Q. If the Board were to determine that the accrued revenue as a result of a change in the revenue recognition policy should be recognized over the two-year period 2006 – 2007, with half being recognized in each year and no other considerations other than tax implications, what effect, giving detailed reasons, would this decision have on the financial and operational plans of NP?

A. Under the scenario proposed (the "Two-Year Scenario"), Newfoundland Power would recognize $12,131,000[1] of the accrued revenue for regulatory purposes in each of 2006 and 2007.

Attachment A provides the Company's forecast 2006 financial results comparing proposals contained in the 2006 Accounting Policy Application to the Two-Year Scenario suggested in this Request for Information.

The comparative impacts are summarized in Table 1.

Table 1
Forecast 2006 Impacts
Newfoundland Power Proposal vs. Two-Year Scenario

	Newfoundland Power Proposal	**Two-Year Scenario**
Rate of Return on Rate Base	8.56%	8.86%
Regulated Rate of Return on Book Equity	9.24%	9.91%
Excess Revenue (000s)	-	$220

Under the Two-Year Scenario, the Company's forecast 2006 rates of return are (i) higher than calculated under the Newfoundland Power proposal and (ii) at the upper end of the range of the currently recognized just and reasonable rates of return.[2] Under the Two-Year Scenario, excess revenue of $220,000 is forecast for 2006.

The Two-Year Scenario would not materially alter the financial and operational plans of the Company from those which would result from the Board's approval of the proposals contained in the 2006 Accounting Policy Application.

The Two-Year Scenario would increase Newfoundland Power's 2006 returns by approximately $2.3 million from those forecast in the 2006 Accounting Policy Application.[3] It would correspondingly reduce the amount of the total accrued revenue available for future benefit of customers.

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1 $24,262,000 ÷ 2 = $12,131,000. See page 4 of Exhibit NP-3 in Newfoundland Power's evidence.

2 The approved rate of return on rate base is currently 8.68%, in a range of 8.50% – 8.86%. The 8.68% rate of return on rate base is based upon a rate of return on common equity of 9.24%.

3 The $2.3 million increase in forecast 2006 return is different from the $2.9 million referred to in the Response to Request for Information PUB 8.0 NP. This is due to differences in the transitional adjustment to rate base for 2006 which results from the Two-Year Scenario and the Full Recognition Scenario. The transitional adjustment is described in the Company Evidence, pp. 24-25.

Newfoundland Power Inc.

2006 Forecast
Newfoundland Power Proposal vs. Two-Year Scenario
(000s)

		Newfoundland Power Proposal[1]	Two-Year Scenario[2]
1			
2			
3	Billed Revenue	$ 417,069	$ 417,069
4	2006 Unbilled Revenue Accrual	457	457
5	2005 Unbilled Revenue Accrual	9,579	11,911
6		427,105	429,437
7	Purchased Power Expense	265,498	265,498
8	Contribution	161,607	163,939
9			
10	Other Revenue	9,950	9,950
11			
12	Other Expenses:		
13	Operating Expenses	54,153	54,153
14	Depreciation	39,079	39,079
15	Finance Charges	32,637	32,637
16		125,869	125,869
17			
18	Income Before Income Taxes	45,688	48,020
19	Income Taxes[3]	15,335	15,335
20			
21	Net Income	30,353	32,685
22	Preferred Dividends	591	591
23			
24	Earnings Applicable		
25	to Common Shares	$ 29,762	$ 32,094
26			
27	Excess Earnings	-	220
28			
29	**Rate of Return Metrics**		
30	Excess Earnings		
31	Regulated Return on Book Equity	9.24%	9.91%
32	Rate of Return on Rate Base[4]	8.56%	8.86%

1 See Exhibit NP-14, Page 1 of 5.

2 Assumes recognition of revenue for regulatory purposes based on the accrual method and all consequential matters as detailed in the 2006 Accounting Policy Application adjusted to reflect the Board's request for information.

3 Income tax expense on the 2005 Unbilled Revenue is determined by the tax settlement. It is therefore unaffected by the amount of 2005 Unbilled Revenue that is recognized for regulatory purposes.

4 In Order No. P.U. 50 (2004), Newfoundland Power's rate of return on rate base, used to set customer rates for 2005, was approved at 8.68% in a range of 8.50% to 8.86%.