IN THE MATTER OF the Public
Utilities Act, R.S.N. 1990, Chapter P-47
(the "Act"), and

IN THE MATTER OF a General Rate Application
(the "Application") by Newfoundland and Labrador Hydro
for approvals of, under Section 70 of the Act, changes
in the rates to be charged for the supply of power and
energy to Newfoundland Power, Rural Customers and
Industrial Customers; and under Section 71 of the Act,
changes in the Rules and Regulations applicable to the
supply of electricity to Rural Customers.

Requests for Information

From Newfoundland and Labrador Hydro

(2006 NLH GRA)

Newfoundland and Labrador Hydro, Applicant

November 8, 2006

Newfoundland and Labrador Hydro ("Hydro") 2006 General Rate Application

Requests for Information from Hydro
To <u>Newfoundland Power Inc.</u>

NLH 7 NP Re: Evidence of Patrick Bowman, page 5, line 13 & section 7 pgs 39 - 42; and Evidence of Douglas Bowman pgs 17 - 19, and page 32 lines 12 - 14

(a) In light of PU 14 (2004) pages 147 - 149 and the status of the Province's Energy Plan, what is NP's position on the appropriateness of a formal IRP exercise in which both Hydro, NP and other interested parties would be required to participate?

(b) Specifically, what is NP's view on the following:
  i. timing;
  ii. participants;
  iii. cost; and
  iv. whether such an exercise is consistent with least cost electricity under section 3(b) (iii) of the Electrical Power Control Act (NL)?

<u>L. Brockman</u>

NLH 8 NP Re: Page 18, lines 17
With regard to risk protection, please outline the stabilization or other adjustment mechanisms that are used or available to NP including the municipal tax adjustment, automatic adjustment mechanism, hydraulic production, NP fuel cost, purchased power, demand costs from Hydro, rate stabilization account, income tax or any other. In a tabular format show the actual annual amounts of each for the period 2001 to 2005 with a comparison to NP's actual return on equity for each year.

Requests for Information from Hydro
To Consumer Advocate

D. Bowman

NLH 9 CA Is integrated resource planning consistent or inconsistent with the supply of least cost electricity under Section 3 (b) (iii) of the Electrical Power Control Act (NL)?

NLH 10 CA Re: Pages 17 - 19, and page 32, lines 12 - 14.
Based on the consultant's knowledge of the experience in other jurisdictions, please provide:
(a) A list of all likely participants in an integrated resource plan in this Province;
(b) A representative budget for Hydro's participation in a comprehensive integrated resource plan;
(c) A similar budget for the participation of all other necessary parties including, but not limited to, the Board and NP; and
(d) A time schedule for planning for, and completion of, such an IRP.

NLH 11 CA Re: Page 32, lines 12 - 14
Please indicate the scope of the integrated resource plan considered appropriate for the Province of Newfoundland and Labrador with respect to:
(a) Fuel substitution for competitive end use energy demands such as space and water heating;
(b) Environmental externalities; and
(c) Socio-environmental values.

NLH 12 CA Re: Page 32, lines 12 –14
(a) Does Mr. Bowman believe that the correct least cost mix and utilization of energy resources will, more-or-less, prevail in an economy, where:
  i. all pricing in the energy economy reflects marginal cost principles,
  ii. information barriers are addressed, and
  iii. externalities have been addressed, (for example incorporating the cost of atmospheric emissions through the use of economic instruments)
(b) Why, or why not?

RFIs to Consumer Advocate cont'd

NLH 13 CA In light of PU 14 (2004) pages 147 - 149 where the Board expressed its preference for a generic hearing on IRP involving both utilities and other interested parties, does the consultant agree that a generic hearing on this issue is most appropriate?

NLH 14 CA Would the consultant agree that proceeding with an integrated resource plan before the release of the Province's Energy Plan would potentially pose the potential for:

(a) Inconsistency, and/or
(b) Unnecessary expenditure/duplication of costs to the detriment of ratepayers?

NLH 15 CA Please confirm that Hydro's costs for participation in a comprehensive IRP have not been included in the 2007 test year.

NLH 16 CA Re: Page 29, lines 1 – 2
"CEA believes it has a responsibility to develop the appropriate cautions concerning the use of non-verified benchmarking data in regulatory settings, and provide these cautions to members for their use in interfacing with regulatory bodies". Does Mr. Bowman agree that the CEA's position is a legitimate and justifiable concern? Why or why not? (CA 4 NLH Attachment 2, page 2 of 6)

NLH 17 CA Re: Page 29, lines 1 – 2
Does Mr. Bowman agree that regulatory actions using benchmarking data for purposes for which it was not intended can lead to incorrect regulatory results? Why or Why not? (CA 4 NLH Attachment 2, page 2 of 6)

NLH 18 CA Re: Page 28, lines 19 - 21
Please provide a specific and detailed listing of the "numerous other sources for peer group information besides the CEA, including regulatory websites, particularly those jurisdictions with the PBR, utility company annual reports, etc." that will provide reliable and consistent performance data to enable Hydro to externally benchmark each of the KPIs outlined on page 2 of Defining a Utility Peer Group for Newfoundland and Labrador Hydro, December 2004, included as Attachment 1 in CA 4 NLH.

W. Cannon

NLH 19 CA Re: Page 2, lines 34 - 37 and Exhibit MGB-1, Table 1, Page 3.

(a) Is it Dr. Cannon's proposal that the cost rate applied to debt would be adjusted annually during the term of the Automated Adjustment Mechanism?

(b) If the answer to (a) above is yes, on what basis would that rate be adjusted?

(c) If the answer to (a) above is no, is Dr. Cannon then suggesting that the cost rate applied to debt would be preset in year one for each year of the four-year term?

NLH 20 CA Re: Page 2, lines 34 - 37 and Exhibit MGB-1, Table 1, Page 3.

(a) Is it Dr. Cannon's proposal that the cost rate applied to equity would be adjusted annually during the term of the Automated Adjustment Mechanism?

(b) If the answer to (a) above is yes, on what basis would that rate be adjusted?

(c) If the answer to (a) above is no, is Dr. Cannon then suggesting that the cost rate applied to equity would be preset in year one for each year of the four-year term?

NLH 21 CA Re: Page 2, lines 34 - 37 and Exhibit MGB-1, Table 1, Page 3.

(a) Is it Dr. Cannon's proposal that the capital structure ratios would remain fixed at test year levels throughout the term of the Automated Adjustment Mechanism?

