1 2 3 4 5 6 7 8	Q.	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.					
9 10	A.	1.	Introduction				
10 11 12 13			There are three primary reserve mechanisms used by Newfoundland Power. They are the Weather Normalization Reserve, the Purchased Power Unit Cost Variance Reserve and the Rate Stabilization Account.				
14 15 16 17			These mechanisms provide Newfoundland Power a measure of financial stability by smoothing changes in revenues due to abnormal weather patterns and purchased power costs due to changes in normal weather patterns, hydraulic patterns and fuel costs.				
19 20 21			These reserves also provide customers with a level of rate stability and predictability by smoothing out material changes in costs that could impact customer rates.				
22 23 24		2.	Weather Normalization Reserve				
24 25 26 27			Newfoundland Power's Weather Normalization Reserve consists of the following two components:				
27 28 29 30 21			 the Degree Day Normalization Reserve established by the Board in Order No. P.U. 1 (1974) to normalize Newfoundland Power's revenue and purchased power costs for the effects of abnormal weather conditions; and, 				
31 32 33 34 35			 the Hydro Production Equalization Reserve established by the Board in Order No. P.U. 32 (1968) to normalize Newfoundland Power's purchased power costs for variations in Newfoundland Power's hydroelectric production due to stream- flows that are either above or below normal in any given year. 				
 36 37 38 39 40 			The purpose of the Weather Normalization Reserve is to stabilize rates for customers. Newfoundland Power's annual revenue and purchased power expense on its financial statements are reflective of normal weather and normal stream-flows to its hydro plants.				
41 42 43 44 45			The calculations supporting transfers to, or from, the Weather Normalization Reserve are reported each year in Return 14 of the Annual Report to the Board. The Board has issued orders approving the balance in the reserve for each year from 1974 to present.				

2.1 Degree Day Normalization

Table 1 shows the net transfers to and from the Degree Day Normalization Reserve by year for the period 2001 to 2005.

Table 1 Net Transfers (To) From The Degree Day Normalization Reserve (\$000's)								
Year	RevenuePurchased PowerNet AdjustmentNet AdjustmentYearAdjustmentAdjustmentBefore Tax1After Tax2							
2001	5,511	5,470	41	24				
2002	1,556	181	1,375	838				
2003	4,904	5,061	(157)	(99)				
2004	9,140	7,017	2,123	1,380				
2005	2005 10,594 8,363 2,231 1,450							
Total	Total 31,705 26,092 5,613 3,593							

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The data in Table 1 shows that for the period 2001 to 2005, on a pre-tax basis, approximately \$5.6 million was transferred from the Weather Normalization Reserve to offset the effects associated with warmer than normal weather patterns.

¹ Is equal to the revenue adjustment less the purchased power adjustment.

 $^{^2}$ Is equal to the net adjustment less income taxes.

2.2 Hydro Production Equalization

Table 2 shows the net transfers to and from the Hydro Production Equalization Reserve by year for the period 2001 to 2005.

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Table 2						
Net Transfers (To) From The Hydro Production Equalization Reserve (\$000's)						
Year	Net Adjustment Before Tax ³	Net Adjustment After Tax				
2001	1,926	1,136				
2002	296	181				
2003	1,121	706				
2004	(327)	(213)				
2005	(1,079)	(701)				
Total	1,937	1,109				

- 9 Transfers from the reserve (i.e. shown as a positive transfer in Table 2) indicate a 10 year with lower than normal water. Transfers to the reserve (i.e. shown as a
 - year with lower than normal water. Transfers to the reserve (i.e. shown as a negative transfer in Table 2) indicate a year with higher than normal water.
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³ The pre-tax amortization of \$1.7 million per year (2003-2005) of the balance in the Hydro Production Equalization Reserve approved by the Board in Order No. P.U. 19 (2003) has not been included in the transfers reported in Table 2. This is a fixed amortization and is therefore not considered a risk item.

2.3 Summary of Weather Normalization Adjustments

Table 3 shows the net transfers to and from the Weather Normalization Reserve and the return on common equity by year for the period 2001 to 2005.

