Newfoundland and Labrador Hydro
Hydro Place. 500 Columbus Drive
P.O. Box 12400. St. John's. NL
Canada A1B 4K7
t. 709.737.1400 I f. 709.737.1800
nlhydro.com

October 22, 2024

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

Attention: Jo-Anne Galarneau
Executive Director and Board Secretary

Re: Newfoundland and Labrador Hydro – Implementation of the Rate Mitigation Plan Report

Please find enclosed Newfoundland and Labrador Hydro's Implementation of the Rate Mitigation Plan report as requested by the Board of Commissioners of Public Utilities on September 19, 2024.

Should you have any questions, please contact the undersigned.

Yours truly,

NEWFOUNDLAND AND LABRADOR HYDRO

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

Encl.

ecc:

Board of Commissioners of Public Utilities
Jacqui H. Glynn
Katie R. Philpott
Maureen Greene, KC
Board General

Island Industrial Customer Group
Paul L. Coxworthy, Stewart McKelvey
Denis J. Fleming, Cox & Palmer
Dean A. Porter, Poole Althouse

Labrador Interconnected Group
Senwung F. Luk, Olthuis Kleer Townshend LLP
Nicholas E. Kennedy, Olthuis Kleer Townshend LLP

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

Newfoundland Power Inc.
Dominic J. Foley
Lindsay S.A. Hollett
Regulatory Email

Implementation of the Rate Mitigation Plan

October 22, 2024

A report to the Board of Commissioners of Public Utilities

Contents

1.0 Introduction

On July 28, 2021, the Government of Canada together with the Government of Newfoundland and Labrador ("Government") announced an agreement in principle with respect to rate mitigation. The agreement in principle provided for $2 billion in federal financing, including a $1 billion investment in the Labrador-Island Link ("LIL") and a third federal loan guarantee of $1 billion in relation to the Muskrat Falls and Labrador Transmission Assets. On February 14, 2022, as part of the province's rate mitigation plan, Newfoundland and Labrador Hydro ("Hydro"), the Government, and the Government of Canada signed term sheets for a $1 billion federal loan guarantee, capital restructuring of Muskrat Falls Corporation and Labrador Transmission Corporation, and a $1 billion investment in the LIL by the Government of Canada in the form of a convertible debenture. These arrangements significantly contribute towards rate mitigation, keeping the cost of financing low and providing an additional source of funding through the Government of Canada convertible debenture.

Since the announcement of the federal financing outlined above, Hydro and the Government worked closely together on the remaining details with respect to rate mitigation, including the mechanics of implementation and the source of funding for the remaining requirements. In May 2024, the Government announced the finalization of its rate mitigation plan and issued two supporting Orders in Council.

In Order in Council OC2024-062, the Board of Directors of Hydro was directed to *"structure any application for utility rate increases such that retail rate increases to domestic rate class customers attributable to Newfoundland and Labrador Hydro shall be targeted at 2.25 per cent per year"* for each rate application filed with the Board of Commissioners of Public Utilities ("Board") relating to the period up to and including the year 2030.[1] Order in Council OC2024-062 further directs that any additional funding required for Hydro to mitigate the Muskrat Falls Project[2] costs for customers subject to Island Interconnected System rates, to achieve the targeted rate increase for the period up to and including 2030, be through Hydro's sources, to the extent possible, and for Hydro to retire the 2023 Supply Cost Variance Deferral Account ("SCVDA") balance of $271 million over the 2024–2026 period.

[1] OC2024-062 (*Hydro Corporation Act*, SNL 2007, c H-17), <https://www.exec-oic.gov.nl.ca/public/oic/details?order-id=21851>.
[2] The Muskrat Falls Project was referenced as the Lower Churchill Project ("LCP") in the Order in Council.