(b) Is it Dr. Cannon's proposal that the structure of the rate base and total rate base would remain fixed at test year levels during the term of the Automated Adjustment Mechanism?

(c) Is it Dr. Cannon's proposal that the Weighted Average Cost of Capital would be re-computed annually during the term of the Automated Adjustment Mechanism based on revised cost rates for debt and equity?

(d) Is it Dr. Cannon's proposal that the revised Weighted Average Cost of Capital would then be applied to compute a revised rate of return on rate base annually during the term of the Automated Adjustment Mechanism?

(e) Is it Dr. Cannon's proposal that should the rate of return on rate base computed fall outside the revised allowable return on rate base range, that the revised return on rate base would then become the mid-point of a new allowable return on rate base range, and that rates would be adjusted accordingly for the forthcoming year?

NLH 22 CA Re: Schedule 2 – A, Page 16.

(a) All other things being equal, would Dr. Cannon's forecast embedded cost of debt for 2008 change if, during the review of the Automated Adjustment Mechanism in the fall of 2007, it is determined that Hydro's cost of issuing long-term debt (30-year term) on the first ten trading days in the month of October is 8%?

(b) Please reflect the changes on a revised Schedule 2 - A, page 18.

(c) Please reflect the change in WACC and return on rate base that would flow from such revised assumptions in a table similar in format to Table 1, page 3 of Exhibit MBG-1.

(d) If this revised calculation results in a return on rate base outside of the range, please confirm that a change in rates (effective January 1) would result.

NLH 23 CA Re: Exhibit MGB-1, Table 1, Page 3.

(a) All other things being equal, would Dr. Cannon's cost rate of equity for 2008 change in the event that, during the review of the Automatic Adjustment Mechanism in the fall of 2007, it is determined that Hydro's cost of issuing long-term debt (30-year term) on the first ten trading days in the month of October is 8%?

(b) Would that require a recalculation of the Weighted Average Cost of Capital and rate of return on rate base?

(c) If so, please reflect the changes that would flow from such revised assumptions in a table similar in format to Table 1, page 3 of Exhibit MGB-1.

(d) If this revised calculation results in a return on rate base outside of the range, please confirm that a change in rates (effective January 1) would result?

NLH 24 CA Re: Schedule 4 – A, Page 22.

On what basis has Dr. Cannon assumed that promissory notes outstanding in the amount of $244.6 million at the end of 2010 is an appropriate level of exposure to short-term variable interest rates?

NLH 25 CA Re: Page 5, lines 18 - 33
On what documentation or external sources does Dr. Cannon rely in making the assumptions stated on page 5, and which assumptions underlie his calculations on all schedules. Please provide copies of all such documentation.

NLH 26 CA At the time of his pre-filed evidence, was Dr. Cannon aware of the history of Newfoundland Power's Automatic Adjustment Mechanism? Specifically, was Dr. Cannon aware that the Board had approved the use of a fixed/embedded cost rate for debt in comparison to a forecast cost rate for equity in Newfoundland Power's Automatic Adjustment Mechanism?

NLH 27 CA Would Dr. Cannon's comments respecting the proposed operation of an Automatic Adjustment Mechanism for determining Hydro's annual allowed return on rate base (see page 2, lines 32 - 37 and page 3, lines 1 - 10) apply equally to Newfoundland Power's Automatic Adjustment Mechanism approved by this Board in PU 16 (1998-99), pages 102 – 107; PU 36 (1998-99), pages 69 – 71; PU 19 (2003), pages 62 - 69 and 121; and PU 39 (2005), pages 1 - 3 attached?

NLH 28 CA (a) Is Dr. Cannon aware that this Board considered the implications of variations in the embedded cost of debt on Newfoundland Power's Automated Adjustment Mechanism during Newfoundland Power's 2003 General Rate Application and subsequently ordered (page 67 of its Order PU 19 (2003)) that "NP will be required to modify the schedule filed as part of its annual return that calculates the embedded cost of debt to identify specifically the causes of variations in the actual embedded cost of debt from the cost forecast for the test year period"?

(b) Is Dr. Cannon aware that Hydro proposed a similar filing requirement as part of its proposed Automatic Adjustment Mechanism (Exhibit MGB-1)?

NLH 29 CA (a) Is Dr. Cannon aware that this Board considered the implications of variations in the embedded cost of debt on Newfoundland Power's Automatic Adjustment Mechanism during Newfoundland Power's 2003 General Rate Application and subsequently ordered (page 68 of its Order PU 19 (2003)) that "The Board will establish a mechanism tied to the observed rate of return on regulated common equity which may trigger an early review of the mechanism and cost of capital. Where the actual rate of return on regulated equity in any intervening year exceeds the cost of equity determined by the Formula by more than 50 basis points, then NP will be required to file a report with the Board in its annual return setting out the circumstances and facts contributing to the difference".

(b) Is Dr. Cannon aware that Hydro proposed a similar mechanism as part of its proposed Automatic Adjustment Mechanism (Exhibit MGB-1)?

NLH 30 CA Re: Page 2, lines 34 - 37, on what basis can anyone today accurately predict the trend in interest rates three years hence?

Newfoundland and Labrador Hydro ("Hydro") 2006 General Rate Application

Requests for Information from Hydro
To Public Utilities Board

Grant Thornton

NLH 31 PUB Re: Evidence of Dr. Cannon, page 3, lines 2 - 4 that "Hydro's proposed Automatic Adjustment Mechanism fails to reflect the WACC that the Company is likely to experience in future years by virtue of the fact that the embedded cost of debt in the WACC calculation is held constant, for each year after the test year".

Please indicate whether:
(a) in NP's Board-approved Automatic Adjustment Mechanism, the embedded cost of debt in the WACC calculation is held constant for each year after the test year; and
(b) in Exhibit MGB-1, Hydro's proposal for an Automatic Adjustment Mechanism is consistent with the Board approved Automatic Adjustment Mechanism for NP in this respect.

NLH 32 PUB Re: Evidence of Dr. Cannon, page 2, lines 34 - 37 and his recommendation that the operation of an Automatic Adjustment Mechanism for determining Hydro's annual allowed return on rate base "should incorporate, in the year-by-year calculation of the range for the allowed return on rate base, a weighted average cost of capital ("WACC") value that, subject to forecast error, is as close as possible to the actual WACC likely to be experienced by Hydro in each future year".