Table 3Net Transfers (To) FromThe Weather Normalization Reserve AsA Percentage of Return on Equity(\$000's)						
Year	Net Adjustment After Tax	Return on Equity ⁴	Adjustment as a Percentage of Return on Equity ⁵			
2001	1,160	28,862	4.0%			
2002	1,019	28,807	3.5%			
2003	607	29,460	2.1%			
2004	1,167	31,122	3.7%			
2005	749	30,729	2.4%			
	Average		3.1%			

Table 3 shows that adjustments to the Weather Normalization Reserve averaged approximately 3.1% as a percentage of the actual return on equity for the period 2001 to 2005.

3. Rate Stabilization Account (the "RSA")

In Order No. P.U. 34 (1985), the Board approved the establishment of a rate stabilization account for Newfoundland Power. This was in response to the establishment of a rate stabilization plan (the "RSP") by Newfoundland and Labrador Hydro ("Hydro") which enabled Hydro to flow through changes in fuel costs to Newfoundland Power.

Rate adjustments resulting from the operation of the RSA occur on July 1st each year. In addition to the adjustments for fuel resulting from the operation of Hydro's RSP, adjustments are made to the RSA for municipal taxes, excess fuel costs, secondary energy costs and mismatches due to Hydro price changes.

⁴ As shown in Return 1 of the Annual Report to the Board for 2001 to 2005.

⁵ Is calculated as the net adjustment after tax divided by the return on equity.

	The activity by month in the RSA account is reported each year in Return 15 of the Annual Report to the Board.
3.1	Municipal Tax Adjustment (the "MTA")
	In response to dramatic increases in municipal taxes during the mid 1980s, the Board, in Order No. P.U. 17 (1987), approved the use of a municipal tax adjustment to the RSA account to recover differences between municipal taxes billed and municipal taxes paid. Previously, municipal taxes were included as an expense in determining revenue requirement.
	The MTA account includes the costs of municipal property taxes and business taxes levied by all municipalities as well as accruals for municipal revenue taxes.
	The MTA account is credited on a monthly basis using the amounts derived from the municipal tax adjustment included in electrical rates to reflect taxes charged to the Company by municipalities.
3.2	Excess Fuel Costs
	Excess fuel costs are the net costs of fuel and additives used in the Company's thermal plants to generate electricity other than at the request of Hydro. The net cost is equal to the actual cost of fuel and additives, less the cost of purchases from Hydro calculated at the current tail block rate (8.805 cents per kWh).
	Adjustments are completed monthly and are reported on an annual basis in Return 15 of the Annual Report to the Board.
3.3	Secondary Energy Costs
	Secondary energy costs are related to the purchase from Hydro of surplus energy generated by Corner Brook Pulp and Paper. The cost of the surplus energy includes Hydro's cost of purchasing the secondary energy as defined in Order No. P.U. 24(1988) and a firming up charge as provided for in Hydro's rate schedule applicable to Newfoundland Power.
	Secondary energy costs result in savings to Newfoundland Power's customers because the price of the surplus energy is less than the tail block energy charge of purchasing firm energy from Hydro. The amount of the savings is credited to the RSA.
3.4	RSA Shortfall Adjustments
	The RSA shortfall adjustments represent the difference between increases in revenue and increases in purchased power costs resulting from Hydro rate changes. The most

recent adjustment was approved in association with the flow through to Newfoundland Power's customers of Hydro base rate changes effective January 1, 2007.

3.5 Interest Costs

Interest is calculated and applied to the balance in the RSA account on a monthly basis using the most recently approved rate of return on rate base.

3.6 Summary of RSA Adjustments

Table 4 is a summary of the adjustments to the RSA account for the period 2001 to 2005.

