Q. **Reference: Schedule 7: Capital Programs and Projects, Program 9: Perform Facilities Refurbishments (2026)**

Page 2, lines 1-2. In creating the budget estimate for this program Hydro started by applying a depreciation value of 2% against its current building systems inflation-adjusted original cost of $274.0 million.

a) Explain how this approach is consistent with the Capital Budget Application Guidelines.

b) Has Hydro previously proposed this methodology for estimating a project or program budget for approval by the Board?

c) Is Hydro aware of other Canadian regulatory jurisdictions where this methodology is used by utilities for estimating a project or program budget?

d) Why were historical estimates or condition assessment estimates not used to create the budget estimate for this program?

A. **a)** The provisional Capital Budget Guidelines do not set out the estimating methodology that is to be used for capital projects or programs. For example, Newfoundland and Labrador Hydro ("Hydro") has Capital Programs which are based on detailed estimation of the annual work scope, as well as programs for which the budget is based on analysis of historical averages. For its Perform Facilities Refurbishments Program, Hydro is proposing what constitutes an investment target to address deficiencies identified through condition assessments and enable an appropriate level of investment in its facilities, while maintaining investment at a level that is proportional to asset value while reflecting inflation. To establish the annual budget for the Perform Facilities Refurbishments Program, Hydro is utilizing annual depreciation of its facilities assets as an analogue for the level of deterioration of these assets.

Depreciation offers a reasonable analogue for the physical depreciation of assets and the investment required to maintain them because both concepts describe the inevitable decline in value and functionality over time. While financial depreciation is an accounting tool rather than a direct measure of wear and tear, it reflects an estimate of how an assets value is consumed over time due to wear and tear, obsolescence, or age. Targeting investment equal to the depreciation of the asset provides a reasonable investment target to maintain the value and function of the asset, which is directly proportional to asset value considering inflation. The Inflation-Adjusted Original Cost was calculated using original asset values from Hydro's asset financial records, escalated to 2025 dollars using CPI inflators provided by Statistics Canada. 2% depreciation is applied to reflect a straight-line, 50-year depreciation assumption for these assets.

This level of investment will allow Hydro to address the deferred maintenance on its facilities as identified through condition assessments, while establishing a reasonable investment target tied to asset value, in light of the significant level of investment required to sustain its core assets and integrate new assets onto the system.

Due to the smaller nature of the scopes of work to be addressed within this program, establishment of an estimate based on detailed estimation of each work scope is considered inefficient and administratively burdensome. The scopes of work to be addressed within this program are high in quantity but are generally minor in nature and of low materiality. Establishment of an investment target and selection of work scopes based on risk prioritization and risk-spend efficiency achieves Hydro's goal of addressing deferred maintenance on its facilities to ensure their longevity while managing costs. Hydro will continue to assess the performance of this program to ensure it is achieving this goal, primarily by measuring the reduction of high and medium-risk items in its facilities deficiencies backlog, provided as Appendix A of the program proposal. Hydro will continue to assess the utilization of a depreciation-based investment target in the establishment of the program budget against this goal and will propose changes to this approach should this level of investment not enable such a reduction in high- and medium-risk items.

b) No, Hydro has not previously proposed this methodology for estimating a project or program budget for approval by the Board of Commissioners of Public Utilities.

c) Hydro is not aware of other Canadian regulatory jurisdictions in which this methodology is utilized by utilities for estimating a project or program budget. While Hydro has reviewed Newfoundland Power Inc.'s method for addressing deteriorated properties, it has not performed a broader jurisdictional scan.

Hydro notes that completing such a scan may not provide comparable data for review due to differences in prevailing regulatory legislation, utility configuration and scale, population density, physical geography, and other unique jurisdictional characteristics. As stated by Midgard Consulting Inc., the majority of Canadian jurisdictions explicitly or implicitly set capital envelope spending limits as part of rate decisions, including but not limited to, the jurisdictions of British Columbia, Alberta, Saskatchewan, Manitoba and Ontario.[1]

d) Please refer to Hydro's response to part a) of this response.

[1] "Capital Budget Application Guidelines Review – Midgard Consulting Report – Revised," Board of Commissioners of Public Utilities, March 30, 2020.