

1 Q. CA 32.0 NP

2
3 **Reference: PUB 1.0 NP**
4 **Exhibit NP-14, page 1, Statement of Earnings, 2005 and 2006**
5 **2003 Rate Application, CA-200. Attachment A (1st Revision)**
6

7 **Preamble: NP states: “While cost management was indicated to be a key part of**
8 **the Company’s overall strategy of rate stability, no specific options**
9 **were identified to deal with the anticipated 2006 shortfall at that**
10 **time.”**
11

12 **Please provide a reconciliation between the forecast Income Statement for 2006**
13 **contained in NP’s 2003 Rate Application, CA-200. Attachment A (1st Revision) and**
14 **the forecast Statement of Earnings for 2006 that appears at Exhibit NP-14, page 1**
15 **of the current Application. Please highlight the cost drivers that have resulted in a**
16 **lower rate of return on rate base in the current forecast although contribution is**
17 **almost \$4 million higher and earnings applicable to common shares are more than**
18 **\$3.2 million higher.**
19

20 A. Attachment A provides a reconciliation of the 2006 forecast Income Statement as
21 contained in Newfoundland Power’s 2003 General Rate Application, CA-200 Attachment
22 A 1st Revision (“CA-200”) and the forecast Statement of Earnings for 2006 that appears
23 at Exhibit NP-14, page 1 of the 2006 Accounting Policy Application (“2006 APA”).
24

25 *Return on Rate Base*
26

27 As stated in the Company’s response to CA-200, the forecast provided at that time was
28 subject to change and variation as actuals for each of the forecast years became known,
29 and as assumptions and circumstances changed.
30

31 As shown in Attachment A, line 28, the forecast return on rate base as contained in the
32 2006 APA is approximately \$2.8 million higher than the 2006 forecast return on rate base
33 shown in CA-200. The forecast return on rate base is higher due to the combined effects
34 of the items described in notes 1 through 10 of Attachment A, Page 2 of 2.
35

36 *Average Rate Base*
37

38 As shown in Attachment A, line 29, the 2006 forecast rate base in the 2006 APA is
39 approximately \$88 million higher than the 2006 forecast rate base shown in CA-200.
40 This is due primarily to the Board’s Order No. P.U. 19 (2003), which was issued
41 subsequent to CA-200, approving the inclusion of deferred charges in rate base beginning
42 in 2003. This increase is partly offset by the Company’s currently proposed reduction in
43 the 2006 forecast rate base of \$19.3 million.

The 2006 forecast rate base in CA-200, adjusted to reflect (i) the Board's order to include deferred charges in rate base beginning in 2003 and (ii) the Company's current proposed reduction in 2006 forecast rate base of \$19.3 million would be as shown in Table 1.

Table 1
Pro Forma 2006 Rate Base
(Based on CA-200)

Forecast 2006 Rate Base – CA-200 ¹	\$656,228
Add: Deferred Charges ²	94,561
Less: Currently Proposed 2006 Rate Base Reduction ³	<u>(19,325)</u>
<i>Pro Forma Rate Base – CA-200</i>	<u><i>\$731,464</i></u>

Rate of Return on Rate Base

As shown in line 30 of Attachment A, the 2006 forecast rate of return on rate base for the 2006 APA is 73 basis points lower than the rate of return on rate base in CA-200.

The reason for this variance is

- (i) the inclusion of deferred charges in rate base approved by the Board in Order No. P.U. 19 (2003);
- (ii) the Company's currently proposed reduction in 2006 forecast rate base (as per the 2006 APA); and
- (iii) the higher forecast return on rate base referred to above.

The forecast rate of return on rate base in CA-200, adjusted to reflect these 3 items would be as shown in Table 2.

¹ From CA-200. Attachment A, 1st Revision, page 7 of 10.

² Calculated from CA-200. Attachment A 1st Revision, page 3 of 10.

³ See Exhibit NP-11, line 28.

1

Table 2
***Pro Forma* 2006 Rate of Return on Rate Base**
(Based on CA-200)

<i>Pro Forma</i> Rate Base (as per Table 1 above)	\$731,464
Return on Rate Base ⁴	\$60,958
<i>Pro Forma</i> Rate of Return on Rate Base ⁵	8.33%

2

3

4

The resulting *pro forma* rate of return on rate base represents a more reasonable comparison to the 2006 forecast rate of return on rate base as shown in the 2006 APA.

⁴ See Attachment A, line 28.

⁵ Equals \$60,958/\$731,464.

Newfoundland Power Inc.

