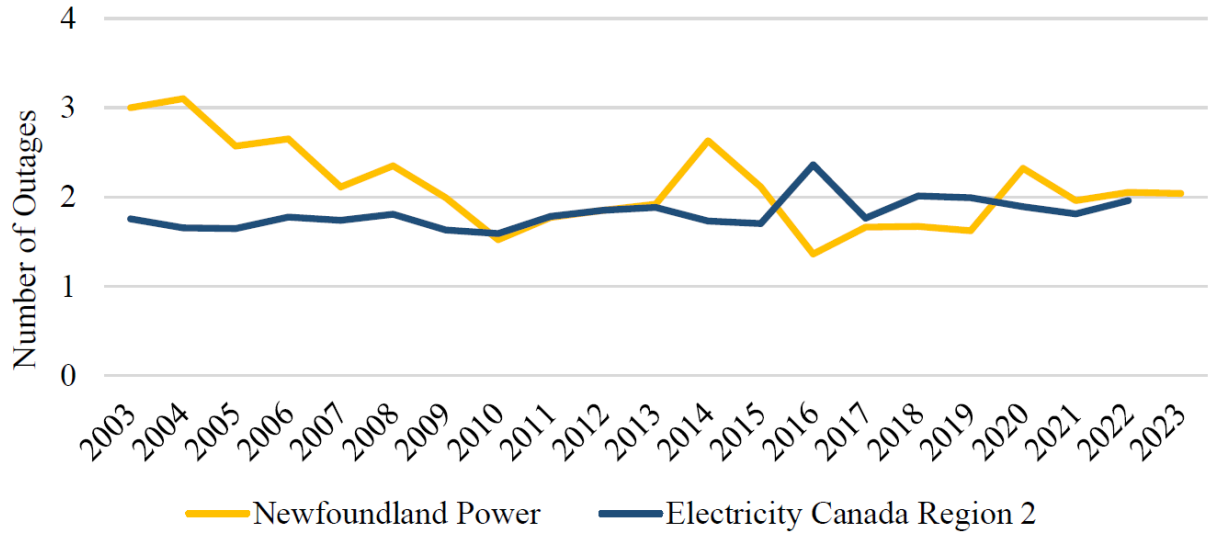
Newfoundland Power noted that its performance with respect to the number of outages is consistent with the Canadian average and the Consumer Advocate's submission implies that it should permit its response to customer outages to degrade from the current level. Newfoundland Power noted that the Consumer Advocate did not provide any evidence that would validate the recommendation that a lower target for reliability would reduce costs.[316] According to Newfoundland Power purposefully targeting lower reliability does not necessarily equate to lower costs.

Board Decision

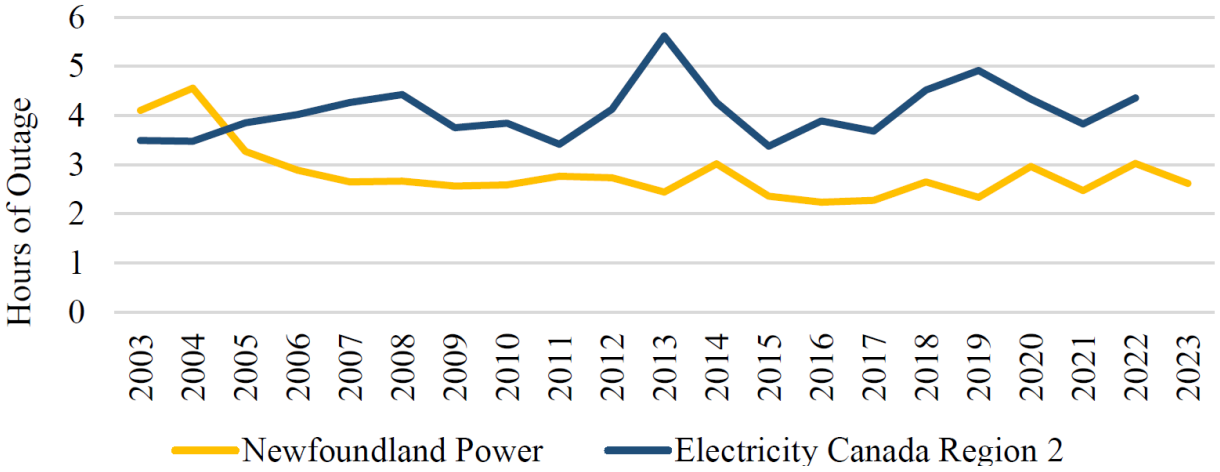
Newfoundland Power tracks its reliability performance in both outage frequency and outage duration. Newfoundland Power evaluates its reliability performance by tracking its own SAIDI[317] and SAIFI[318] data and by evaluating its performance in comparison to its peers.[319] Newfoundland Power has been consistent with other Canadian utilities for the last number of years with respect to the frequency of outages under normal operating conditions. While it was similar to other Canadian utilities in terms of outage frequency, Newfoundland Power has been better than average with respect to the duration of outages. Outage duration reflects both the condition of Newfoundland Power's system and its response when outages occur. As set out in the figures below Newfoundland Power's SAIFI was broadly consistent with the Canadian average over the 2003 to 2023 period and its SAIDI was approximately 40% better.[320]