Please indicate whether:
(a) In PU 36 (1998-99), the Board (following evidence from its financial consultant) determined that test year values would be used for each of the dependent variables of NP's Automatic Adjustment Mechanism with the exception of the cost of common equity.
(b) Dr. Cannon's recommendation would be contrary to ratemaking principles which are based on test year values.

Requests for Information
From Newfoundland and Labrador Hydro
(2006 NLH GRA)

NLH 27 CA
Referenced Attachments

Excerpts from:
PU 16 (1998-99)
PU 36 (1998-99)
PU 19 (2003)
PU 39 (2005)

without any adjustment for the one-half month revenue recognition lag.

Rate adjustments are to be made without any adjustment of revenue to cost ratios for the different rate classes.

The Board will hear further evidence at the Fall hearing on the accounting methodology for calculating the allowed return on rate base in the context of the relationship between rate of return on rate base and the cost of the various components of capital structure. The Board will also hear evidence with respect to 1998 financial projections. This evidence will be assessed by the Board in determining rates, tolls and charges through a final Order under Section 70 of the *Act*. In setting the allowed return on rate base for 1998, the Board will provide an opportunity to earn a rate of return on common equity of 9.25% for a common equity component deemed to be the lesser of 45% of the capital structure and the projected average common equity ratio in 1998. The Board will estimate the cost of preferred shares at 6.33%, and apply it to the forecast average value of preferred equity and the forecast average value of any common equity in excess of 45%.

COMMISSION DECISION ON ADJUSTMENT MECHANISM

The Board has heard divergent views on the need for an automatic adjustment mechanism. One of the concerns expressed by expert witnesses during the hearing relates to the complexity of the relationship between required returns and bond yields and the need for informed judgement to be exercised. Another concern was that the Company may benefit unduly if upward adjustments occur more quickly in the future than downward adjustments have occurred in the past.

The Board is of the view that there is merit to a formula, in light of the cost burden of a full cost of capital hearing and the potential savings to consumers which could be realized. The Board also believes that the adoption of an automatic adjustment mechanism will create greater predictability, which will thereby reduce the risk of regulatory uncertainty. In the opinion of the Board, a mechanism to facilitate an annual review at modest costs will be of benefit to the ratepayer and to the Company.

The Board is of the view that the proposed adjustment mechanism is within its legislative competence. The wide acceptance of such a mechanism by other Canadian tribunals, to adjust the allowed rate of return, supports its use as being in accordance with "generally accepted sound public utility practice". Given that a formula approach accords with "generally accepted sound public utility practice" and is within the purpose and policies of the governing legislation it is appropriate to adopt such a mechanism. The Coram's opinion provides clarification and interpretation of the powers of the Board. The Coram set out the following general principles, *inter alia*, to be used in the interpretation and application of the legislation:

> "1. The Act should be given a broad and liberal interpretation to achieve its purposes as well as the implementation of the power policy of the province;
>
> 2. The Board has a broad discretion, and hence a large jurisdiction, in its choice of the methodologies and approaches to be adopted to achieve the purposes of the legislation and to implement provincial power policy;
>
> 3. The failure to identify a specific statutory power in the Board to undertake a particular impugned action does not mean that the jurisdiction of the Board is thereby circumscribed; so long as the contemplated action can be said to be "appropriate or necessary" to carry out an identified statutory power and can be broadly said to advance the purposes and policies of the legislation, the Board will generally be regarded as having such an implied or incidental power;
>
> 4. In carrying out its functions under the *Act*, the Board is circumscribed by the requirement to balance the interests, as identified in the legislation, of the utility

against those of the consuming public;..."(pp. 21, 22, paragraph 36)

Adoption of a formula to revise the allowed rate of return on rate base does not limit the discretion of the Board to convene a hearing. The Board believes that there is sufficient flexibility in its governing legislation so that a hearing can be considered when ratepayers, the Company or the Board believe that circumstances so require. The Board will call a hearing if circumstances change, so as to render the use of an automatic adjustment formula to be inappropriate. Without attempting to enumerate all of the circumstances which might result in a hearing being convened, the following are intended as examples:

(a) deterioration in the financial strength of the Company, resulting in an inappropriately low interest coverage;

(b) changes in financial market conditions which would suggest that the formula is not accurately reflecting the appropriate return on equity; and

(c) fundamental changes in the business risk of the Company.

In exercising its discretion to convene a hearing, the Board will ensure that the interests of consumers are protected. The Board has a responsibility under the *Electrical Power Control Act*, 1994, to implement the Power Policy of the Province which requires that the power sources and facilities are managed and operated in a manner:

> "that would result in power being delivered to consumers in the Province at the lowest possible costs consistent with reliable service".[*Electrical Power Control Act*, 1994, Sec. 3(b)(iii)]

The *Act* provides that a complaint may be made to the Board by "an incorporated municipal body or the Newfoundland and Labrador Federation of Municipalities or by five persons, firms or corporations ......”.[*the Act*, Sec. 84(1)]

The Board also has the power to conduct an investigation and to convene a hearing upon its own motion.[the *Act*, Sec. 82 and 88]

While the Board believes that adoption of an automatic adjustment mechanism is desirable, the evidence heard at this hearing relates primarily to the adjustment of the appropriate rate of return on equity. Before articulating an adjustment formula to set the allowed rate of return on rate base for 1999 and subsequent years, the Board wishes to hear further evidence which bears directly on the derivation of the allowed return on rate base.

Recognizing that

> “the analysis of appropriate rates of return on common equity will be undertaken and factored into the conclusion as to what is a just and reasonable return on rate base”.(Opinion of Newfoundland Court of Appeal, June 15th, p. 30, paragraph 61)

The following approach will be adopted in this Order:

(a) An automatic adjustment mechanism will be implemented based upon the equity risk premium model, using the long term (30 years) Government of Canada bonds as the risk free rate. The Board will take an average of the daily closing yields on long term Canada bonds for the last five trading days in the month of October and the first five trading days in the month of November. The Government of Canada bond issues used by the Board will be the 8.00% Issue maturing on June 1st, 2027, and the 5.750% Issue maturing on June 1st, 2029. This average of ten trading days will be adopted as the forecast long term bond rate for the following year to be used in implementation of the formula.

(b) In estimating the appropriate return on common equity the forecast long term bond rate for the following year will be subtracted from the current year’s forecast value. The difference will be multiplied by a factor of 0.20 and the resulting product will be used to adjust the risk premium in the opposite direction. The adjusted risk premium will be added to the forecast long term bond rate to produce the rate of return on equity for the following year.

