

**NEWFOUNDLAND AND LABRADOR
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES**

AN ORDER OF THE BOARD

NO. P.U. 33(2021)

1 **IN THE MATTER OF** the *Electrical Power*
2 *Control Act, 1994*, SNL 1994, Chapter E-5.1
3 (the “*EPCA*”) and the *Public Utilities Act*,
4 RSNL 1990, Chapter P-47 (the “*Act*”), as
5 amended, and regulations thereunder; and
6

7 **IN THE MATTER OF** an application by
8 Newfoundland and Labrador Hydro for approval
9 of new deferral accounts, changes to existing deferral
10 accounts, and an accounting deviation, associated with
11 the commissioning of the Muskrat Falls Project,
12 pursuant to section 58 of the *Act*.
13
14

15 **Application**

16
17 On July 29, 2021 Newfoundland and Labrador Hydro (“Hydro”) filed an application with the
18 Board requesting approval of:

- 19 (i) a Supply Cost Variance Deferral Account to become effective on the date upon which
20 Hydro is required to begin payments under the Muskrat Falls Power Purchase Agreement
21 (“Muskrat Falls PPA”);
22 (ii) the discontinuance, on the date of the implementation of the proposed Supply Cost
23 Variance Deferral Account, of the following established deferral accounts:
24 (a) Rate Stabilization Plan (the “RSP”);
25 (b) Revised Energy Supply Cost Variance Deferral Account;
26 (c) Isolated Systems Supply Cost Variance Deferral Account; and
27 (d) Holyrood Conversion Rate Deferral Account;
28 (iii) a Holyrood Thermal Generating Station (“Holyrood TGS”) Accelerated Depreciation
29 Deferral Account to be effective January 1, 2022;
30 (iv) a deviation from International Financial Reporting Standards (“IFRS”) to allow Hydro
31 to recognize the power purchase costs relating to the delivery of post-commissioning
32 energy in accordance with the commercial terms of the Muskrat Falls PPA and the
33 Transmission Funding Agreement; and
34 (v) a Muskrat Falls PPA Sustaining Capital Deferral Account.
35

36 The Application was copied to Newfoundland Power Inc. (“Newfoundland Power”); the
37 Consumer Advocate, Dennis Browne, Q.C. (the “Consumer Advocate”); a group of Island

1 Industrial Customers: Corner Brook Pulp and Paper Limited, NARL Refining Limited Partnership
2 and Vale Newfoundland and Labrador Limited (the “Industrial Customer Group”); the
3 communities of Sheshatshiu, Happy Valley-Goose Bay, Wabush and Labrador City (the “Labrador
4 Interconnected Group”); Iron Ore Company of Canada; Praxair Canada Inc.; and Teck Resources
5 Limited.

6
7 Requests for information (“RFIs”) were issued by the Board, Newfoundland Power, the Industrial
8 Customer Group and the Labrador Interconnected Group.¹ On October 15, 2021 Newfoundland
9 Power, the Consumer Advocate and the Industrial Customer Group filed submissions. Hydro filed
10 a reply submission on October 22, 2021.

11 **Submissions**

12
13
14 Newfoundland Power supported Hydro’s supply cost deferral account proposals with the exception
15 of the proposed calculation of financing charges in the account. Newfoundland Power opposed the
16 use of Hydro’s approved test year Weighted Average Cost of Capital (“WACC”) and submitted
17 that Hydro should be permitted to recover its short-term debt costs until the long-term approach is
18 determined through Hydro’s next general rate application. Newfoundland Power also suggested
19 that Hydro should report quarterly on the Supply Cost Variance Deferral Account balances.
20 Newfoundland Power supported Hydro's proposed IFRS deviations and the proposed Holyrood
21 TGS Accelerated Depreciation Deferral Account but submitted that the account should also
22 include the variance related to the 2023 depreciation expense which is forecast to be materially
23 lower than 2022.

24
25 The Consumer Advocate submitted that he is not opposed to a deferral account being established
26 to accumulate Muskrat Falls Project costs until Hydro’s next general rate application when the
27 Board will determine the appropriateness of cost recovery and the distribution of the costs among
28 Hydro's customers. Nevertheless, the Consumer Advocate suggested that it might be prudent for
29 the Board to delay a decision on this Application until Hydro is in receipt of additional information
30 in relation to the numerous uncertainties stemming from the Muskrat Falls Project. The Consumer
31 Advocate noted that in a short period of time Hydro expects to know more about the Government's
32 rate mitigation plan, the Muskrat Falls Project commissioning date and final project costs.