[315] Newfoundland Power Submission, page 104, line 25 to page 105, line 5.
[316] Newfoundland Power Submission, page 105, lines 7-12.
[317] Outage duration is measured using the System Average Interruption Duration Index (SAIDI).
[318] Outage frequency is measured using the System Average Interruption Frequency Index (SAIFI).
[319] Region 2 Utilities are those serving a mix of urban and rural markets. Electricity Canada's Region 2 utilities which include Maritime Electric, New Brunswick Power, Nova Scotia Power, Hydro Quebec, Manitoba Hydro, BC Hydro, Sask Power, ATCO Electric, Fortis Alberta, Fortis BC, Hydro One, Newfoundland and Labrador Hydro, Newfoundland Power Inc., Newmarket-Tay Power Distribution, Elexicon Energy and Blue Mountain Power Corp.
[320] PUB-NP-041.

Newfoundland Power vs. Canadian Average
SAIFI Under Normal Operating Conditions
2003 to 2023



Newfoundland Power vs. Canadian Average
SAIDI Under Normal Operating Conditions
2003 to 2023



The Board notes that Newfoundland Power's target is to maintain its current level of reliability and while it does not target to outperform the Canadian average, its outage duration was significantly better than the Canadian average over the period 2003 to 2023. When asked whether this imposed additional costs for customers and whether there were areas of capital and operating spending that could be reduced while still ensuring SAIDI is comparable with the Canadian average, Newfoundland Power explained:

> Newfoundland Power is focused on maintaining current levels of reliability for its customers in a least cost manner. This requires routine capital expenditures to both maintain the condition of the electrical system and to support the Company's operational response. However, a reliable power system can also be more efficient to operate, with fewer unplanned events that would require a costlier response, and can result in lower overall cost to customers compared to an unreliable system. The Company's capital planning process is a deliberate effort to balance the cost and reliability of service provided to customers. As such, there are no incremental costs to customers to continue receiving current levels of reliability.[321]

According to Mr. Chubbs, Vice-President, Engineering and Energy Supply:

> I think the key message there is that in Newfoundland Power's view, and from our operational experience, that a reliable system is an efficient system. And if you're managing your system in a manner that gets the maximum life out of your assets, and you're inspecting it a way that you are replacing assets prior to failure as best you can, we can't always do that, that that [sic] is the least cost way to maintaining your electricity grid that provides good reliability outcomes for customers and does so at the lowest possible cost.[322]

In balancing cost and reliability, the Board is mindful of the increasing reliance customers place on the provision of reliable power and the increasing demand caused by electrification initiatives and load growth as well as supply reliability concerns.[323] Other significant issues which must be considered include the impacts of climate change on reliability and maintaining and upgrading aging infrastructure. In light of these considerations, the Board believes that it would be inappropriate to direct a lower level of reliability performance for Newfoundland Power. The Board is aware of the importance of ensuring that Newfoundland Power appropriately prioritizes reliability to ensure that it is well positioned to address the needs and expectations of customers and the challenges associated with climate change and its aging infrastructure.

