STEWART McKELVEY
LAWYERS • AVOCATS

Queen's Marque, 600-1741 Lower Water Street, P.O. Box 997
Halifax NS B3J 2X2 Canada tel: 902.420.3200 fax: 902.420.1417 stewartmckelvey.com

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Nancy G. Rubin, K.C.
Direct Dial: 902.420-3337
nrubin@stewartmckelvey.com

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Delivered by E-mail

Crystal Henwood
Regulatory Affairs Officer/Clerk
Nova Scotia Utility and Review Board
3rd Floor, 1601 Lower Water Street
PO Box 1692, Unit "M"
Halifax NS B3J 3S3

Dear Ms. Henwood:

Re: M11990 – NSPI – WACC and AFUDC Rates Application for 2025

These submissions are filed on behalf of the Industrial Group.

NSPI has applied to lower the current Weighted Average Cost of Capital (**WACC**) and Allowance for Funds Used During Construction (**AFUDC**) rates to align with the updated financial cost of capital. The proposed rate is now 6.66%.

The Industrial Group limits its comments to the change in methodology to calculate short term interest rate forecasting. Specifically, the use of the Bloomberg Outlook rate and the use of the Canadian Overnight Repo Rate Average ("**CORRA**") to calculate short-term debt.

Change in Methodology

NSPI stated that the methodology employed to calculate WACC/AFUDC is consistent with that used in prior GRAs and WACC Applications.[1] At the same time, NSPI acknowledged that it "updated" its short-term interest rate forecasting methodology from relying on T-Bills information from five Canadian banks to incorporating an average short-term interest rate from Bloomberg,[2] along with adopting the new CORRA as the Canadian dollar benchmark.[3] These are both new components to the calculation for short term interest rate forecasting.

NSPI disagrees that these are modifications to the methodology used based on the proposition that using a different Treasury Bill rate and different benchmark rate does not change that NSPI is forecasting its short-term borrowing rate by calculating the spread between its commercial paper rate and forecast Canadian Treasury Bill rates.[4] While the overall approach may be similar, the rates used to calculate the interest forecast are key components of the methodology used by

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1 Exhibit N-1, Application, at page 5, lines 8-10.

2 Exhibit N-3, NSPI (IG) IR-1(a).

3 Exhibit N-1, Application, page 7, lines 1-3.

4 Exhibit N-3, NSPI (IG) IR-1(b).

NSPI and approved by the Board. This is precisely the issue addressed in the 2024 WACC and AFUDC proceeding (M11563), when the Board specifically confirmed that NSPI had "chosen to change its methodology for estimating short-term interest rates" when NSPI filed using the Bloomberg rate rather than a proxy group of five financial institutions.[5] NSPI has now implemented an additional change with respect to the benchmark reference rate used.

These two methodological changes are now before the Board for approval.

Bloomberg

At the Board's request, NSPI has now provided the requisite information to determine whether the Bloomberg Outlook rate should be used to calculate the short-term interest rate forecasts going forward. NSPI provides three rationales for using Bloomberg data: (1) it improves accuracy of forecasting by using a larger sample size from a more diverse group of financial institutions; (2) it is less cumbersome for NSPI by eliminating the number of manual steps to calculate short term interest; and (3) it aligns with the approach taken by many in the industry as Bloomberg is a widely used, highly reputable source.

NSPI has provided the historical data on Bloomberg dating back to 2022 (the earliest available data), along with the impact on the WACC rates using the Bloomberg rate instead of the five Canadian Banks for this time period.[6] Based on the time period provided, the change in methodology has had little to no impact on the WACC applied for; historically, it would only have changed the rate by ~0.01%.

The Industrial Group agrees that it appears that using the Bloomberg Outlook rate will have minimal impact on rates. NSPI states it will be administratively less burdensome by eliminating manual steps. The Industrial Group expects that there would be a correlative cost reduction, and perhaps more importantly, a reduction in the risk of manual errors. Accordingly, the Industrial Group does not object to using Bloomberg Outlook. It may be appropriate to monitor this periodically to ensure that the differential impact on rates continues to be minimal.

CORRA

The rationale and changes implemented with respect to the transition to Term CORRA from the Canadian Dollar Offered Rate (**CDOR**), is less clear. NSPI states that this is a replacement recommended by the Canadian Alternative Reference Rate (**CARR**) Working Group[7], but it appears that this benchmark rate is not the only available benchmark, nor is the "Term CORRA" the only way to use this rate.

NSPI has stated that the CDOR was previously administered by Refinitiv Benchmark Services (UK) Limited and the calculation and publication of this rate permanently ceased as of June 28, 2024.[8] The transition away from this rate is somewhat complicated, and there are number of

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5 M11563, 2024 WACC and AFUDC Application, Decision Letter dated April 3, 2024, page 2.

6 Exhibit N-3, NSPI (IG) IR-3(b).

7 Exhibit N-3, NSPI (IG) IR-1(c).

8 Exhibit N-1, Application, page 6, lines 29-31.

secondary sources that provide guidance on how to implement this change.[9] The replacement rate recommended by CARR, and most often seen as a replacement for CDOR, is a version of CORRA.[10] The approach used, however, differs. Term CORRA is just one option; it is a forward-looking version that represents the market's future expectations and can be for 1 or 3 months forward.