For example, if the forecast long term bond rate for 1999, as calculated in November, 1998 pursuant to (1) above, were to be 6.75%, then the difference (6.75% - 5.75%) between the current year's forecast and the coming year's forecast would be +1%. This would result in a downward adjustment of 20 basis points in the risk premium from 3.50% (the 1998 value) to 3.30% and an allowed return for 1999 of 10.05%(6.75% + 3.30%).

If the forecast long bond rate were 4.75% then the risk premium would be adjusted upward by 20 basis points so that the allowed return would be 8.45% (4.75% + 3.705).

(c) The resulting rate of return on common equity along with the appropriate rate of return on preferred equity and the embedded cost of debt will be factored into the determination of an allowed rate of return on rate base in a manner to be decided by the Board upon hearing further evidence on accounting methodology in the Fall as to how this can best be achieved.

(d) The mechanism will allow any change in the return on rate base to be determined by the Board through an automatic adjustment mechanism in November or December and any rate change would normally be effective on January 1st of the following year.

(e) The Board will issue an Order for revised rates to be filed for the following year if the change in the rate of return on rate base has the effect of moving the rate of return outside the previously approved range.

(f) With regard to a full cost of capital hearing, the Board determines that after the rate of return on rate base has been set for three consecutive years, by application of the formula, and without a hearing, that a hearing will be convened in the following year.

The Board is of the view that this approach will provide sufficient flexibility to address the concerns expressed at the hearing. The Board also believes that adjustments in the allowed return on rate base should be achieved without imposing upon ratepayers the cost burden of a full cost of capital hearing for each such adjustment.

The Board notes that the automatic adjustment mechanism does not contemplate modifications in the capital structure, which will, for purposes of rate setting, be based upon the lesser of the projected average common equity ratio in the test year, and 45%. The Board believes that the capital structure should be modified with caution and on an infrequent basis. However, should a review of either the capital structure or the rate of return be required, the Board may, on its own motion, upon complaint or by application, conduct a hearing.

COSTS

Pursuant to Section 90 of the *Act*, Counsel for Abitibi requested an Order awarding costs to Abitibi. This application was initially made on April 2, 1998, and petitioned once again at the close of the hearing on June 18, 1998. P. U. 4 (1998-99) ordered that the issue of costs of Abitibi would be considered by the Board at the conclusion of the hearing.

Abitibi participated in the hearing on a limited basis, insofar as they received and reviewed all materials filed, cross-examined expert witnesses and provided final argument. The purpose of the intervention was put forth by Counsel for Abitibi as grounded in their interpretation that the hearing was generic, with effect on both NLP and Hydro. Abitibi, as an industrial customer of Hydro, believed they had an interest in the outcome of the hearing and any policies that might later apply to Hydro.

The Board served notice to the public that a hearing would be held with regard to NLP's current rates, tolls and charges and return on rate base pursuant to the *Act*. Hydro did not participate in this hearing. Abitibi, an industrial customer of Hydro, has a distinctly separate power and order contract with Hydro and Hydro's industrial customer rate will not change as a result of this order. Hydro has not received or reviewed the material filed, cross-examined witnesses nor provided final argument. The order provided on matters raised at this hearing are specific to NLP. Procedural fairness dictates any policies related to Hydro's rate of return and capital structure would require a adopt such a range for both 1998 and 1999.

The range of return on rate base for 1998 will be from 9.63% to 9.99% with a midpoint of 9.81%.

The forecast rate of return on rate base for 1998 is 9.79%, which is slightly below the midpoint of the allowed range of 9.81%.

Finalization of Rates

The rates, tolls and charges set as interim rates by Order P.U. 21 (1998-99) will become final with this Order, under section 70 of the *Act*.

ADJUSTMENT FORMULA

The Board has heard evidence from the company and from the Board's financial consultants on the relationship between rate of return on rate base and the cost of various forms of invested capital. The relevant formulae were presented in the prefiled evidence of Mr. Smith (exhibits KWS-9 and KWS-10). The test year values in these formulae will be used for the purpose of adjusting the return on rate base in years subsequent to a test year until adjusted by Board order. This means, *inter alia*, that when applying the 1999 test year data the Board will use 9.18% as the forecast average cost of embedded debt and 6.33% as the forecast average cost of preferred equity. The weighted average cost of capital will vary with changes in the cost of common equity as forecasted by changes in the long Canada bond rate specified in P.U. 16 (1998-99). Equation 4 shows how "R" will vary with variations in "c" and without changes in other variables.

The introduction of an expanded range of 36 basis points will provide an incentive for the company to improve productivity and will allow for some variation in financial variables other than those adjusted by the formula.

The Board has observed that an increase in the ratio of average invested capital to the average rate base from 1998 to the 1999 test year had the effect of raising the required return on rate base by 12 basis points. The Board has expanded the range of return on rate base to accommodate such unanticipated changes other than changes in the cost of common equity capital. The Board will also consider adjusting the test year values in the adjustment formula if they are no longer appropriate. A capital budget hearing would provide an opportunity to hear evidence as to the need to revise rate base, while a hearing of an application under section 91 of the *Act* would be a suitable venue to hear evidence on invested capital.

The Board will be restating in its order the elements of the mechanism set out in P.U. 16 (1998-99) which will be used to adjust rates annually based upon variations in the rate of return on rate base. This restatement will include the conclusions arising from this hearing based upon its review of accounting methodology, including the following:

The Board accepts the recommendation of its financial consultant that annual reviews by the Board will continue to monitor company expenses.

The Board also accepts the recommendation of its financial consultant that factors such as growth in sales volume should be monitored and that a new revenue requirement should be set through a hearing convened by its own motion if there is reason to believe that the adjustment mechanism has led or would lead to a level of earnings above what the Board believes to be just and reasonable.

In P.U. 16 (1998-99) the Board determined that after the rate of return has been set for three consecutive years by application of the formula and without a specific hearing on the full cost of capital derivation, that a hearing should be convened in the fourth year. The Board accepts the recommendation that such a cost of capital hearing should include a full review of new forward test year projections as is the practice in a general rate hearing.

The adjustment formula set out in Equation 1 of the reasons for decision will be used to set the rate of return on rate base for the forecast year using the risk premium approach to forecast the cost of common equity. Test year values will be used for each of the dependent variables determining the rate of return on rate base, with the exception of the cost of common equity, which will be estimated pursuant to P.U. 16(1998-99).