Currently, Newfoundland Power's target is to maintain its level of reliability. The Board is satisfied that this is reasonable in the circumstances. Newfoundland Power's outage frequency is consistent with Canadian averages and its outage duration is better. The Board accepts the evidence that strong reliability can result in lower overall costs to customers, with fewer unplanned events and less costly responses. The Board is satisfied that the evidence demonstrates that targeting a reduction in reliability would not reduce costs and may increase costs. The Board is also concerned that reducing reliability targets below current levels could impact Newfoundland Power's ability to maintain current reliability levels, particularly given the challenges associated with electrification and climate change.

The Board notes that in the 1990's Newfoundland Power's reliability performance was below the Canadian average. The Board retained a consultant to review Newfoundland Power's operations

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[321] PUB-NP-050.

[322] Transcript, June 26, 2024, page 195, line 18 to page 196, line 6.

[323] Supply reliability concerns are currently being reviewed as part of the proceeding relating to Hydro's Resource Adequacy Plan.

and reliability performance and Newfoundland Power was directed to improve its reliability performance. Newfoundland Power changed its approach to asset management and, as set out in the figures above, its reliability performance has been, on average, consistent with the Canadian average since that time.[324] Another review was undertaken in 2014 as a part of the Board's investigation into power supply issues on the Island Interconnected system. The Board's consultant concluded at that time that Newfoundland Power's asset management practices conformed with good utility practice and its maintenance practices were appropriate and its response effective.[325] The Board also notes that Newfoundland Power, with the assistance of external consultants, is currently undertaking a comprehensive review of its asset management practices which may result in changes to its maintenance practices. In addition, Newfoundland Power explained that its design and construction standards are based on national standards which are currently being reviewed by the Canadian Standards Association. This review will determine if the standards are sufficient to meet future demands from climate change impacts.[326] The Board notes that in the future it may be necessary to consider whether there are areas of Newfoundland Power's operations which may require a reassessment with respect to reliability levels to address evolving circumstances, particularly aging assets, electrification and climate change.

The Board is satisfied that it is not necessary for Newfoundland Power to submit a report at this time addressing whether its current level of reliability is consistent with the provision of least-cost service.[327] The Board notes that over the period 2013 to 2022 Newfoundland Power reduced its Operating Costs per customer by 10%, on an inflation adjusted basis, while maintaining reliability levels.[328] In addition, Newfoundland Power's capital investment in transmission and distribution assets increased less than other Atlantic utilities over the same period.[329] The Board notes that while Newfoundland Power's Operating Costs had been decreasing for a number of years, as discussed in Section 4, this trend has reversed. Since 2021 Newfoundland Power's Operating Costs per customer have been increasing at rates higher than inflation. The proposed Operating Costs increases for the 2025 and 2026 Test Years contribute to the proposed customer rate increases. Newfoundland Power has been directed in this proceeding to reduce its proposed Operating Costs by $2.0 million in 2025 and in 2026. The Board believes that these reductions can be implemented without jeopardizing Newfoundland Power's current levels of reliability and will reasonably balance cost and reliability for 2025 and 2026. Should Newfoundland Power be unsuccessful in managing cost increases, or if concerns arise with respect to reliability, these issues will be identified through the Board's ongoing supervision of Newfoundland Power and appropriate steps will be taken.

[324] Transcript, June 26, 2024, 197, line 5-page 198, line 11; Transcript, June 26, 2024, page 87, line 11 to page 88, line 11 and NLH-NP-050.
[325] Transcript, June 26, 2024, page 101, lines 9-13; PUB-NP-045, Attachment A, page 8.
[326] Transcript, June 26, 2024, page 89, line 3 to page 90, line 5.
[327] Consumer Advocate Submission, page 85, lines 1-4.
[328] PUB-NP-039, page 2, lines 10-14.
[329] Newfoundland Power's 2025 Capital Budget Application Capital Budget Overview, pages 12-13.

The Board finds that Newfoundland Power should not be directed to target a lower level of reliability at this time.