Order in Council OC2024-063, issued on the same date, directed the Board of Directors of Nalcor Energy that any additional funding required for Hydro to mitigate the Muskrat Falls Project[3] costs or to retire the 2023 SCVDA balance of $271 million be through Nalcor Energy's sources.[4]

Hydro's SCVDA was approved by the Board in Order No. P.U. 33(2021), with the definition for the account reflecting the Board's directions in Order No. P.U. 4(2022), issued in February 2022.[5] The purpose of the SCVDA was to address material changes in system costs associated with the integration of the Muskrat Falls Project assets into the provincial electricity system. The SCVDA allows Hydro to defer, among other supply cost and revenue variances, the variance between Muskrat Falls Project costs incurred and those reflected in customer rates. In addition, Hydro is permitted to include any rate mitigation funding received as per the SCVDA definition to offset supply cost variances. To September 30, 2024, $575.4 million of rate mitigation funding has been applied against the balance owed from customers in the SCVDA.

The first rate change implemented under the Government's rate mitigation plan became effective August 1, 2024, as part of Hydro's Application for July 1, 2024 Utility Rate Adjustments.[6] Hydro is currently preparing the necessary analysis and evidence to file its next general rate application ("GRA"), planned for the second half of 2025. Hydro's GRA will incorporate the Muskrat Falls Project costs and the Government's rate mitigation plan into its updated cost of service study.

On September 19, 2024, the Board requested additional information on the implementation of the Government's rate mitigation plan and directed Hydro to file a report by October 22, 2024. The following sections are presented in the same categories as the Board correspondence, with the inclusion of each question or request from the Board, followed by Hydro's response and applicable background information, where necessary.

[3] The Muskrat Falls Project was referenced as the LCP in the Order in Council.
[4] OC2024-063 (*Energy Corporation Act,* SNL 2007, c E-11.01 and *Corporations Act,* RSNL 1990, c C-36), <https://www.exec-oic.gov.nl.ca/public/oic/details?order-id=21852>.
[5] The SCVDA definition was last approved by the Board in Order No. P.U. 34(2023).
[6] Board Order No. P.U. 15(2024).

2.0 Board Inquiries

2.1 General

Are the capping of rate increases provided for in the rate mitigation plan attributable to all changes in Hydro's costs or limited to cost recovery associated with the MFP only?

The targeted maximum rate increase provided for in the rate mitigation plan limits the rate impact to customers resulting from the inclusion of Muskrat Falls Project costs in rates. The purpose of the Government's rate mitigation plan is to offset the costs of the Muskrat Falls Project through rate mitigation; however, Order in Council 2024-062 provides for a target rate increase for Domestic customers on the Island Interconnected System, attributable to Hydro's costs, to 2.25% per year and therefore, by design, effectively limits the rate increase regardless of changes in other costs on the Island Interconnected System.

The approach to capping annual rate increases to apply rate mitigation to Island Industrial customers, if applicable.

Order in Council OC2024-062 directs that rate increases be structured for other customers subject to Island Interconnected System rates in a manner that is compatible with the Domestic rate class increase of 2.25% per year.

In January 2024, the Project Cost Recovery Rider was applied to Island Industrial Customers based on the estimated balances owed by them, considering the contributions made by the Utility customer since July 1, 2022, and utilizing the application of an energy allocator. Similar to the approach taken in Hydro's January 1, 2024 Industrial Customer Rate Adjustment application, Hydro will propose an adjustment to the Industrial customer Project Cost Recovery Rider accordingly to allow for the collection of prior amounts owing. The objective of this methodology is to maintain fairness in amounts collected through the Project Cost Recovery Rider between both customer groups given the different rate rider implementation dates. Hydro is currently reviewing the forecast of amounts due from Industrial customers to propose changes in rates effective January 1, 2025.

Hydro will review the Industrial customer rate as part of its next GRA once the impact of the Muskrat Falls Project costs and rate mitigation are reflected in the updated cost of service study. Rate mitigation

funds will be proposed to be allocated in the test year cost of service study in the same manner as the Muskrat Falls Project costs. The rate mitigation required is the amount that, after the allocation among the customer classes, results in the target increase of 2.25% to Domestic customers attributable to Hydro's costs.

The projected rate mitigation funding requirements for each year from 2024 to 2030.

