

1 **Q. Page 4-43, lines 3-5: Please explain whether or not the forecast credit metrics for**
2 **2016 and 2017 under the existing rates are consistent with the maintenance of the**
3 **continued financial integrity of Newfoundland Power and its ability to attract**
4 **capital on reasonable terms.**

5
6 A. Newfoundland Power does not believe the forecast credit metrics for 2016 and 2017
7 under existing rates are consistent with the maintenance of the continued financial
8 integrity and its ability to attract capital on reasonable terms. The maintenance of
9 Newfoundland Power's creditworthiness and its ability to maintain a sound credit rating
10 is not solely a matter of credit metrics.

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12 *Exhibit 4, in Volume 2, Exhibits & Supporting Materials, shows Newfoundland Power's*
13 *current credit ratings from Moody's and DBRS. As outlined in the Company Evidence,*
14 *Section 4: Finance, Newfoundland Power's credit ratings are influenced by a number of*
15 *factors, including credit metrics, financial metrics such as capital structure, and regulatory*
16 *considerations such as the regulatory framework and the ability to recover costs and earn*
17 *returns.¹*

18
19 Table 4-11 in the *Company Evidence, Section 4: Finance*, shows Newfoundland Power's
20 actual and forecast rates of return on common equity from 2013 to 2017 under current
21 customer rates. Under current customer rates, the rate of return on common equity is
22 forecast to decline from 9.16% in 2013 to 7.22% in 2017. A return on common equity of
23 7.22% is well below current Canadian and U.S. allowed returns for regulated utilities. It
24 is clear from *Exhibit 4* that the credit rating agencies which rate Newfoundland Power
25 consider the existing supportive regulatory environment as a credit strength. If the Board
26 were to allow returns on equity well below current North American norms, there is a risk
27 that the credit rating agencies may take a more negative view on the regulatory
28 environment. This, in turn, would increase the risk to Newfoundland Power's existing
29 credit ratings.

30
31 Table 4-12 in the *Company Evidence, Section 4: Finance*, shows Newfoundland Power's
32 actual and forecast credit metrics from 2013 to 2017 under current customer rates. Under
33 current customer rates, pre-tax interest coverage is forecast to decline from 2.3 times in
34 2013 through 2015 to 2.1 times in 2017. Similarly, cash flow debt coverage is forecast to
35 decline from 20.1% in 2013 to 16.9% in 2017. The erosion of Newfoundland Power's
36 credit metrics increases the risk to existing credit ratings.

¹ See *Volume 1, Company Evidence, Section 4: Finance*, page 4-14 *et seq.* and page 4-41 *et seq.*

1 The *Company Evidence, Section 4: Finance*, outlines how the Board has interpreted the
2 utility entitlement to a just and reasonable return under the *Public Utilities Act* in a
3 manner consistent with the fair return standard. Section 3(a)(iii) of the *Electrical Power*
4 *Control Act, 1994* indicates, in effect, that rates should yield sufficient revenues to enable
5 a utility “...to earn a just and reasonable return as construed under the *Public Utilities Act*
6 so that it is able to achieve and maintain a sound credit rating in the financial markets of
7 the world...”.

8
9 The evidence shows at page 4-19, *et. seq.* that the Board recognizes that the attributes of a
10 fair utility return include that it be (i) commensurate with return on investments of similar
11 risk, (ii) sufficient to ensure financial integrity, and (iii) sufficient to attract necessary
12 capital. A forecast return on common equity of 7.22% simply does not meet the just and
13 reasonable return standard referred to in Section 3(a)(iii) of the *Electrical Power Control*
14 *Act, 1994*.