33
34 The Industrial Customer Group stated that it does not object to the discontinuance of the RSP and
35 the other supply cost deferral accounts, the proposal to deviate from IFRS to recognize power
36 purchase costs in accordance with the commercial terms of the Muskrat Falls Project agreements,
37 or the proposed Muskrat Falls PPA Sustaining Capital Deferral Account. In relation to the
38 proposed Supply Cost Variance Deferral Account the Industrial Customer Group objected to the
39 use of WACC in the calculation of financing charges and submitted that that the account should
40 accrue interest at prevailing short-term borrowing costs. The Industrial Customer Group also
41 submitted that the account should reflect all revenues from greenhouse gas performance credits
42 for the years 2019, 2020 and 2021. With respect to the proposed Holyrood TGS Accelerated
43 Depreciation Deferral Account, the Industrial Customer Group submitted that the proposal is not
44 justified and should not be approved, considering the uncertainty with respect to the retirement

¹ A total of 113 RFIs were answered by Hydro.

1 date of Holyrood and the unbalanced risk profile that arises from Hydro deferring added costs to
2 ratepayers but not crediting ratepayers with cost savings.

3
4 In its reply Hydro submitted that its proposals will serve to enable the deferral of material supply
5 cost variances from those reflected in current rates until the conclusion of its next general rate
6 application and until rate mitigation is provided by Government and/or a cost recovery plan can
7 be established for future recovery from customers. Hydro noted that Newfoundland Power
8 provided support for the establishment of the Supply Cost Variance Deferral Account and the
9 Industrial Customer Group and the Consumer Advocate did not object. Hydro submitted that
10 delaying the implementation of the deferral account, as suggested by the Consumer Advocate,
11 would introduce additional risks for Hydro. Hydro agreed to provide quarterly updates on the
12 Supply Cost Variance Deferral Account balances in its quarterly regulatory reports. In relation to
13 the calculation of finance charges on the Supply Cost Variance Deferral Account Hydro proposed
14 that, given the blending of historical balances from Hydro's existing deferral accounts with the
15 payments under the Muskrat Falls Project agreements, the use of its 2019 Test Year Embedded
16 Cost of Debt would give Hydro a reasonable opportunity to recover the cost of financing the
17 deferral account balances. In relation to greenhouse gas performance credits Hydro cautioned
18 against retroactive ratemaking but stated that it does not oppose the inclusion of 2021 greenhouse
19 gas performance credit revenues. In relation to the proposed Holyrood TGS Depreciation Deferral
20 Account Hydro submitted that the additional capital investments since 2019 were necessary and
21 prudent and the uncertainty as to the decommissioning of the Holyrood Thermal Generating
22 Station as a generating facility is impacted by factors beyond Hydro's control. According to Hydro
23 the inclusion of the 2023 depreciation variance is unnecessary since 2023 will likely be a test year
24 but, if this changes, Hydro does not object to including it in the deferral account.

25 26 **Board Findings**

27 28 (i) Supply Cost Variance Deferral Account

29
30 The Application requests approval of an account to defer costs which will be incurred by Hydro
31 pursuant to the Muskrat Falls Project agreements. Upon the commissioning of the Muskrat Falls
32 generating facilities and the Labrador Transmission Assets Hydro is required to begin monthly
33 payments pursuant to the Muskrat Falls PPA. After commissioning of the Labrador-Island Link,
34 Hydro will be required to begin monthly payments related to the costs of these assets, pursuant to
35 the Transmission Funding Agreement. Given the anticipated timing of the commissioning of the
36 assets and the Government direction with respect to the recovery of costs from customers, Hydro
37 will be required to begin payments under the Muskrat Falls PPA, and perhaps the Transmission
38 Funding Agreement, before it can begin to recover the costs from customers.² These payments are
39 significant and are not currently reflected in rates and, as a result, could materially impact Hydro's
40 financial performance.³ Approval of the account would allow the deferral of these costs until rate

² Order in Council OC2013-343 requires Muskrat Falls Project commissioning before Hydro can recover project costs through customer rates. On November 4, 2021 Hydro advised that it expects that the Labrador-Island Link will be commissioned in late March 2022. On November 29, 2021 Hydro advised it formally accepted the final of the four units at the Muskrat Falls Generating Facility into commercial operation on November 25, 2021 and was required to make payments under the Muskrat Falls PPA.

³ Application, Schedule 1, page 15 sets out that the projected monthly payments for 2021 are approximately \$33 million under the Muskrat Falls PPA and approximately \$34 million under the Transmission Funding Agreement.