Table 1 outlines the forecasted rate mitigation funding requirements for each year from 2024 up to and including 2030. These forecasted rate mitigation requirements represent the amount required to achieve the targeted 2.25% increase on an annual basis. The forecast provided below is based on estimates and assumptions made at a point in time; therefore, actual results may differ.[7]

Table 1: Forecasted Rate Mitigation Required
2024–2030
($ Millions)

	2024	2025	2026	2027	2028	2029	2030
Rate Mitigation Required	483.5	569.6	541.3	502.4	496.5	489.2	446.0

The sources and timing of annual rate mitigation funding for the period July 1, 2024 to the end of 2030.

Hydro's forecasted rate mitigation funding comes from three sources, the Government of Canada convertible debenture, the LCP dividends, and internally generated funding as directed by Orders in Council OC2024-062 and OC2024-063.

The Government of Canada's convertible debenture allows for drawings of up to $150 million annually to a maximum funding balance of $1 billion. In August 2023, the first drawing on the convertible debenture occurred in the amount of $144.7 million, which was transferred to Hydro and applied against Hydro's SCVDA balance owed from customers. Funding received in 2024 and forecasted for future years is reflected in Table 2.

[7] Forecast balances align to Hydro's internal financial forecast which was used to estimate rate mitigation required at the time of the Government's announcement and release of the rate mitigation plan in May 2024.

Hydro is planning to utilize internally generated funding to retire the remaining balance in the SCVDA as of December 31 of each year in the first quarter of the following year, with the exception of the December 31, 2023 balance. Orders in Council OC2024-062 and OC2024-063 directed the retirement of the 2023 SCVDA balance of $271.3 million over the 2024–2026 period. This timing is reflected accordingly in Table 2, spread evenly over the three years.

Table 2 outlines the forecasted sources and timing of annual rate mitigation funding for the period of January 1, 2024[8] through to the end of 2030. These forecasts are based on estimates and assumptions made at a point in time and actual results and timing of payments may vary.[9]

Table 2: Forecasted Rate Mitigation Funding – Sources and Timing
January 1, 2024–December 31, 2030
($ Millions)

	2024	2025	2026	2027	2028	2029	2030
Beginning Balance, Rate Mitigation Required[10]	**271.3**	**514.5**	**420.6**	**320.9**	**267.0**	**249.0**	**276.7**
Current Period Rate Mitigation Required[11]	**483.5**	**569.6**	**541.3**	**502.4**	**496.5**	**489.2**	**446.0**
Rate Mitigation Funding:							
Government of Canada Convertible Debenture	(150.3)[12]	(150.0)	(150.0)	(150.0)	(150.0)	(105.3)	-
LCP Dividends[13]	-	(90.0)	(70.4)	(85.4)	(97.5)	(107.2)	(78.7)
Internally Generated Funding	(90.0)	(423.5)	(420.6)	(320.9)	(267.0)	(249.0)	(276.7)
Total Rate Mitigation Funding during the Period	**(240.3)**	**(663.5)**	**(641.0)**	**(556.3)**	**(514.5)**	**(461.5)**	**(355.4)**
Ending Balance, Rate Mitigation Required	**514.5**	**420.6**	**320.9**	**267.0**	**249.0**	**276.7**	**367.3**

Hydro notes that the Government's current rate mitigation plan matures in 2030; however, there is an ending balance as presented in Table 2. This balance is forecasted to be settled in the first quarter of 2031 through internally generated funding. In addition, the Government has committed publicly to rate

[8] Hydro acknowledges the request from the Board cited July 1, 2024; however, Hydro has used a beginning date of January 1, 2024, to ensure clarity of the requirements and timing of payments for 2024.
[9] Forecast balances align to Hydro's internal financial forecast which was used to estimate the rate mitigation required at the time of the Government's announcement and release of the rate mitigation plan in May 2024.
[10] Beginning Balance, Rate Mitigation Required for 2024 is equal to the December 31, 2023 SCVDA balance.
[11] Current Period Rate Mitigation Required is the amount required to cover costs not being recovered from customers through base rates or the Project Cost Recovery Riders and is equal to the balances reported in Table 1.
[12] The 2024 balance of the convertible debenture funding includes $0.3 million in accrued interest.
[13] This balance includes any excess cash generated from operations associated with the Lower Churchill entities which is forecasted to be provided to the parent company through a common dividend.

mitigation post-2030 and keeping customer rates affordable for the people of the province. Hydro will work with the Government in advance of 2030 on future rate mitigation requirements.

