Q. Please explain why Hydro is proposing to begin cost recovery in 2026, rather than in its 2027 test year, including the relevance of section 80 of the Act associated with the effective date of January 1, 2026.

A. The Allowance for Funds Used During Construction ("AFUDC") Deferral Account is proposed to capture the difference between AFUDC and Interest During Construction ("IDC") effective January 1, 2026. This is when the difference between AFUDC and IDC becomes more material, and setting the effective date for then allows Newfoundland and Labrador Hydro ("Hydro") to defer an additional $2.1 million in interest costs to help improve the Return on Equity for 2026[1] by approximately 29 basis points. The account definition requires amortization to commence in the year after the transfer of the cost to the AFUDC Deferral Account. Therefore, Hydro is proposing to begin cost recovery of the balance in the account in 2027.

Hydro is proposing to include the account balance in its regulated rate base as of January 1, 2026. As Hydro notes within the application, Section 80(1) of the *Public Utilities Act* states that a public utility is entitled to earn annually a just and reasonable return. In Appendix A to Board of Commissioners of Public Utilities ("Board") Order No. P.U. 8(2007), the Board noted that the just and reasonable rate of return ". . . allowed on rate base is equivalent to the cost of capital representing the sum of the weighted costs of both debt and equity in the capital structure."[2] Hydro submits that AFUDC, which reflects the full cost of capital, is more consistent with the entitlement to a just and reasonable return than IDC, which reflects only debt financing costs. Accordingly, Hydro proposes to begin recording AFUDC–IDC variances as of January 1, 2026, when the material under-recovery first arises. Hydro acknowledges that the impact of AFUDC will not be included in customer rates until Hydro's 2027 Test Year is approved.

[1] Hydro's Return on Equity is forecast to be approximately 3.1% in 2026, including the proposed impact of the AFUDC Deferral Account, compared to an approved Return on Equity of 8.60%.
[2] Board Order No. P.U. 8(2007), Part Five, app. A, p. 10 of 11.