8.2. Distribution Planning

The Consumer Advocate recommended that the Board direct Newfoundland Power to develop a distribution planning guideline that gives full consideration to costs, quantification of project risks and service improvements, the environment and government net-zero emission efforts, the value customers place on service improvements, behind-the-meter alternatives and the potential for stranding of hard infrastructure alternatives. He also submitted Newfoundland Power should be directed to develop a 5-year expansion plan as a part of the distribution planning guide.[330]

The Consumer Advocate's Expert, Mr. Bowman, stated:

> The current planning and asset management practices look at programs in isolation rather than from an overall utility and customer service perspective. They do not quantify service improvements or risks, and fall short of environmental requirements specified in legislation or anticipated under government electrification and net-zero emissions efforts. Further, they fail to take into consideration customer willingness to pay for reliability and service improvements.[331]

According to Mr. Bowman:

> (i) a comprehensive distribution planning guideline on the other hand would include planning principles and criteria, strategic plans, a five-year distribution system plan, the procedure to be followed for the five-year plan, planning data, electronic maps, planning facilities, loss reduction, load forecasting and distribution system studies;[332] and
> (ii) the distribution planning guideline would be included as part of a distribution code that covered four areas: planning code; operating code; connection code; and retail metering.[333]

Newfoundland Power submitted that its current distribution planning process adequately addresses its distribution planning requirements. It stated:

> Newfoundland Power's distribution planning processes, documentation, and participation in industry organizations with peers ensures proper planning of the distribution system. The Board's annual review of the Company's capital budget ensures capital expenditures associated with planning the distribution system are appropriate. Development of a new distribution planning guideline and five-year distribution expansion, as recommended by

[330] Consumer Advocate Submission, page 83, lines 38-43 and page 82, lines 33-36.
[331] Pre-filed Evidence, C. Douglas Bowman, dated April 17, 2024, page 44, lines 25-30.
[332] Ibid., page 44, lines 1-13.
[333] Ibid., page 45, line 3 to page 46, line 12.

> the Consumer Advocate is not necessary to ensure Newfoundland Power's distribution system is planned and managed in a manner consistent with the EPCA. [334]

According to Newfoundland Power its current distribution planning processes adequately address all objectives that Mr. Bowman suggested be met in a distribution planning guideline. Newfoundland Power noted that its current Distribution Planning Guidelines outlines the technical criteria and principles for planning the distribution system, including net metering and the Service and Metering Guide outlines the policies, procedures and technical requirements for establishing service connection and metering to the system.[335]

Board Decision

As already discussed, a number of issues which have potentially significant implications for Newfoundland Power's system and its customers, were raised during the hearing, including the potential implications of electrification and climate change, cybersecurity, increasing rate pressures for customers, information technology strategy and costs, aging infrastructure, and the level of capital spending. The Board notes that the evidence does not demonstrate that Newfoundland Power has an overall strategic plan addressing the significant issues currently facing its system and the associated costs.

Mr. Chubbs, Vice-President, Engineering and Energy Supply listed a number of individual initiatives to address electrical growth on the system but did not outline a comprehensive plan to address this significant issue of the implications for the system of load growth due to electrification demands. The specific initiatives he listed included building the impact into the load forecast, reviewing whether lines are reaching capacity and if so, planning capital projects to add capacity and distribution upgrades. [336]

In terms of how Newfoundland Power is addressing the potential impacts of climate change for its system, Mr. Chubbs outlined certain actions Newfoundland Power has taken, such as designing its system to current national construction and design standards, preventative maintenance and corrective maintenance projects and programs, improvements to its preparedness for adverse weather events, and its response time to outages.[337] In response to a question as to whether Newfoundland Power had considered developing an overall strategy to comprehensively outline how it is dealing with the potential for adverse impacts from climate change, Mr. Chubbs responded:

> I think that's something that is worth considering, you know, how we present that to customers. I know we have a lot in place internally and we do communicate with our customers when we have severe weather and system events to help customers understand

[334] Newfoundland Power Submission, page 102, lines 4-10.
[335] Newfoundland Power Rebuttal Evidence, page 45, line 1 to page 46, line 5.
[336] Transcript, June 27, 2024, page 19, line 4-25, and page 23, line 14.
[337] Transcript, June 27, 2024, page 11, line 6 to page 16, line 16.