2.2 Cost of Service Study Issues

On November 15, 2018, Hydro filed an application for revisions to its cost of service methodology ("2018 Cost of Service Study Methodology Review") for use in the determination of test year customer class revenue requirements reflecting the inclusion of the Muskrat Falls Project costs upon full commissioning.

Board Order No. P.U. 37(2019) approved the recommendations in the settlement agreement on the cost of service issues agreed to by the parties. The approved recommendations regarding the Muskrat Falls Power Purchase Agreement ("PPA"), Transmission Funding Agreement ("TFA") and export revenues included:

1) Power purchase costs resulting from the Muskrat Falls PPA and the TFA shall be functionalized as generation;

2) Net export revenues shall be functionalized as generation, which is the same manner as the functionalization of the Muskrat Falls Project costs;

3) The classification between demand and energy for the power purchase costs resulting from the Muskrat Falls PPA and the TFA shall be based on the system load factor. For greater clarity, it was agreed that this is inclusive of the costs related to the Muskrat Falls Generation, the LIL and the Labrador Transmission Assets; and

4) Net export revenues shall be classified using the system load factor, which is the same manner as the classification of the Muskrat Falls Project costs.[14]

The 2018 Cost of Service Methodology Review addressed the sharing of net revenue from export sales but did not address the treatment of rate mitigation funds that may be provided from other sources.

[14] Board Order No. P.U. 37(2019), sch. A, pp. 2–4.

The treatment of rate mitigation in the GRA test year revenue requirement.

The total rate mitigation required to meet the target rate increase of 2.25% in the test year revenue requirement will be shown as a credit to the test year revenue requirement, thereby reducing the revenue to be collected in rates from customers on the Island Interconnected System.

Whether rate mitigation funding will be identified on customer bills.

Hydro currently has no plans to identify rate mitigation as a separate item on customer bills. Rate mitigation will reduce the costs recovered from customers on the Island Interconnected System and published rates will be calculated based on the reduced revenue requirement.

The allocation of rate mitigation funding within the test year cost of service study, if applicable.

The 2018 Cost of Service Methodology Review likened export sales[15] to a form of rate mitigation and proposed that the revenue be classified in the same manner as the classification of the charges from the TFA and the Muskrat Falls PPA. The proposal on the treatment of export sales was agreed to amongst the parties and approved in Board Order No. P.U. 37(2019).

While the 2018 Cost of Service Methodology Review did not address the treatment of rate mitigation funds from other sources, Hydro believes the same cost of service treatment should apply to other forms of rate mitigation given the purpose of the funding, to reduce the impact of the Muskrat Falls Project costs on rates, is consistent.

Whether the cost of service methodology needs to be updated to accommodate rate mitigation funding and, if so, the planned timing of any application.

Hydro is planning to propose this change to the cost of service methodology in its next GRA along with any other issues to be addressed for the test year cost of service. If the Board considers this issue more appropriately addressed in a separate application in advance of the GRA, given the materiality, Hydro will file an application in the first quarter of 2025 requesting approval for the allocation of rate mitigation in the test year cost of service.

[15] "2018 Cost of Service Methodology Review Report," Newfoundland and Labrador Hydro, November 15, 2018, sec. 2.4, p. 6.

2.3 Deferral Account Issues

Projected year-end balances in the Supply Cost Variance Deferral Account for the period 2024 to 2030.

Please refer to Table 2. "Ending Balance, Rate Mitigation Required" provides a forecast for the ending SCVDA balance for the period of 2024 up to and including 2030.

The timing of when the methodology will be proposed to allocate the balances in the Supply Cost Variance Deferral Account among customer classes.