1 mitigation is provided by Government and/or a cost recovery plan can be established for future
2 recovery from customers. The parties did not oppose the proposed deferral account. The Board is
3 satisfied that it is reasonable and necessary at this time to approve the deferral of the costs incurred
4 by Hydro pursuant to the Muskrat Falls Project agreements.

5
6 While the Board accepts that Hydro should be permitted to defer the payments required by the
7 Muskrat Falls Project agreements, the proposed account includes a number of other components.
8 Most of the proposed components are related to the Muskrat Falls Project agreements or the
9 changes on the Island Interconnected system upon the commissioning of the Muskrat Falls Project.
10 These include the contractually required payments as well as rate mitigation funding and cost
11 recovery through customer rates. The account also includes variances related to Holyrood Thermal
12 Generating Station fuel costs, other Island Interconnected system supply costs, net revenues from
13 exports, transmission tariff revenues, load, and greenhouse gas credit revenues. The Board is
14 satisfied that these components should be reflected in the Supply Cost Variance Deferral Account
15 as they are associated with the changes in supply on the Island Interconnected system upon
16 commissioning of the Muskrat Falls Project.

17
18 In addition the Application proposes that the Rural Rate Alteration be included as a component in
19 the new Supply Cost Variance Deferral Account and that it be expanded to also include changes
20 in revenues for Hydro Rural Island Interconnected system customers resulting from sales variances
21 from the test year load forecast.⁴ The parties did not object to the Rural Rate Alteration proposals.
22 The Board accepts that the Rural Rate Alteration should be a component of the new account and
23 that it should be expanded to reflect load variances on the basis that the fixed payment structure of
24 the Muskrat Falls Project agreements creates the potential for material earnings volatility if sales
25 to Hydro's Rural Island Interconnected system customers vary from the test year forecast.

26
27 The Application also proposes the RSP, the Revised Energy Supply Cost Variance Deferral
28 Account, the Holyrood Conversion Rate Deferral Account and the Isolated Systems Supply Cost
29 Variance Deferral Account be discontinued upon the implementation of the Supply Cost Variance
30 Deferral Account. There are a number of issues which arise in relation to the specific proposals
31 associated with the discontinuance of these accounts, including:

- 32 • Upon the discontinuance of the Revised Energy Supply Cost Variance Deferral Account
33 and the Holyrood Conversion Rate Deferral Account the balances would be transferred to
34 the Other Island Interconnected System Supply Cost Variance component of the new
35 account.⁵
- 36 • Upon the discontinuance of the Isolated Systems Supply Cost Variance Deferral Account
37 the balance in the account would be transferred to the Isolated System Supply Cost
38 Variance component of the new account.⁶

⁴ The Rural Rate Alteration reflects the Rural Rate Adjustment to transfer variations in revenue resulting in changes in Hydro's Rural Rates between test years to Newfoundland Power's Rate Stabilization Current Plan.

⁵ NP-NLH-007, Attachment 1 sets out the forecast balance at October 1, 2021 is approximately \$19 million in the Revised Energy Supply Cost Variance Deferral Account and \$1.4 million in the Holyrood Conversion Rate Deferral Account.

⁶ NP-NLH-007, Attachment 1 sets out the forecast balance at October 1, 2021 is approximately (\$1.1) million in the Isolated Systems Supply Cost Variance Deferral Account.

- 1 • Upon the discontinuance of the RSP:
- 2 ○ The RSP Current Plan balances for Newfoundland Power and Industrial customers
- 3 would be transferred to the RSP Conclusion component of the new account which
- 4 would reflect monthly RSP activity, including transfers and financing charges, until the
- 5 conclusion of the RSP.⁷
- 6 ○ The balance in the Hydraulic Production Variation component of the RSP would be
- 7 transferred to the Holyrood Thermal Generating Station Fuel Cost Variance component
- 8 of the new account.⁸
- 9 ○ The existing RSP rates would continue until the rates are changed in 2022 at which
- 10 time the RSP Fuel Riders would be discontinued and the RSP Current Plan rates would
- 11 be revised.
- 12 ○ The RSP Current Plan rates would not include any recovery of the amounts transferred
- 13 from the Hydraulic Production Variation component of the RSP, the Revised Energy
- 14 Supply Cost Variance Deferral Account, the Holyrood Conversion Rate Deferral
- 15 Account or the Isolated Systems Supply Cost Variance Deferral Account.⁹
- 16 ○ The timing of the RSP rate changes, which are scheduled on January 1, 2022 for
- 17 Industrial customers and July 1, 2022 for Utility customers, would be dependent on the
- 18 implementation schedule of the rate mitigation plan.
- 19 • The recovery of the amounts transferred from the discontinued accounts would not begin
- 20 until after Hydro files an application for the approval of a plan for the recovery following
- 21 the conclusion of its next general rate application.¹⁰
- 22

