Q. CA 2.0 NP

Reference: 2006 Accounting Policy Application, para. 15 (i)
Exhibit NP-15, NP Forecast 2006 Financial Results

Preamble: NP proposes that: "the amount of $9,579,000 be recognized in 2006 to satisfy the increased forecast 2006 depreciation expense described in paragraph 13 together with appropriate tax effects".

Please confirm that if 2006 costs other than depreciation were forecast to decline (or if revenues were forecast to increase) by enough to fully offset the increase in forecast 2006 depreciation expense plus the 2006 tax effect of the tax settlement (e.g., operating costs decline by $10,036,000), the financial results for "2006 Existing" in Exhibit NP-15 would show a rate of return on rate base of 8.56%.

A. That is not correct. If 2006 costs other than depreciation were forecast to decline (or if revenues from rates were forecast to increase) by $10,036,000, the financial results for "2006 Existing" in Exhibit NP-15 would show a rate of return on rate base of 7.88%. The lower rate of return on rate base is due to the resulting increase in Newfoundland Power's 2006 income tax expense. This is generally described in Section 2.2.3 **Income Tax Effects of the Tax Settlement**.

As noted at page 22 of 34 of the Company Evidence, approximately $15,700,000 in additional cash revenue from customers through rates or reduced operating costs would be required in 2006 to fully offset the impact on Newfoundland Power's return if $10,036,000 in unbilled revenue is not recognized in 2006.[1]

Newfoundland Power's forecast operating costs for 2005 and 2006 are approximately $54 million.[2] These costs are comparable to those used to set rates for 2004. A single year operating cost decline of $15.7 million, or almost 30%, is not a reasonable expectation.

As shown in Exhibit NP-14, Newfoundland Power is forecasting revenue from customer rates to increase from $410,669,000 in 2005 to $417,069,000 in 2006 as a result of forecast load growth. To obtain an additional $15,700,000 in revenue based on the Company's current load forecast would require a 3.8% increase in customer rates for 2006.

[1] See also Exhibit NP-6.
[2] Exhibit NP-14, page 1 of 5, line 11.