> what we're doing, but I can't say that we've put anything out there that kind of outlines the strategy and what we're doing… .[338]

The Board notes that the preventative maintenance projects and programs Mr. Chubbs referred to include the Distribution Refurbishment and Modernization Plan and the Transmission Line Rebuild Strategy which have been in place since 2007 and 2006, respectively. While Newfoundland Power is currently undertaking an asset management review, it is not clear that there it has a comprehensive approach to balancing cost and reliability. The Board believes that Newfoundland Power should develop an overall plan as to how it approaches the balance of cost and reliability, identifying issues and challenges that may have significant potential implications for its system and customers. Newfoundland Power should consider strategies and approaches to assess and manage these issues in a comprehensive, coordinated way and should communicate effectively with the Board in relation to these efforts. This would provide both transparency and clarity for the Board and customers with respect to Newfoundland Power's plans and policies. While the Board believes that a strategic plan is warranted, the Board is satisfied that it is not appropriate at this time to direct the development of a distribution planning guideline. The Board believes that the first step is for Newfoundland Power to develop an overall plan as to balancing cost and reliability and how it will address significant and emerging issues such as electrification, climate change, technology advancements, vegetation management and aging infrastructure, including potential strategies or approaches for managing them. The Board will require Newfoundland Power to propose a scope of work for the development of this plan and the timeframe, considering the ongoing asset management review, and report to the Board.

The Board finds that Newfoundland Power should file on or before October 15, 2025, a scope of work for the development of a strategic plan as to its approach to the balancing of cost and reliability, identifying issues and challenges that may have significant implications for its system and customers and potential strategies to address these issues in the short, medium and long term.

9. COSTS

The Board finds that Newfoundland Power shall pay the costs and expenses of the Board arising from this Application, including the expenses of the Consumer Advocate incurred by the Board, pursuant to sections 90(1) and 117(3) of the Act.

10. COMPLIANCE APPLICATION

Revisions to the proposals in the Application will be required to reflect the settlement agreements and the determinations of the Board in this Decision and Order and in Order No. P.U. 16(2024), Order No. P.U. 20(2024) and Order No. P.U. 2(2025). As a result, Newfoundland Power will be required to file a compliance application setting out revised proposals, including,

[338] Transcript, June 27, 2024, page 18, lines 13-21.

among other things, forecast revenue requirements for the 2025 and 2026 Test Years, a forecast average rate base and rate of return on rate base for 2025 and 2026, its schedule of rates, tolls and charges and its rules and regulations. This Application should also include a revised revenue shortfall for 2025, to be amortized over the period July 1, 2025 to December 31, 2027, resulting from the implementation of the revised Hydro wholesale rate on January 1, 2025, and the implementation on July 1, 2025 of new rates arising from this Decision and Order.

The Board notes that, in accordance with the established rates, rules and regulations, Newfoundland Power's rates are adjusted each year to reflect the annual Rate Stabilization Account ("RSA") adjustment and Municipal Tax Adjustment Factor ("MTA"). When the last RSA and MTA adjustments were made on August 1, 2024, the Board found that the proposed overall average customer rate increases should be reduced to approximately 7.0% from the proposed increase of 9.3%. The Board also found that the portion of Newfoundland Power's March 31, 2024 RSA balance not collected though rates was to be maintained in the RSA to be addressed as part of Newfoundland Power's March 31, 2025 RSA balance. The Board stated:

> When Newfoundland Power files an application for July 1, 2025 rates it should address issues related to rate shock, rate stability and the timely recovery of prudent costs in the context of the information available at the time regarding rate increases which are expected over the period 2025 to 2027.[339]

The Board believes that considering the anticipated timeline for the compliance application, the rate proposals in the compliance application should incorporate the annual Rate Stabilization Account adjustment and Municipal Tax Adjustment Factor for July 1, 2025. This will bring together the rate increases associated with this Application and the annual RSA and MTA adjustments and will allow consideration of issues related to rate shock, rate stability and the timely recovery of prudent costs, as directed by the Board. To the extent that the information as to these adjustments is not finalized at the time of the filing of the compliance application, Newfoundland Power should use forecast information. Differences between actual and forecast can be maintained in the RSA to be addressed as part of the Newfoundland Power's March 31, 2026 RSA balances.

The Board finds that Newfoundland Power should file a compliance application revising the Application proposals to reflect the settlement agreements, the Board's determinations in this Decision and Order and in Order No. P.U. 16(2024), Order No. P.U. 20(2024) and Order No. P.U. 2(2025), and the annual Rate Stabilization Account adjustment and Municipal Tax Adjustment Factor for July 1, 2025. The compliance application should include, among other things, a revised forecast revenue requirement for the 2025 and 2026 Test Years, the revised revenue shortfall for 2025, a revised forecast average rate base for the 2025 and 2026 Test Years, and a revised rate of return on rate base for the 2025 and 2026 Test Years as well as revised rate proposals reflecting the direction of the Board with respect to rate smoothing and

[339] Order No. P.U. 16(2024), page 6.

incorporating the annual Rate Stabilization Account adjustment and Municipal Tax Adjustment Factor for July 1, 2025.