23 The Board accepts that, with the changes in supply on the Island Interconnected system as a result

24 of the commissioning of the Muskrat Falls Project and deferral of the supply costs through the new

25 deferral account, the RSP, the Revised Energy Supply Cost Variance Deferral Account and the

26 Holyrood Conversion Rate Deferral Account will no longer be necessary. The Board agrees that

27 these accounts should be concluded but has significant concerns in relation to the proposal to defer

28 the recovery of existing balances until after the conclusion of Hydro's next general rate application.

29 The recovery of the balances in the Revised Energy Supply Cost Variance Deferral Account, the

30 Holyrood Conversion Rate Deferral Account and a portion of the Hydraulic Production Variation

31 balance would normally begin in the year after being incurred.¹¹ Instead Hydro proposes that, after

32 the conclusion of its next general rate application, it will file an application for the recovery of the

33 balance in the new Supply Cost Variance Deferral Account which would include the historical

34 balances. Given the ongoing uncertainty as to the timing of Hydro's next general rate application,

35 and considering it is likely to be a lengthy proceeding, the Board is concerned that Hydro's

36 proposals would mean that it would be some time before the historical balances would begin to be

37 recovered from customers. These are historical balances which were incurred in the provision of

38 service prior to the commissioning of the Muskrat Falls Project. The Board does not believe that

⁷ The monthly activity includes the monthly transfers reflecting the approved RSP adjustments to the Current Plan of the RSP, and transfers from the Rural Rate Alteration component of the new account.

⁸ NP-NLH-007, Attachment 1 sets out the forecast balance at October 1, 2021 is approximately \$66.1 million in the Hydraulic Production Variation component of the RSP Variance Deferral Account.

⁹ PUB-NLH-007, NP-NLH-009 and NP-NLH-026.

¹⁰ PUB-NLH-003, IIC-NLH-013 and NP-NLH-026.

¹¹ The current RSP Rules provide that twenty-five percent of the balance in the Hydraulic Production Variation component of the RSP and all of the financing charges are recovered through the RSP Current Plan rates in the following year.

1 it is appropriate to transfer these balances to the Supply Cost Variance Deferral Account which is
2 intended for the deferral of costs associated with the commissioning of the Muskrat Falls Project.
3 These balances are not related to the Muskrat Falls Project and the proposed transfer to the new
4 account would not provide for the transparent collection of these balances apart from the unrelated
5 Muskrat Falls Project costs. To be consistent with the principle of intergenerational equity the
6 Board believes that there should be timely recovery of supply costs incurred prior to the
7 commissioning of the Muskrat Falls Project.
8

9 The Board notes that Hydro stated it did not foresee any issues with maintaining the balances in
10 the Revised Energy Supply Cost Variance Deferral Account and the Holyrood Conversion Rate
11 Deferral Account to be addressed in an application filed in the spring of 2022, though it was noted
12 that the dead band in the accounts may need to be changed.¹² In terms of the balance in the
13 Hydraulic Production Variation component of the RSP, Hydro expressed the view that several
14 factors would need to be considered prior to developing a plan for the recovery of the existing
15 balance from customers, including the potential material upward pressure on Island Industrial
16 customer rates and the availability of information related to the rate mitigation plan.¹³ Hydro also
17 noted concerns in relation to the number of rate changes in 2022 and indicated that the timing of
18 the 2022 rate changes may be dependent on the implementation schedule of the rate mitigation
19 plan. The Board believes that concerns about rate shock should be addressed for each customer
20 group as part of the 2022 rate applications, especially given that the projected 2022 rate changes
21 are significantly different for the Utility and Industrial customers.¹⁴ In terms of the concerns related
22 to the rate mitigation plan and the number of rate changes the Board notes there is ongoing
23 uncertainty as to these issues and does not believe that timely collection of historic balances should
24 be changed on this basis.
25