Hydro's Supply Cost Accounting Application, filed with the Board on July 29, 2021, provided its timeline for proposing additional changes for the long-term approach for the SCVDA and disposition of any balance accumulated in the proposed (now existing) account. Hydro stated:

> In its next GRA, Hydro will provide additional evidence on a long-term approach to the SCVDA to provide an opportunity for recovery of supply cost variances from those reflected in customer rates (including Muskrat Falls Project costs); and
>
> Hydro plans to file a separate application to deal with the balance allocation and disposition in the proposed (now existing) SCVDA after the conclusion of its next GRA.[16]

Hydro is reviewing the requirements for a long-term approach to the SCVDA that will come into effect after the conclusion of the GRA and is expecting to be in a position to file an application on the matter in the first quarter of 2025. Filing an application in advance of the GRA will create efficiency by reducing the issues to be dealt within the GRA proceeding, in particular the allocation of the long-term SCVDA amongst customer classes. The long-term SCVDA will address the allocation to customer classes of supply cost variances from the test year values approved in the GRA. In addition to the allocation methodology for assigning variances to customers, the application will also address:

1) The interest rate accruing on balances in the account;

2) Rules for calculating and adjusting the marginal cost energy rate, if required; and

3) The extent of rules required for the disposition of balances, given the rate mitigation plan.

As planned, Hydro is proposing to deal with any issues related to the disposition and conclusion of the existing SCVDA in an application to be filed after the conclusion of the GRA. The existing SCVDA will be

[16] "Supply Cost Accounting Application," Newfoundland and Labrador Hydro, July 29, 2021, para. 27 and 28, p. 6.

used to record variances until a new test year is approved in the GRA, at which point adjustments will be made to transition to the approved long-term SCVDA.

The treatment of the Rural Rate Adjustment balance in the Supply Cost Variance Deferral Account and what options are available for timely balance disposition to Newfoundland Power.

The Rural Rate Adjustment ("RRA") transfers the following to Newfoundland Power Inc. ("Newfoundland Power"):

1) Changes in Hydro's Rural customer revenues resulting from changes in rural rates between test years; and

2) Changes in Hydro's Rural customer revenues on the Island Interconnected System as a result of changes in Rural customer load between test years.

The Rate Stabilization Plan ("RSP"), discontinued since the effective date of the existing SCVDA on November 1, 2021, historically recorded activity relating to the RRA. The RSP was designed to smooth rate impacts for Newfoundland Power and Island Industrial Customers for variations between actual results and test year cost of service estimates for:

- Hydraulic production;
- No. 6 fuel cost used at Hydro's Holyrood Thermal Generating Station;
- Customer load; and
- Rural rates.

The RSP contained established rules for the allocation of monthly variations in hydraulic production, fuel cost and the rural rate alteration and transferred the applicable amounts to the plan balances for Newfoundland Power or Island Industrial Customers. The plan balances also included rate rider activity and interest resulting in a total plan balance that would be collected or refunded to customers annually when rates were adjusted.

Balances in the RSP were incorporated into rates for Newfoundland Power annually on July 1 based on their March 31 balance in the RSP, including the RRA. The wholesale rate impact of the RSP balance for Newfoundland Power had a flow-through impact on their customers, including Domestic customers.

Subsequent to the effective date of the existing SCVDA on November 1, 2021, the RRA balance for Newfoundland Power has been accumulating in the SCVDA Section B: Utility Customer Balance. As noted previously, unlike the RSP, the existing SCVDA currently has no rules for the allocation of balances to customer classes, except for the RRA which is allocated between Newfoundland Power and regulated Labrador Interconnected System Customers.[17] In addition, there are currently no rules for the reflection of balances owed to customers, such as the RRA, in the annual rate adjustments. As previously noted, the balance of the existing SCVDA and the disposition or allocation to customers is proposed to be addressed in an application to be filed after the conclusion of the GRA.

The current balance in the SCVDA owing to Newfoundland Power associated with the RRA is approximately $20 million. Table 3 demonstrates the average end-customer rate impact of a decrease of 2.6%, which would occur if the RRA balance owing was allocated and refunded to Newfoundland Power in a future July 1 Utility Rate Adjustment, assuming all other items are kept constant.