11. NEXT GENERAL RATE APPLICATION

The timing of Newfoundland Power's next general rate application was not raised in this proceeding. As previously noted, it is accepted regulatory practice for Newfoundland Power to file a general rate application every three years. This provides for timely and efficient regulatory process. This Application was filed in late 2023 for 2025 and 2026 Test Years and 2027 was discussed in Section 6 of this Decision and Order. In keeping with regulatory practice Newfoundland Power should file its next general rate application no later than June 1, 2027.

The Board finds Newfoundland Power should file its next general rate application no later than June 1, 2027.

12. ORDER

IT IS THEREFORE ORDERED THAT:

Rate Base, Rate of Return on Rate Base and Range of Return

1. Newfoundland Power shall file an application for approval of a revised forecast average rate base and rate of return on rate base for the 2025 and 2026 Test Years, based on the proposals in the Application and incorporating the recommendations of the settlement agreements, the determinations of the Board in this Decision and Order and in Order No. P.U. 16(2024), Order No. P.U. 20(2024) and Order No. P.U. 2(2025), including:

- **i) a common equity component in the capital structure not to exceed 45% for rate setting purposes; and**
- **ii) a rate of return on common equity of 8.6% for rate setting purposes.**

2. Newfoundland Power shall file information relating to changes in its forecast cost of debt, forecast average rate base and a proforma rate of return on rate base for 2027, on or before September 15, 2026.

3. Newfoundland Power shall, unless otherwise directed by the Board, file its next general rate application, no later than June 1, 2027.

Revenue Requirement

4. Newfoundland Power shall calculate and file a revised forecast revenue requirement for the 2025 and 2026 Test Years, based on the proposals contained in the Application and incorporating the recommendations of the settlement agreements, the determinations of the Board in this Decision and Order and in Order No. P.U. 16(2024), Order No. P.U. 20(2024) and Order No. P.U. 2(2025), including:

- **i) a productivity allowance reduction of $2.0 million in the proposed 2025 Operating Costs and the proposed 2026 Operating Costs; and**
- **ii) the exclusion of the costs associated with short-term incentive payments to the executive and directors; and**
- **iii) reductions of $995,000 for the 2025 Test Year and $495,000 for the 2026 Test Year, related to Newfoundland Power's conversion to International Financial Reporting Standards.**

Depreciation

5. The proposed calculation of depreciation expense based on the 2019 Depreciation Study is approved.

Other Regulatory Matters

6. The amortization, over the period July 1, 2025 to December 31, 2027, of the revised forecast revenue shortfall for 2025 is approved.

7. The amortization of Board and Consumer Advocate hearing costs in an amount up to $1.0 million, over the period July 1, 2025 to December 31, 2027, with differences between actual and estimated hearing costs to be transferred to the Rate Stabilization Account, is approved.

8. The proposed deferral account definition changes are approved, including:

- **i) The amendment of the Demand Management Incentive Account to establish a threshold of +/- $500,000, effective January 1, 2025, as set out in Schedule A;**
- **ii) The amendment of the Pension Capitalization Cost Deferral Account, effective January 1, 2025, to cease charges to the account effective December 31, 2024, as set out in Schedule B;**
- **iii) The creation of the International Financial Reporting Standards Cost Deferral Account, to provide for the deferred recovery of actual costs incurred as a result of Newfoundland Power's conversion to International Financial Reporting Standards, as set out in Schedule C; and**
- **iv) The amendment to Clause II.9 of the Rate Stabilization Clause to allow for recovery of costs charged annually to the Electrification Cost Deferral Account for costs incurred commencing January 1, 2021, as set out in Schedule D.**