26 The Board concludes that the RSP, the Revised Energy Supply Cost Variance Deferral Account,
27 and the Holyrood Conversion Rate Deferral Account should be maintained to provide for the
28 transparent and timely recovery of the historical balances. For the same reason the 2022 rate
29 adjustments should proceed as scheduled on January 1 and July 1. A plan for the reasonable
30 recovery of the historic balances, giving consideration to rate impacts and timing, will need to be
31 developed by Hydro and proposed for the approval of the Board. This may require changes to the
32 normal approach for the recovery of the balance in the Hydraulic Production Variation component
33 of the RSP for either the Industrial customers and/or Utility customers. Hydro's proposal with
34 respect to the balances in the Revised Energy Supply Cost Variance Deferral Account, and the
35 Holyrood Conversion Rate Deferral Account should be addressed in the applications to be filed in
36 the spring pursuant to the provisions of the accounts. Hydro will need to apply for approval of
37 changes to the account definitions and to address the determinations of the Board as well as any
38 concerns about the dead bands in the accounts.
39

40 The Board also has concerns in relation to the proposal to discontinue the Isolated Systems Supply
41 Cost Variance Deferral Account and include a Isolated Systems Supply Cost Variance component

¹² PUB-NLH-032.

¹³ PUB-NLH-008, page 1.

¹⁴ NP-NLH-010 sets out average rate reductions of approximately 8% for retail customers and increases of approximately 20% for Island Industrial customers. IIC-NLH-028 sets out that the primary reason for the increase for the Island Industrial customers is the elimination of the Fuel Rider.

1 in the new account. The Isolated Systems Supply Cost Variance Deferral Account was approved
2 in Order No. P.U. 22(2017) to permit Hydro to defer price variances from the test year related to
3 fuel and power purchases on Hydro's Isolated systems. These variances are related to Hydro's
4 Isolated systems and are not related to the commissioning of the Muskrat Falls Project. Hydro
5 confirmed that the balance in this account is not impacted by supply costs related to Muskrat Falls
6 and the operation of the Isolated Systems Supply Cost Variance Deferral Account would remain
7 the same after the implementation of the Supply Cost Variance Deferral Account.¹⁵ Given that this
8 variance is not related to the Muskrat Falls Project and to ensure transparency the Board believes
9 that the Isolated Systems Supply Cost Variance Deferral Account should be maintained and the
10 balances recovered separate and apart from the Supply Cost Variance Deferral Account.

11
12 The parties raised concerns in relation to two aspects of the proposed Supply Cost Variance
13 Deferral Account - financing charges and greenhouse gas performance credit revenues. Both
14 Newfoundland Power and the Industrial Customer Group opposed the use of Hydro's approved
15 WACC in the calculation of financing charges in the account. The Industrial Customer Group
16 submitted that interest should be accrued at prevailing short-term borrowing costs and noted that,
17 in the near-term, the account will primarily operate with negative balances, the balances are
18 expected to be material and fast-growing, and the payments will be made using short-term debt
19 financing. According to the Industrial Customer Group it is inconsistent with rate mitigation to
20 compensate Hydro for using high cost long-term capital to finance the proposed account when
21 Hydro will use lower-cost capital for this purpose. Newfoundland Power also submitted that short-
22 term financing costs be used until the long-term approach is determined through Hydro's next
23 general rate application. According to Newfoundland Power there is no reason to treat this account
24 differently than Hydro's existing supply cost variance deferral accounts or the proposed sustaining
25 capital deferral account. In response Hydro proposed the use of the 2019 Test Year Embedded
26 Cost of Debt, considering the blending of the historic balances from Hydro's existing deferral
27 accounts with the payments under the Muskrat Falls Project agreements. Given that the Board has
28 determined that the existing balances will not be included in the Supply Cost Variance Deferral
29 Account and considering that Hydro plans to use short-term borrowing in the near-term, the Board
30 believes that it is appropriate to use short-term borrowing costs as the basis for the calculation of
31 the financing charges. Hydro will need to develop a proposal in relation to the short term borrowing
32 costs to be used in the calculation of the financing charges in the account.

33
34 In relation to the greenhouse gas performance credits the Industrial Customer Group suggested
35 that, to be fair, the revenues received for the years 2019, 2020 and 2021 should also be credited to
36 the benefit of customers. The Board notes that the revenues for these years were not included in
37 Hydro's 2019 Test Year costs and were not reflected in a deferral account and agrees that requiring
38 that the 2019 and 2020 revenues be credited to the benefit of customers at this stage may constitute
39 retroactive ratemaking. The Board accepts Hydro's proposal that the 2021 greenhouse gas
40 performance credit revenues be included in the account.

41 42 *Conclusion on the Supply Cost Variance Deferral Account*

43
44 The Board accepts that the costs to be incurred by Hydro in relation to the commissioning of the
45 Muskrat Falls Project should be deferred through the approval of a deferral account, but finds that

¹⁵ PUB-NLH-032.