If test year values become inappropriate, the Board will adjust them after hearing evidence at a capital budget hearing, a hearing pursuant to an application under section 91 of the *Act*, or any other hearing where evidence can be taken as to the need for adjustments of any of the dependent variables in the adjustment formula.

The new rate of return on rate base resulting from application of the formula will be taken as the midpoint of the range which will be allowed for calculating revised rates, tolls and charges. However, if the new rate falls within the range of allowed rate of return on rate base for the current year, the Board will make no adjustment in rates, tolls and charges and maintain the previously allowed range of rate of return on rate base.

CAPITAL PROGRAM FOR 1999

VI. AUTOMATIC ADJUSTMENT FORMULA

In Order No. P.U. 16(1998-99) and P.U. 36(1998-99) the Board ordered the use of an automatic adjustment formula (the *"Formula"*) to set an appropriate rate of return on rate base for NP on an annual basis. The Board also determined that after NP's rate of return on rate base had been set for three consecutive years using the Formula, and without a hearing, then a hearing will be convened in the following year to consider the cost of capital, including a full review of forward looking test year projections.

The Formula put in place by the Board in 1998 is as follows:

$$\textbf{Rate of Return On Rate Base} = \left[\frac{\textbf{Invested Capital}}{\textbf{Rate Base}} \times \textbf{Weighted Average Cost of Capital} \right] + \frac{\textbf{Z}}{\textbf{Rate Base}}$$

Where Z represents amounts which are recognized in the calculation of either weighted average cost of capital or rate of return on rate base, but not both. These amounts include:

(A) Amortization of Capital Stock Issue Expenses;
(B) Interest on Customer Deposits; and
(C) Interest Charges to Construction.

The Formula adjusts NP's rate of return annually based on changes in the forecast cost of common equity. This forecast change is based on changes in long term Government of Canada Bond yields. By use of an equity risk premium approach the Board determined that the appropriate return on regulated equity for NP was the sum of the risk free cost of capital (i.e. the average of long term Government of Canada bond yields) and an adjusted risk premium which varies based upon the changes to the risk free cost of capital. The resulting rate of return on common equity, along with the appropriate rate of return on preferred equity and the embedded cost of debt are then used to calculate the Weighted Average Cost of Capital (WACC). The appropriate rate of return on rate base is calculated by multiplying this WACC by the ratio of forecast average invested capital to forecast average rate base plus a Z factor as shown above. The Formula also adjusts on an annual basis the ROE, forecast average invested capital and average rate base. All other components of the Formula are based on 1999 test year data.

1. Existing Formula Performance

The Formula has been used in each of 1999, 2000 and 2001 to set the rate of return on rate base (and hence rates) for NP for the years 2000, 2001 and 2002. In Order No. P.U. 28(2001-2002) the Board ordered, among other things, that NP undertake a review of the performance of the Formula. The results of this review were filed as part of the evidence in this proceeding. (Exhibit BVP-17)

The following table shows the allowed range of return on rate base as set by the Board for 1997-1999 and as derived by the Formula for 2000-2002 and, for comparison purposes, the actual returns achieved by NP:

Returns on Rate Base: 1997 to 2002			
Year	**Allowed Rate of Return**	**Allowed Range (%)**[1]	**Actual Return (%)**[2]
1997	10.65	10.50- 10.80	10.71
1998	9.81	9.63 - 9.99	9.86
1999	9.98	9.80- 10.16	10.04
2000	10.28	10.10- 10.46	10.46
2001	10.28	10.10- 10.46	10.46
2002	10.06	9.88- 10.24	9.94

[1] As set out in various Board Orders.
[2] As reported by NP in its annual returns.

Consumer electricity rates were set each year based on the rate of return on rate base, which is the midpoint of the allowed range of return set by the Board, using a 36 basis point spread. The operation of the Formula resulted in adjustments to rates for 2000 and 2002 of less than 1% with rates remaining unchanged in 2001.

One of the conclusions of the Formula review contained in BVP-17 is that the Formula yielded a low return on common equity when compared to similar mechanisms adopted by the NEB and the BCUC.

A significant issue raised during the hearing was the increasing spread between the actual rate of return on rate base and the actual rate of return on regulated equity. This issue was highlighted by Grant Thornton as part of their annual reviews of the operation of the Formula for 2000 and 2001. The following comparison of the actual return on average regulated common equity with the actual return on average rate base for 1998 to forecast 2002 was provided by Grant Thornton (Grant Thornton Report-NP 2003 GRA, pgs. 19-20):

Comparison of Actual Returns on Rate Base and Regulated Common Equity					
	1998	**1999**	**2000**	**2001**	**Forecast 2002**
Return on Average Common Equity	9.58%	9.81%	10.80%	11.35%	10.32%
Return on Average Rate Base	9.86%	10.04%	10.46%	10.46%	9.79%
Spread between actual returns	(0.28%)	(0.23%)	0.34%	0.89%	0.53%
Spread based on formula returns	-	(0.73%)	(0.69%)	(0.69%)	(1.01%)

In its evidence NP describes two events which have affected the returns for 2000 and 2001 i.e. the treatment of GEC for income tax purposes and the Aliant pole purchase. Grant Thornton adjusted the returns for the effect of these two events as shown below:

Returns Adjusted for Extraordinary Events per Exhibit BVP-2					
	1998	1999	2000	2001	Forecast 2002
Return on Average Common Equity	9.58%	9.81%	9.92%	8.50%	9.43%
Return on Average Rate Base	9.86%	10.04%	10.07%	9.23%	9.47%

Grant Thornton also prepared an analysis of the impact of changes in the individual components of the Formula. As a result of this analysis two additional areas were identified for further consideration by the Board: (i) changes in forecast versus actual embedded cost of debt; and (ii) changes in forecast versus actual ratio of average invested capital to average rate base.

Before considering the evidence put forward in the hearing regarding proposed changes to the Formula the Board wishes to provide its opinion and findings regarding the effectiveness of the Formula since 1998 and on the continued use of the Formula for setting rates beyond this Decision.