Regardless, there is an economic difference between CDOR and CORRA and additional steps are needed to address the change.[11] CDOR incorporates a bank credit risk premium, whereas CORRA is risk free. CARR recommended that CORRA or Term CORRA be used with credit spread adjustments to address any impact of the transition on loan transactions. The CARR made no recommendation on the credit spread adjustment to be used, but rather, stated that the adjustment will depend on the market and the bank funding conditions, and is individually determined.[12]

CARR issued a Transition FAQ which articulates the complexities behind this transition to CORRA.[13] Pages 11-13 relate exclusively to the use of Term CORRA and confirm that Term CORRA cannot be used as a benchmark for a managed bond overlay mandate nor benchmarking an investment strategy in that regard. The switch to Term CORRA is not as simple and straightforward as suggested by NSPI, and it is not clear how NSPI has approached this change.

The NSUARB specifically asked NSPI, at IR 4(e) whether NSPI made any adjustments to the credit spread in response to the transition to CORRA.[14] NSPI stated that the transition did not impact NSPI's credit spread and that NSPI's spread compared to the Term CORRA benchmark rate has decreased but the total spread is "fairly consistent" to 2024. This response is confusing when interpreting NSPI's later response to NSUARB IR 12(a), which asks about why NSPI applied its spread to the Outlook T-Bills to Term CORRA rates spread.[15] Presumably, this additional step responds to the issue noted by CARR related to switching to the risk free CORRA. NSPI notes

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9 For example, see commentary on this cessation, and outcome of this change at: Jeffery Nagle, et al, "2024 Update on the Cessation of CDOR and SIBOR", January 26, 2024 (Cadwalader):<https://www.cadwalader.com/fund-finance-friday/index.php?eid=2005&nid=279#:~:text=The%20rate%20recommended%20by%20CARR,Average%20(%E2%80%9CCORRA%E2%80%9D)> ; and Gordon Baird, et al, "The CDOR to CORRA Transition: The End of the Road is Nigh", May 22, 2024 (McCarthy Tetrault): <https://www.mccarthy.ca/en/insights/articles/cdor-corra-transition-end-road-nigh>.

10 Canadian Alternative Reference Rate- Working Group, "Transitioning Loans from CDOR to CORRA – Best Practice", July 21, 2023 (Bank of Canada): <https://www.bankofcanada.ca/wp-content/uploads/2023/07/best-practices-transitioning-loans-cdor-corra.pdf>.

11 Canadian Alternative Reference Rate- Working Group, "Transitioning Loans from CDOR to CORRA – Best Practice", July 21, 2023 (Bank of Canada) at page 2.

12 Canadian Alternative Reference Rate- Working Group, "Transitioning Loans from CDOR to CORRA – Best Practice", July 21, 2023, (Bank of Canada) at page 3; and Canadian Alternative Reference Rate-Working Group, "CDOR Transition FAQs", July 10, 2024, (Bank of Canada) at page 7: <https://www.bankofcanada.ca/wp-content/uploads/2023/08/cdor-transition-faqs.pdf>.

13 Canadian Alternative Reference Rate- Working Group, "CDOR Transition FAQs", July 10, 2024, (Bank of Canada).

14 Exhibit N-4, NSPI (NSUARB) 4(e).

15 Exhibit N-4, NSPI (NSUARB) 12 (a).

that while the total spread is "fairly consistent", the presentation has changed. Based on the Industrial Group's understanding of the Term CORRA being risk free, compared to the previous CDOR, it appears that this is a required new step in the calculation to use a credit spread adjustment and is undoubtedly a change in the methodology used.

While this change to the Term CORRA appears in line with the industry change from the CDOR, the Industrial Group questions the characterization of this transition being outside of NSPI's decision making.[16] The CARR provides a recommendation, but it is NSPI that must implement the change, individually choosing what option makes the most sense for the purposes used.

The present Application, as filed, does not present any apparent impediment to utilizing this new rate, although the reporting from NSPI makes it difficult to truly appreciate the impact of this change. The reporting that it was outside NSPI's choice to implement this new rate,[17] or that it has "no impact" to short-term borrowing costs does not present an accurate, or at least complete, picture of what this transition means. It is also difficult to understand how, or why the calculated spread at Appendix A page 5 was reached.

It is recommended that if NSPI wishes to have this approved, it should provide a more complete response regarding how this transition has been implemented, what went into the decision-making to choosing the Term CORRA approach used, including the credit spread adjustment at Appendix A page 5, and what, if any, this change in rate has on the calculation of short-term borrowing costs.

CONCLUSION

The Industrial Group does not object to the change to using Bloomberg data and recommends that if not included as part of its Reply, the Board direct NSPI to more clearly justify the choice and impact of using the Term CORRA rate instead of the CDOR for the 2025 calculations within a compliance filing. Thank you for the opportunity to submit these comments.

Yours truly,

Nancy G. Rubin, K.C.

Brianne Rudderham

NGR/BER/lmc

cc Bill Mahody
Participants in M11990

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16 Exhibit N-3, NSPI (IG) IR-1(c).

17 Exhibit N-3, NSPI (IG) RIR -1 (c).