1 the Supply Cost Variance Deferral Account definition should be revised to include only the
2 following proposed components:

- 3 i) Muskrat Falls Project cost variances;
- 4 ii) Rate mitigation funding;
- 5 iii) Project cost recovery from customers;
- 6 iv) Holyrood Thermal Generating Station fuel cost variance, excluding the proposed transfer
7 of the RSP Hydraulic Production Variation component balance;
- 8 v) Other Island Interconnected System Supply cost variance, excluding the proposed
9 transfer of the balances in the Revised Energy Supply Cost Variance Deferral Account
10 and the Holyrood Conversion Rate Deferral Account;
- 11 vi) Net revenue from exports variance, including the proposed IFRS deviation;
- 12 vii) Transmission tariff revenue variance;
- 13 viii) Load variation;
- 14 ix) Rural Rate Alteration, including the variance from the test year load forecast for Hydro
15 Rural Island Interconnected System customers; and
- 16 x) Greenhouse gas credit revenues variance, including the 2021 variance.

17
18 The Supply Cost Variance Deferral Account definition should also reflect the calculation of
19 financing charges based on Hydro's short-term borrowing costs. The Hydraulic Production
20 Variation component and the Current Plan balances of the RSP can continue to be calculated using
21 Hydro's approved WACC and the three existing supply accounts should continue without monthly
22 interest charges as they are included in the 2019 Test Year rate base.

23
24 The RSP Rules and the existing account definitions for the Revised Energy Supply Cost Variance
25 Deferral Account and the Holyrood Conversion Rate Deferral Account should be revised to reflect
26 the determinations of the Board in this Order. The Isolated Systems Supply Cost Variance Deferral
27 Account should be maintained separate from the Supply Cost Variance Deferral Account.

28
29 To ensure timely and predictable rate changes Hydro should file rate applications for January 1,
30 2022 rates for Industrial Customer and July 1, 2022 rates for utility and rural customers. These
31 applications should include a proposal for the reasonable recovery of the historic balances in
32 accordance with the principle of intergenerational equity and the avoidance of rate shock.

33
34 The Board also believes that in the coming months it will be important for Hydro to keep the Board
35 and the parties informed as to the circumstances surrounding the payments pursuant to the Muskrat
36 Falls Project agreements. The Board shares Newfoundland Power's concern with respect to the
37 forecast material deferred supply cost balances.¹⁶ In addition, as noted by the Consumer Advocate,
38 there continue to be numerous uncertainties stemming from the Muskrat Falls Project. Given the
39 potential risks associated with a delay in the approval of the Application, the Board will not delay
40 its Order on the basis of these uncertainties but will require that Hydro file updates to keep the
41 Board and the parties informed as to the balances in the Supply Cost Variance Deferral Account,
42 the circumstances surrounding the commissioning of the Muskrat Falls Project and the plan for the
43 mitigation of rates.

¹⁶ PUB-NLH-022 sets out that Hydro has adequate short-term borrowing capacity to make approximately five months in payments without rate mitigation funding or additional revenue from customers.

1 (ii) Holyrood Thermal Generating Station Accelerated Depreciation

2
3 The Application requests approval of the Holyrood TGS Accelerated Depreciation Deferral
4 Account to defer the difference between the actual accelerated depreciation expense in 2022 and
5 test year depreciation expense related to the Holyrood Thermal Generating Station assets that are
6 scheduled for retirement. The Application states that Hydro is projecting a material increase in
7 depreciation expense for these assets in 2022 as a result of the use of accelerated depreciation and
8 the projected end of generation date.¹⁷ This increase is not reflected in existing customer rates.

9
10 The Industrial Customer Group submitted that the deferral account is unnecessary and inconsistent
11 with fair prospective ratemaking as it is well-accepted practice that rates are adjusted for the
12 addition and disposal of old assets in a general rate application. According to the Industrial
13 Customer Group approval of an increase in Holyrood Thermal Generating Station depreciation
14 expense without reflecting other cost changes which may offset this increase is inconsistent with
15 normal future forward test year regulation. Newfoundland Power supported the proposed
16 Holyrood TGS Accelerated Depreciation Deferral Account but suggested that the 2023
17 depreciation expense variance also be included in the deferral account since it is forecast to be
18 much lower than 2022. Hydro replied that the additional capital investments in the Holyrood
19 Thermal Generating Station since 2019 were necessary and prudent. Hydro submitted that the
20 uncertainty around the decommissioning of the Holyrood Thermal Generating Station as a
21 generating facility is impacted by several factors beyond Hydro's control, including the
22 commissioning of the Labrador-Island Link. According to Hydro the proposed deferral account
23 would avoid negative impacts on Hydro's 2022 earnings as a result of a forecast material increase
24 in Hydro's actual depreciation expense in 2022 of approximately \$13.2 million.¹⁸ Hydro noted that
25 2023 is expected to be a test year, though it was not opposed to including the 2023 depreciation
26 expense variance in the deferral account should 2023 not be a test year.