2. Board's View on Continued Use of the Formula

The appropriateness of implementing an automatic adjustment mechanism for resetting the rate of return in years subsequent to a test year to reflect changes in financial benchmarks was considered by the Board in NP's 1998 cost of capital hearing. In Order No. P.U. 16(1998-99) the Board stated the following (pg. 103):

> *"The Board is of the view that there is merit to a formula, in light of the cost of a full cost of capital hearing and the potential savings to consumers which could be realized. The Board also believes that the adoption of an automatic adjustment mechanism will create greater predictability, which will thereby reduce the risk of regulatory uncertainty. In the opinion of the Board, a mechanism to facilitate an annual review at modest costs will be of benefit to the ratepayer and the Company."*

The Board also stated in Order No. P.U. 16(1998-99) that it would call a hearing if circumstances change, so as to render the use of an automatic adjustment formula to be inappropriate, citing specific examples on pg. 104 as follows:

a) deterioration in the financial strength of the Company, resulting in an inappropriately low interest coverage;
b) changes in financial market conditions which would suggest that the formula is not accurately reflecting the appropriate return on equity; and
c) fundamental changes in the business risk of the Company.

The Board has monitored the operation of the Formula as part of its ongoing supervisory role in regulating the utility. Revised values for rate base and invested capital for use in the Formula for each year were reviewed and approved by the Board as part of that year's capital budget hearing. The Board's financial consultants reviewed the operation of the Formula as part of their annual financial reviews of NP. As well NP was required to file quarterly reports with the Board which, in addition to the required annual report, provided information on actual financial performance, both regulated and non-regulated. In Order No. P.U. 36(1998-99) the Board also specified the time period for the setting of rates using the Formula to three consecutive years, after which a full cost of capital hearing would be convened.

As stated in Order No. P.U. 16(1998-99) one of the primary motivations for adopting the Formula was the potential savings to be realized from a regulatory process that does not require frequent cost of capital hearings, which are time consuming and expensive. It was also recognized that the use of a formula may reduce regulatory risk due to the certainty associated with an automatic adjustment mechanism in reflecting changing financial conditions. In the Board's view the use of the Formula has contributed to stable rates for consumers and lower regulatory costs since 1998. Rate changes due to the operation of the Formula have been +0.71% in January 2000, no change in January 2001 and a decrease of 0.56% in 2002. Many of the issues raised during this hearing relating to NP's earnings and the impact of extraordinary events on those earnings do not relate to the operation of the Formula and are discussed elsewhere in this Decision. None of the parties advocated abandoning the Formula but rather proposed specific changes to the Formula on a go forward basis.

In the Board's view there is merit in continued use of a formula for the same reasons as set out in Order No. P.U. 36(1998-99) and stated above. This was the Board's first experience with an automatic adjustment mechanism and, based on the evidence in this hearing, the Board believes that adjustments to the Formula itself and implementation of specific triggers leading to a review of the Formula's components will improve its operation and effectiveness.

3. Changes as Proposed by NP

In this Application NP is proposing three changes to the Formula: 1) change the manner of determining the risk free rate by adopting the method utilized by the National Energy Board (NEB) and the British Columbia Utilities Commission (BCUC); 2) adopt an equity risk premium of 4.75% at a risk free rate of 6%; and 3) expand the range of return on rate base to 50 basis points. These proposals are discussed in detail in the following sections.

i) Risk-Free Rate

NP stated that the calculation of the risk-free rate in the Formula as put in place by the Board is out of step with similar mechanisms currently in use in Canada and that, as a result, "*NP's returns are established by means outside of the mainstream for such mechanisms in use for Canadian utilities*" [Pre-filed Evidence, B. V. Perry, (1st Revision), pg. 47/1-2]. Mr. Perry goes on to state that the short observation period for setting the risk-free rate exposes NP's investors to additional risk.

The risk-free rate used in the existing Formula is based on the actual yields of two series of long-term Government of Canada bonds. The observed average of the daily closing yields for the last five trading days of October and the first five trading days of November for Government of Canada 8% Issue, maturing June 1, 2027 and the 5.75% Issue, maturing June 1, 2029 is used to forecast the risk-free rate for the upcoming year.

NP proposes that the Formula be amended to adopt the NEB and BCUC approach to determining the risk-free rate. The NEB's formula uses a forecast 10-year bond yield as calculated by taking the average of the 3-month and 12-month-out forecasts of 10-year Government of Canada bond yields as set out in the November issue of *Consensus Forecasts* (published by Consensus Economics Inc., London, England). This forecast 10-year bond yield is added to the observed spread between the 10-year and 30-year Government of Canada bond yields for the current year, calculated by averaging the yields published daily in the National Post throughout October of the current year, to provide a forecast risk-free rate for the next year. The BCUC uses the same calculation for the forecast risk-free rate.

NP provided a comparison of the risk-free rate forecasts and actual 30-year Government of Canada bond yields for 1999 to 2002 as outlined below (Written Submissions, NP, Section G, pg. 8):

Comparison of Risk Free Rate Forecasts and Actual 30-Year Government of Canada Bond Yields: 1999-2002 (%)				
Forecasts:	**1999**	**2000**	**2001**	**2002**
Newfoundland	5.49	6.18	5.75	5.50
NEB	5.69	6.12	5.73	5.63
BCUC[1]	5.47	6.04	5.73	5.63
Actual Yields[2]	**5.72**	**5.71**	**5.76**	**5.68**

[1]In 2000 the BCUC adopted a longer observation period to establish the forecast spread between 10 and 30-year bond yields.
[2]Actual yields are the average of Bank of Canada published month end yields for 30-year Government of Canada Bonds for each year.

NP submitted that the table above provides conclusive evidence that the NEB formula has greater predictive accuracy and lower volatility in predicting the risk-free rate than the existing methodology contained in the Formula. Dr. Morin and Ms. McShane agreed with this proposed change, principally because of its relative stability as compared to spot observations of long-term Canada bond yields.

The Consumer Advocate does not support this proposed change, and stated that "*if the Board is to continue with a formula it should continue with the ten trading days' methodology as provided for in P.U. 16 (1998-99)…*" (Final Submission, Consumer Advocate, pg. 28). Dr. Kalymon suggested that the existing formula methodology for calculating the risk-free rate has been more accurate than the NEB's methodology.

As stated previously in this Decision the Board is not convinced that either the NEB or the BCUC model demonstrates sufficiently superior operating characteristics to warrant a change in formula methodology. The Board believes that greater regulatory stability and consistency is encouraged by retaining the existing Formula.