Table 4								
Adjustments To The Rate Stabilization Account (\$000's)								
Year	Revenue Billed	Transfer To Hydro	Municipal Taxes	Excess Fuel Costs	Secondary Energy Costs	RSA Shortfall Adj.	Interest Costs	
2001	(8,076.1)	7,779.6	(115.3)	85.3	(0.2)	0.0	(37.9)	
2002	(7,965.8)	8,120.4	(226.6)	272.1	(0.8)	801.3	(35.3)	
2003	(10,937.5)	11,170.2	44.9	111.0	0.0	0.0	55.7	
2004	(22,542.9)	22,912.6	(177.7)	124.4	0.0	1,215.0	85.1	
2005	(41,687.4)	41,441.3	(279.3)	101.9	(0.4)	0.0	158.5	
Total	Total (91,209.7) 91,424.1 (754.0) 694.7 (1.4) 2,016.3 226.1							

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Table 5 shows total adjustments to the Rate Stabilization Account, and the return on common equity by year for the period 2001 to 2005.

Table 5 Adjustments To The Rate Stabilization Account As A Percentage of Return on Equity (\$000's)						
Year	Total Adjustments (after-tax)	Return on Equity ⁶	Adjustment as a Percentage of Return on Equity ⁷			
2001	(215.2)	28,862	(0.7%)			
2002 ⁸	588.8	28,807	2.0%			
2003	279.9	29,460	1.0%			
2004 ⁹	1050.7	31,122	3.4%			
2005	(172.5)	30,729	(0.6%)			
	Average ⁹	1.0%				

Table 5 shows that adjustments to the Rate Stabilization Account averaged approximately 1.0% as a percentage of the actual return on equity for the period 2001 to 2005.

4. Purchased Power Unit Cost Variance Reserve (the "PPUCVR")

The PPUCVR reduces the financial impacts to Newfoundland Power resulting from variations between actual and forecast purchased power costs. The PPUCVR was established as a consequence of the introduction of a demand and energy rate structure for power purchased from Hydro. Order No. P.U. 44 (2004) approved the establishment of the PPUCVR. Order No. P.U. 35 (2005) approved the detailed definition which governs the operation of the account.

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⁶ As shown in Return 1 of the Annual Report to the Board for 2001 to 2005.

⁷ Is calculated as the net adjustment divided by the return on equity.

⁸ Includes pre-tax amounts of \$801,259 in 2002 and \$1,215,000 in 2004 related to the adjustment for the difference in the increase in revenue and the increase in purchased power costs resulting from the 2002 and 2004 Hydro rate changes.

⁹ The average shown is calculated based on the absolute percentages for 2001 to 2005.

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13 14 In principle, when actual purchased power costs¹⁰ exceed forecast purchased power costs¹¹, the PPUCVR is charged with the amount by which the difference exceeds a pre-determined deadband.

In 2005, the purchased power unit cost variance was less than the approved deadband amount of \$588,000; therefore, no adjustment was required.

5. **Aggregate Effects**

Table 7 shows the aggregate of the adjustments for the Weather Normalization Account and the Rate Stabilization Account as a percentage of return on equity for the period 2001 to 2005. There were no adjustments related to the PPUCVR over this period.

	Table 7						
	Adjustments To The Weather Normalization Account and The Rate Stabilization Account As A Percentage of Return on Equity						
		Percentage of					
Year	WNR ¹²	RSA ¹³	Adjustments	Equity	Return on Equity ¹⁴		
2001	1,160.0	(215.2)	944.8	28,862	3.3%		
2002	1,019.0	588.8	1,607.8	28,807	5.6%		
2003	607.0	279.9	886.9	29,460	3.0%		
2004	1,167.0	1050.7	2,217.7	31,122	7.1%		
2005	749.0	(172.5)	576.5	30,729	1.9%		
		4.2%					

17 Table 7 shows that the total adjustments to the Weather Normalization Reserve and 18 the Rate Stabilization Account for the period 2001 to 2005 averaged approximately

4.2% of the return on equity for the period.

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¹⁰ Annual purchased power cost after normalization and defined on a unit cost basis.

¹¹ Forecast purchased power costs as defined on a unit cost basis.

¹² WNR is the Weather Normalization Reserve. A positive number indicates an increase in the amount due from customers.

¹³ RSA is the Rate Stabilization Account. A positive adjustment indicates an increase in the amount to be collected from customers on July 1 of the following year.

¹⁴ Is calculated as total adjustments divided by the return on equity.