27
28 While rates are based on test year costs and, in the absence of special circumstances, variances in
29 costs between general rate applications are normally borne by the utility, there are circumstances
30 where a utility may apply to defer costs between test years. The Board acknowledges that the
31 planned transition of the Holyrood Thermal Generating Station to synchronous condensing mode
32 has been delayed for a number of years as a result of the delay in the commissioning of the Muskrat
33 Falls Project, which is beyond Hydro's control. The increase in depreciation costs in 2022 for these
34 assets is material, approximately \$13.2 million. This is much larger than the variances over the
35 2019 to 2021 period which were on average approximately \$2.5 million each year.¹⁹ The Board is
36 satisfied that the forecast increase in the depreciation expense for 2022 is sufficient to have a
37 material impact on Hydro's opportunity to earn a fair return. The Board believes that approval
38 should be granted for Hydro to defer depreciation expense variances greater than \$2.5 million in
39 2022 for the Holyrood Thermal Generating Station assets. In addition Hydro does not oppose
40 including 2023 in the deferral account should 2023 not be a test year. Given the ongoing
41 uncertainty associated with the timing of the filing of Hydro's next general rate application the
42 Board believes that the deferral account should be revised to also include the 2023 variance if it is

¹⁷The projected end of generation date is March 31, 2023.

¹⁸ Hydro's submission, page 7.

¹⁹ Based on Hydro's submission, page 7 the variance was (\$2.6) million in 2019, \$2.7 million in 2020 and is forecast to be \$2.2 million in 2021.

1 not a test year. The Board is satisfied that the Holyrood TGS Accelerated Depreciation Deferral
 2 Account should be established with a revised definition to defer variances in excess of \$2.5 million
 3 for 2022 and also 2023 if it is not a test year.

4
 5 (iii) IFRS Deviation
 6

7 The Application requests approval to deviate from IFRS, using IFRS 14 - *Regulatory Deferral*
 8 *Accounts* to allow Hydro to recognize the power purchase costs relating to the delivery of post-
 9 commissioning energy in accordance with the commercial terms of the Muskrat Falls PPA and the
 10 Transmission Funding Agreement.²⁰ The payment terms of these agreements are structured to
 11 recover the Muskrat Falls Project costs primarily using fixed monthly payments which do not vary
 12 by the amount of the energy purchases. Absent an approved deviation, IFRS would require Hydro
 13 to recognize the costs under the Muskrat Falls PPA and the Transmission Funding Agreement in
 14 a manner that will not match the payment terms. Under IFRS 14 - *Regulatory Deferral Accounts*,
 15 the deviations would result in a regulatory adjustment on Hydro's income statement and a
 16 corresponding regulatory asset or liability on Hydro's balance sheet.

17
 18 Newfoundland Power supported the proposed IFRS deviations and the Industrial Customers and
 19 the Consumer Advocate did not oppose or provide comment. The Board notes that the proposed
 20 deviation is similar to the treatment approved in Order No. P.U. 9(2021).²¹ The approval of the
 21 proposed IFRS deviation will have no impact on customers and is consistent with Hydro's past
 22 regulatory accounting policies of recognizing purchase power expenses. The Board is satisfied that
 23 the proposed IFRS deviations should be approved.

24
 25 (iv) Muskrat Falls PPA Sustaining Capital Deferral Account
 26

27 The Application requests approval of the Muskrat Falls PPA Sustaining Capital Deferral Account
 28 to defer contributions required to be made by Hydro for sustaining capital investments pursuant to
 29 the Muskrat Falls PPA until the approach to be taken to recover these costs is determined in
 30 Hydro's next general rate application. This agreement requires Hydro to make operating cost
 31 payments, which include sustaining capital contributions as they are incurred for the Muskrat Falls
 32 generating assets and the Labrador Transmission Assets. According to Hydro recognizing
 33 sustaining capital costs as required by the Muskrat Falls PPA would not match the timing of the
 34 benefit they provide. Hydro believes that this approach is inconsistent with intergenerational equity
 35 principles and may lead to rate volatility because ratepayers would be required to pay the full
 36 amount of sustaining capital investments as they are incurred.