The Board will continue to use the existing methodology in the Formula for calculating the risk-free rate. However, the risk-free rate will now be calculated based on the actual yields of the three most recent series of long-term Government of Canada bonds

during the 10 trading days being monitored as reported in The Globe and Mail under the heading *"Ask Yields"*. The observed average of the daily ask yields for the last five trading days of October and the first five trading days of November for these three most recent issues will be used to forecast the risk-free rate for the upcoming year, in each year of operation of the Formula.

ii) Equity Risk Premium

NP is also proposing that the Formula be amended by establishing, at a risk-free rate of 6.0%, an equity risk premium of 4.75%.

In Order No. P.U. 16(1998-99) the Board determined that the total risk premium (including an allowance of 50 basis points to cover underwriting costs, the risk of dilution of share value and unforeseen circumstances) to be used in the Formula with a risk-free rate of 5.75% was 350 basis points, or 3.50%, to give an ROE of 9.25%.

The Board has determined that a total risk premium of 415 basis points, or 4.15%, is reasonable. This is the value that will be used and adjusted on the same basis as was ordered in Order No. P.U. 36(1998-99) in the application of the Formula.

4. Embedded Cost of Debt

The issue of the variance between the embedded forecast cost of debt used in the Formula and the actual cost of debt was raised by Grant Thornton (Grant Thornton Report-NP 2003 GRA, February 4, 2003, pg. 22). In Order No. P.U. 36(1998-99) the Board fixed the embedded cost of debt for purposes of the Formula at 9.18%. This cost of debt remains constant from year to year. Actual embedded cost of debt for 1999 to 2001 has been below that used in the Formula, ranging from 9.01% in 1999 to 7.79% in 2002. According to Grant Thornton:

> *"The decrease in the embedded cost of debt means that actual interest costs are lower than anticipated in the Formula. Generally speaking, assuming other items are constant, as interest costs decrease earnings increase and vice versa. What this means in terms of the operation of the Formula is that because the cost of debt is set at a higher level than actual, the Company has the opportunity to increase the return on equity while still staying within the limits of rate of return on rate base."*

Grant Thornton suggested the Board consider the significance of variations in the embedded cost of debt and whether the Board should consider modifying the Formula to adjust for forecast changes in the embedded cost of debt annually. In supplementary evidence Grant Thornton suggested that, as an alternative to modifying the cost of debt annually in the Formula, the Board may establish criteria which would trigger a review of the Formula and the cost of capital. This review would be triggered whenever certain variables or returns generated by operation of the Formula vary significantly from expectations. (Supplementary Evidence, Grant Thornton, pg. 3)

The Consumer Advocate submitted that the operation of the Formula unadjusted for the true cost of embedded debt has resulted in additional income of approximately $7,500,000 for NP for the years 2000, 2001 and 2002. This extra income, according to the Consumer Advocate, contributed to NP's over-earning on its equity in each year since the implementation of the Formula. The Consumer Advocate supports the annual adjustment of the forecast embedded cost of debt. (Final Submission, Consumer Advocate, pgs. 36-39)

The Board agrees that the changes in the embedded cost of debt from that set by the Formula for the 1999 test year have contributed in part to the earnings above the ROE used in the Formula. These changes in debt costs are caused by a number of factors, however, including use of more short-term debt by NP to finance its operations, and changes in interest rates. In addressing this issue in the context of the Formula the Board does not wish to put mechanisms in place that would restrict the ability of NP's management to lower costs, including debt costs, between cost of capital hearings. The real issue for the Board is how the benefit of these lower costs is passed on to consumers.

In the Board's view it would be contrary to the purpose of having an automatic adjustment mechanism if, once a formula has been established, the Board were to use variances from forecasts of requirements to adjust various formula components as they change. In implementing a formula the Board must select reasonable and justified test year values based on the evidence. In the Board's view this is consistent with the prospective nature of setting rates. Changes in test year values are expected. The primary concern for the Board is to ensure that the components in the Formula remain appropriate. This was recognized by the Board in Order No. P.U. 36(1998-99).

The Board concludes that a triggering mechanism tied to the overall cost of capital would be more appropriate. This will provide the Board with the opportunity to review not only the components of the Formula but also to examine the reasons for the variances from test year values. If the variances are related to changing financial and market conditions that the Board or parties could not have foreseen or anticipated, an adjustment to the Formula may be appropriate. The Board does not want, however, to discourage NP from continuing to seek efficiencies to lower costs and will focus primarily on those components that remain outside the control of the utility. As an added monitoring mechanism the Board will require NP to provide additional information on changes in the embedded cost of debt as part of its annual returns.

NP will be required to modify the schedule filed as part of its annual return that calculates the embedded cost of debt to identify specifically the causes of variations in the actual embedded cost of debt from the cost forecast for the test year period.

5. Trigger Mechanism for Early Review

From the Board's perspective, a significant indicator that the Formula may not be operating as intended in setting the rate of return on rate base is when NP's actual earned return on regulated equity in a given year is significantly higher than the expected return or cost of equity determined for that year. In this context it is logical that the triggering mechanism for an early review of the Formula be some pre-defined threshold for the observed rate of return on regulated equity. The Board finds that a good reference point for the threshold is the upper limit of the range of return on rate base. The threshold should be higher than the upper limit otherwise a review would be triggered even though the utility did not earn outside the allowed range.

The Board feels that an appropriate trigger point would be when the actual rate of return on regulated equity for any given year is greater than 50 basis points above the cost of equity as determined by the Formula. Where in any year this threshold trigger is exceeded, the Board will require NP to file a report, as part of its annual return, which details the variations in all components of the cost of capital and explains the circumstances or facts leading to such variations. The Board will undertake an immediate review of this information and make an assessment as to the most appropriate course of action which may involve calling for a hearing on cost of capital.

The Board will establish a mechanism tied to the observed rate of return on regulated common equity which may trigger an early review of the Formula and cost of capital. Where the actual rate of return on regulated equity in any intervening year exceeds the cost of equity determined by the Formula by more than 50 basis points, then NP will be required to file a report with the Board in its annual return setting out the circumstances and facts contributing to the difference.

6. Period of Operation

NP set out its position on the period of operation of the Formula in its response to CA-343. NP has proposed that the Formula be used for a further three year period, stating that customer rates should be set for 2003 and 2004 by Order arising from this hearing and the Formula be used to set rates for 2005, 2006 and 2007. This would mean, presumably, that NP would come before the Board no earlier than late 2007 or early 2008 for a cost of capital hearing unless circumstances change such that an earlier hearing is required by the Board or requested by NP.