Comparison of Forecast 2006 Financial Results
CA-200 to Exhibit NP-14
(000s)

	CA-200	Exhibit NP-14	Difference
1			
2 Billed Revenue	\$ 390,577	\$ 417,069	\$ 26,492 ¹
3 2006 Unbilled Revenue Accrual	-	457	457 ²
4 2005 Unbilled Revenue	-	9,579	9,579 ³
5	390,577	427,105	36,528
6 Purchased Power Expense	232,887	265,498	32,611 ⁴
7 Contribution	157,690	161,607	3,917
8			
9 Other Revenue	9,637	9,950	313 ⁵
10			
11 Other Expenses:			
12 Operating Expenses	54,938	54,153	(785) ⁶
13 Depreciation	38,736	39,079	343 ⁷
14 Finance Charges	33,126	32,637	(489) ⁸
15	126,800	125,869	(931)
16			
17 Income Before Income Taxes	40,527	45,688	5,161
18 Income Taxes	13,420	15,335	1,915 ⁹
19			
20 Net Income	27,107	30,353	3,246
21 Preferred Dividends	613	591	(22) ¹⁰
22			
23 Earnings Applicable			
24 to Common Shares	\$ 26,494	\$ 29,762	\$ 3,268
25			
26			
27 Return on Rate Base			
28 Return on Rate Base	60,958	63,715 ¹⁴	2,757 ¹¹
29 Average Rate Base	656,228	744,326	88,098 ¹²
30 Rate of Return on Rate Base	9.29%	8.56%	-0.73% ¹³

Requests for Information

Notes:

- ¹ The increase in forecast revenue is due to higher than anticipated customer and energy sales growth since CA-200, and a 5.56% flow through rate increase resulting from increased purchased power rates from Hydro approved by the Board in Order No. P.U. 19 (2004). In addition, the following electricity rate changes are reflected in the 2006 APA forecast revenue which were not reflected in CA-200.
- (i) 0.15% reduction in rates effective August 1, 2003 as per Order No. P.U. 23 (2003).
 - (ii) 0.56% reduction in rates effective January 1, 2005 as per Order No. P.U. 50 (2004).
- ² 2006 unbilled revenue accrual as per the 2006 APA which arises from the proposed change to the accrual method of revenue recognition for regulatory purposes beginning in 2006.
- ³ 2005 unbilled revenue accrual as per the 2006 APA which arises from the proposed change to the accrual method of revenue recognition for regulatory purposes beginning in 2006.
- ⁴ Increase in forecast purchased power expense due to (i) a forecast increase in energy sales, (ii) a 5.56% increase in the rate changed to Newfoundland Power by Newfoundland & Labrador Hydro in 2004, as approved by the Board in Order No. P.U. 17 (2004), and (iii) a 3-year demand and energy wholesale rate phase-in approved by the Board in Order No. P.U. 44 (2004).
- ⁵ Increase in Other Revenue due to a forecast increase in customer jobbing revenue.
- ⁶ Operating expenses for 2006 are forecast to be reduced due to cost saving initiatives implemented in 2005, namely:
- (i) 2005 Early Retirement Program
 - (ii) Outsourcing of Cash Services in 2005
 - (iii) eBills initiative
- ⁷ The increase in forecast depreciation expense is due to increased plant investment as compared to CA-200.
- ⁸ The reduction in forecast finance charges is due to lower short-term interest rates. The average short-term interest rate forecast for 2006 in CA-200 was 5.13%. (See CA-200 Attachment A, 1st Revision, page 9 of 10.) The average short-term interest rate forecast in the 2006 APA was 4.00%. (See Exhibit NP-14, page 5 of 5.)
- ⁹ The increase in forecast income taxes is due primarily to income tax effects related to the Tax Settlement in 2005.
- ¹⁰ The reduction in forecast preferred dividends is due to the redemption of preferred shares in 2003, 2004 and 2005 which were not known or anticipated in CA-200.
- ¹¹ The forecast return on rate base is higher due to the combined effects of all items described in notes 1 through 10 above.
- ¹² The increase in average rate base is due primarily to the inclusion of deferred charges in rate base beginning in 2003, as ordered by the Board in Order No. P.U. 19 (2003), partly offset by the \$19.3 million reduction in rate base beginning in 2006 as proposed in the 2006 APA.
- ¹³ Line 28 divided by line 29.
- ¹⁴ For purposes of further comparison, the 2006 Existing Return on Rate Base (before revenue accruals) as shown in Exhibit NP-15 equals approximately \$53.6 million.