37
 38 The Board notes that capital costs are normally amortized over the expected life of the asset which
 39 allows for the matching of the expenditures with the timing of the benefit it provides, consistent
 40 with intergenerational equity principles. The approval of the Muskrat Falls PPA Sustaining Capital
 41 Deferral Account to defer the required payments would avoid Hydro having to treat these
 42 sustaining capital costs as operating expenses in the year they are incurred in accordance with the

²⁰ Order No. P.U. 13(2012) approved Hydro's adoption of IFRS. Hydro elected at that time to adopt IFRS 14 -
 Regulatory Deferral Accounts which permits Hydro to continue to have regulatory deferral account balances.

²¹ In Order No. P.U. 9(2021) the Board approved Hydro's proposal to deviate from IFRS related to the purchase of
 pre-commissioning energy in accordance with the terms of the Muskrat Falls PPA.

1 Muskrat Falls PPA and allow a decision to be made in Hydro's next general rate application as to
2 how the payments should be recovered from customers. The Board notes that the parties did not
3 oppose the approval of the Muskrat Falls PPA Sustaining Capital Deferral Account. The Board is
4 satisfied that the proposed Muskrat Falls PPA Sustaining Capital Deferral Account should be
5 approved.
6
7

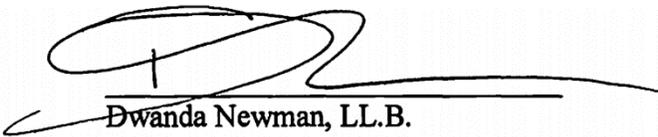
8 **IT IS THEREFORE ORDERED THAT:**
9

- 10 1. The proposal to establish an account to defer payments under the Muskrat Falls Project
11 agreements, rate mitigation funding, project cost recovery from customers and supply cost
12 variances is approved, and Hydro shall file for the approval of the Board a Supply Cost
13 Variance Deferral Account definition reflecting the determinations of the Board in this Order,
14 to be effective on the date upon which Hydro is required to begin payments under the Muskrat
15 Falls Power Purchase Agreement.
16
- 17 2. The proposals related to the discontinuance of the Rate Stabilization Plan, the Revised Energy
18 Supply Cost Variance Deferral Account, the Isolated Systems Supply Cost Variance Deferral
19 Account and the Holyrood Conversion Rate Deferral Account are not approved, and Hydro
20 shall file for the approval of the Board revised RSP Rules and Revised Energy Supply Cost
21 Variance Deferral Account and Holyrood Conversion Rate Deferral Account definitions
22 reflecting the determinations of the Board in this Order, to be effective on the same date that
23 the Supply Cost Variance Deferral Account is effective.
24
- 25 3. The deferral of the Holyrood Thermal Generating Station accelerated depreciation expense
26 variance beginning in 2022 is approved, and Hydro shall file for the approval of the Board a
27 Holyrood Thermal Generating Station Accelerated Depreciation Deferral Account definition
28 reflecting the determinations of the Board in this Order, to be effective January 1, 2022.
29
- 30 4. The proposed deviation from International Financial Reporting Standards to allow Hydro to
31 recognize power purchase costs relating to the delivery of post-commissioning energy in
32 accordance with the commercial terms of the Muskrat Falls Project agreements is approved.
33
- 34 5. The proposed Muskrat Falls Power Purchase Agreement Sustaining Capital Deferral Account
35 is approved to be effective on the date upon which Hydro is required to begin payments under
36 the Muskrat Falls Power Purchase Agreement.
37
- 38 6. Hydro shall pay all expenses of the Board arising from this Application.

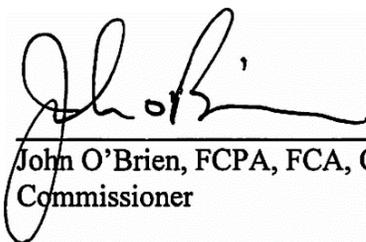
DATED at St. John's, Newfoundland and Labrador, this 8th day of December, 2021.



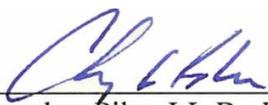
Darlene Whalen, P. Eng., FEC
Chair and Chief Executive Officer



Dwanda Newman, LL.B.
Vice-Chair



John O'Brien, FCPA, FCA, CISA
Commissioner



Christopher Pike, LL.B., FCIP
Commissioner



Cheryl Blundon
Board Secretary