It is evident from the record that there are several events that will occur in the next 2-3 years that may impact NP's financial position. These were summarized in the final brief of Board Hearing Counsel (pg. 24). The specific impacts of these events on NP cannot be determined at this time, especially those events outside NP's control, such as the outstanding CCRA issue and the outcome of S & P's ratings review. If either of these events has a negative or material impact on NP's financial position the Board anticipates that NP will request an earlier hearing to review its cost of capital. However, the Board is of the opinion that the proposed period of operation of the Formula for a three-year period starting in 2004 (i.e. to set rates for 2005, 2006 and 2007) is reasonable and meets the intended objective of regulatory efficiency and stability. The Board has put in place with this Decision a triggering mechanism which, along with the Board's ongoing monitoring, will provide the opportunity for the Board to convene an early review if deemed necessary.

The Board will approve the use of the Formula, as modified by this Decision, for a further three-year period. Customer rates will be set for 2003 and 2004 by this Decision and Order. The Formula will be used to set the rate of return on rate base, and hence customer rates, for 2005, 2006 and 2007.

AUTOMATIC ADJUSTMENT FORMULA

8. Unless the Board otherwise orders upon application by NP or by the Board of its own motion, the rate of return on rate base for the years 2005, 2006 and 2007 shall be set using the Automatic Adjustment Formula that was established by the Board in Order No. P. U. 36 (1998-99), incorporating the changes set out in this Decision and Order, including:

i. The move to the Asset Rate Base method; and

ii. The use of the three most recent, rather than the two previously specified, series of long-term Government of Canada bonds in determining the risk-free rate.

9. NP shall apply no later than November 30th in each of 2004, 2005 and 2006 for the application of the Automatic Adjustment Formula to the rate of return on rate base and for a revised Schedule of Rates, Tolls and Charges effective January 1 in each year following.

10. NP shall prepare and file with the Board:

i. With its annual return until otherwise directed by the Board, a modified schedule calculating the embedded cost of debt for the reporting year to identify specifically the causes of variations in the actual embedded cost of debt from the cost forecast for the test period; and

ii. With its annual return where in a year the actual rate of return on regulated equity is greater than 50 basis points above the cost of equity as determined by the Formula, a report explaining the circumstances and facts contributing to the difference.

INTER-CORPORATE RELATIONSHIPS AND CHARGES

11. NP shall review and update its operating practices and procedures to reflect the principles governing all inter-corporate transactions as set out in this Decision and Order, and which may be amended by the Board from time to time.

12. NP shall file with the Board:

i. By June 30, 2004 a report addressing its stand-alone status in respect of the corporate credit linkage of NP to Fortis, as detailed by the Board in this Decision and Order.

ii. By March 31, 2004 a report as to its operating practices and procedures relating to any and all inter-corporate transactions, including:

a) An investigation of the utilization of market rates or a suitable proxy markup for executive and management time charges;

P.U. 39(2005)

IN THE MATTER OF the
PUBLIC UTILITIES ACT,
R.S.N. 1990, c. P-47, as amended
(the "*Act*")

AND

IN THE MATTER OF the application (the "Application") by Newfoundland Power Inc. ("Newfoundland Power") for the approval of a schedule of rates, tolls and charges on an interim basis pursuant to the operation of the Automatic Adjustment Formula (the "Formula"), filed pursuant to Sections 70, 75, and 80 of the *Act* and Order No. P. U. 19(2003).

WHEREAS Newfoundland Power is a corporation duly organized and existing under the laws of the Province of Newfoundland and Labrador, is a public utility within the meaning of the *Act*, and is also subject to the provisions of the *Electrical Power Control Act*, *1994*, and

WHEREAS by Order Nos. P.U. 16 (1998-99) and 36 (1998-99), the Board ordered the establishment of the Formula for use in determining Newfoundland Power's rate of return on rate base and in setting customer rates, tolls and charges (collectively, "Customer Rates") in years subsequent to a test year, and

WHEREAS by Order No. P.U. 19 (2003), the Board modified the Formula and ordered (i) that Newfoundland Power's rate of return on rate base and Customer Rates for 2005, 2006 and 2007 be set using the Formula and (ii) that Newfoundland Power shall apply, by no later than November 30th in each of 2004, 2005 and 2006, for the application of the Formula to the rate of return on rate base and for a revised schedule of Customer Rates to become effective January 1 in each year following, and

WHEREAS by Order Nos. P.U. 19(2003) and P.U. 23(2003), the Board approved the establishment of the 2004 test year parameters for use in calculating Newfoundland Power’s rate of return on rate base and Customer Rates, and

WHEREAS by Order No. P.U. 23(2003), the Board approved the definition of the Excess Earnings Account whereby earnings for 2004 and subsequent years in excess of the maximum allowable rate of return on rate base be credited to the Excess Earnings Account, unless otherwise ordered by the Board, and

WHEREAS by Order No. P.U. 16(2005), the Board approved rate stabilization and municipal tax adjustment factors (the “RSA & MTA Factors”) to be included in Customer Rates for the period July 1, 2005 through June 30, 2006, and

WHEREAS on September 29, 2005, Newfoundland Power filed with the Board an application to change its accounting policy related to its method of recognizing revenue and included in the application a proposal for dealing with the resulting unbilled revenue, and

WHEREAS the forecast rate base and the forecast invested capital for 2006 will be determined by the implementation of the pending decision of the Board regarding Newfoundland Power’s application to change its accounting policy, and

WHEREAS on November 16, 2005, Newfoundland Power filed with the Board its calculation of the cost of common equity for 2006 pursuant to the operation of the Formula, which cost of common equity for 2006 is calculated at 8.77%, and

WHEREAS pursuant to the operation of the Formula, the rate of return on rate base using the figures for 2006 included in Newfoundland Power's application to change its accounting policy is 8.54%, which falls within the range of 8.50% to 8.86% approved by the Board in Order No. P.U. 50(2004), and

WHEREAS in accordance with the provisions of Order No. P. U. 36(1998-99), the rate of return on rate base for 2006 will remain at 8.68%, in a range of 8.50% to 8.86%, and

WHEREAS Appendix A to the Application sets out the cost of common equity as calculated using the long Canada bond yields for the period from October 25 to November 7, 2005, and

WHEREAS Appendix B to the Application sets out the calculation of the weighted average cost of capital for 2006 based upon the operation of the Formula; and

WHEREAS Appendix C to the Application sets out the calculation of the rate of return on rate base for 2006 based upon the operation of the Formula, and

WHEREAS the Application of the Formula will result in no change in the existing customer rates approved by the Board in Order No. P. U. 16(2005).