9. Newfoundland Power shall file:

- **i) an update on its review of the implementation of Advanced Metering Infrastructure as part of its 2026 Capital Budget Application;**
- **ii) updates on the status of its Load Research Study and the Rate Design Review, addressing, among other things, its transmission asset contribution policy, on or before April 1 and September 30 each year;**
- **iii) a report reviewing its supply cost recovery mechanisms, on or before December 31, 2025;**
- **iv) a report in relation to the Customer, Energy and Demand Forecast methodology, on or before December 31, 2025;**
- **v) a report in relation to the calculation of the rate of return on rate base and the Asset Rate Base Method, on or before February 15, 2026;**
- **vi) a report in relation to executive and director compensation with its next general rate application; and**
- **vii) a scope of work for the development of a strategic plan as to its approach to balancing cost and reliability, on or before October 15, 2025.**

Rates, Rules and Regulations

10. Newfoundland Power shall file an application for approval of revised rates, tolls and charges, effective for service provided on and after July 1, 2025, based on the proposals in the Application, incorporating the recommendations of the settlement agreements, the determinations of the Board in this Decision and Order and in Order No. P.U. 16(2024), Order No. P.U. 20(2024), Order No. P.U. 2(2025), and the July 1, 2025 Rate Stabilization Account adjustment and Municipal Tax Adjustment Factor.

11. Newfoundland Power shall file revised rules and regulations.

Costs

12. Newfoundland Power shall pay the costs and expenses of the Board arising from the Application, including the expenses of the Consumer Advocate incurred by the Board.

DATED at St. John's, Newfoundland and Labrador this 16th day of January 2025.

Kevin Fagan
Chair and Chief Executive Officer

Dwanda Newman, LL.B.
Vice-Chair

John O'Brien, FCPA, FCA, CISA
Commissioner

Jo-Anne Galarneau
Executive Director and Board Secretary

Newfoundland Power Inc.
Demand Management Incentive Account

This account shall be charged or credited with the amount by which the Demand Supply Cost Variance exceeds the Demand Management Incentive. The Demand Management Incentive equals ± $500,000 of test year wholesale demand charges.

The Demand Supply Cost Variance expressed in dollars shall be calculated as follows:

$$(A – B) \times C$$

Where:

A = actual demand supply cost in dollars per kWh determined by dividing the wholesale demand charges in the calendar year by the weather normalized kWh purchases for that year (as will be reported in Return 15 of Newfoundland Power's Annual Report to the Board).

B = test year demand supply cost in dollars per kWh determined by dividing the test year wholesale demand charges by the test year kWh purchases.

C = the weather normalized annual purchases in kWh.

The amount charged or credited to this account shall be adjusted for applicable income taxes calculated at the statutory income tax rate.

Disposition of Any Balance in this Account

Newfoundland Power shall file an Application with the Board no later than the 1st day of March each year for the disposition of any balance in this account.

Newfoundland Power Inc.
Pension Capitalization Cost Deferral Account

This account shall be charged with amounts equal to cost impacts resulting from the change in capitalizing pension costs from the indirect method via general expenses capitalized to the direct method via a labour loader, effective January 1, 2023 and ending December 31, 2024.

Charges to the account will be amortized over a 5-year period commencing January 1, 2023.

Transfers to, and from, the account will be tax-effected.

Newfoundland Power Inc.
International Financial Reporting Standards Cost Deferral Account

Effective January 1, 2025, this account shall be charged with the operating costs incurred to enable Newfoundland Power to report its financial statements in accordance with International Financial Reporting Standards ("IFRS").

Transfers to, and from, the proposed account will be tax-effected.

Amortization of the account balance will be subject to a future order of the Board.

Newfoundland Power Inc.
Rate Stabilization Clause

The Rate Stabilization Clause is amended to include Clause II.9 as follows:

9 On March 31st of each year, beginning in 2025, the Rate Stabilization Account shall be increased on a before tax basis, by the Electrification Cost Recovery Transfer.

The Electrification Cost Recovery Transfer, expressed in dollars, will be calculated to provide for the recovery of costs charged annually to the Electrification Cost Deferral Account over a 10-year period, commencing in the year following the year in which the Electrification Cost Deferral is charged to the Electrification Cost Deferral Account.

The Electrification Cost Deferral Account will identify the year in which each Electrification Cost Deferral was incurred.

The Electrification Cost Recovery Transfer for each year will be the sum of individual amounts representing 1/10th of each Electrification Cost Deferral, which individual amounts shall be included in the Electrification Cost Recovery Transfer for 10 years following the year in which the Electrification Cost Deferral was recorded.

Newfoundland & Labrador
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