Table 3: **Estimated Customer Rate Impact of Current RRA Balance**

	Billing Units[18]	Unit	Current Rates	Billings at Existing Rates ($)	Proposed July 1 Rates	Revised Billings ($)	Change ($)	Change Utility (%)	Estimated Change End Customer[19] (%)
Demand (kWs)	15,164,268	$/kW/mo	5.00	75,821,340	5.00	75,821,340			
Energy (MWhs)	3,960,000	¢/kWh	2.444	96,782,400	2.444	96,782,400			
Energy (MWhs)	1,840,700	¢/kWh	18.165	334,363,155	18.165	334,363,155			
Total Base Rate				**506,966,895**		**506,966,895**	-		
RSP: Current Plan Adjustment	5,800,700	¢/kWh	0.000	-	(0.345)	(20,000,000)	(20,000,000)	(3.9)	(2.6)
Project cost Recovery Rider	5,800,700	¢/kWh	0.000	-	0.000	-	-	0.0	0.0
Total				**506,966,895**		**486,966,895**	**(20,000,000)**	**(3.9)**	**(2.6)**

The Government's rate mitigation plan targets the domestic residential rate increases attributable to Hydro's costs at 2.25% annually up to and including 2030. Therefore, under this plan, any refund of balances in the SCVDA, such as the RRA, will result in a higher Project Cost Recovery Rider to achieve the target 2.25% rate increase, as demonstrated in Table 4.

[17] The portion allocated to Hydro Rural Labrador Interconnected System is removed from the plan and written off to Hydro's net income (loss).
[18] Billing units are based on 2019 Test Year.
[19] Assumes a 66.80% flow-through rate.

Table 4: Estimated Overall Customer Rate Impact

	Billing Units[20]	Unit	Current Rates	Billings at Existing Rates ($)	Proposed July 1 Rates	Revised Billings ($)	Change ($)	Change Utility (%)	Estimated Change End Customer[21] (%)
Demand (kWs)	15,164,268	$/kW/mo	5.00	75,821,340	5.00	75,821,340			
Energy (MWhs)	3,960,000	¢/kWh	2.444	96,782,400	2.444	96,782,400			
Energy (MWhs)	1,840,700	¢/kWh	18.165	334,363,155	18.165	334,363,155			
Total Base Rate				**506,966,895**		**506,966,895**	-		
RSP: Current Plan Adjustment	5,800,700	¢/kWh	0.000	-	(0.345)	(20,000,000)	(20,000,000)	(3.9)	(2.6)
Project cost Recovery Rider	5,800,700	¢/kWh	0.000	-	0.634	36,755,100	36,755,100	7.3	4.9
Total				**506,966,895**		**523,721,995**	**16,755,100**	**3.4**	**2.3**

Hydro is proposing to dispose of all balances in the SCVDA, including the RRA, after the GRA. If Hydro were to refund the RRA balance, the rate impact would continue to reflect a 2.25% increase in end customer rates, in accordance with the rate mitigation plan, as demonstrated in Table 4.

Whether any further additions or revisions the Supply Cost Variance Deferral Account are required to reflect the rate mitigation plan.

There are currently no further known additions or revisions required to the existing SCVDA to reflect the rate mitigation plan.

3.0 Conclusion

The Government's final rate mitigation plan was released in May 2024 and implemented into customer rates beginning on August 1, 2024. Hydro has existing regulatory mechanisms that support the rate mitigation plan such as the Project Cost Recovery Riders and the existing SCVDA. Rate mitigation funding received is captured through Hydro's existing SCVDA and passed on to customers by reducing the balance owed.

Hydro is in the process of preparing the analysis and evidence necessary to file its next GRA, which will incorporate Muskrat Falls Project costs and rate mitigation funding into its updated cost of service study. Hydro is also preparing to file, in advance of its next GRA, an application with the Board for a

[20] Billing units are based on 2019 Test Year.
[21] Assumes a 66.80% flow-through rate.

long-term SCVDA that will include proposed customer class allocation methodology and disposition. As outlined in Hydro's application for its existing SCVDA, Hydro is proposing to deal with any issues related to the disposition and conclusion of the existing SCVDA in an application to be filed after the conclusion of its next GRA.