

1 **Q. In response to CA – NP – 44 NP confirms that it wishes the Board to consider that**
2 **the Automatic Adjustment Formula be discontinued. Please provide a discussion of**
3 **the costs and benefits to consumers over the period from 2010 to 2015 of any**
4 **alternative means of setting rates, such as setting test year rates and allowing them**
5 **to continue until the next General Rate Application.**
6

7 A. The principal benefits to consumers associated with the use of the automatic adjustment
8 formula (“the Formula”) are reduced costs associated with cost of capital hearings and
9 reduced regulatory risk resulting from increased predictability and certainty. The
10 realization of these benefits is based upon the Formula’s accurate reflection of the
11 appropriate return on equity. When it was adopted in 1998, it was recognized that
12 changes in financial market conditions could suggest that the Formula would not
13 accurately reflect the appropriate return on equity. (See Order Nos. P.U. 16 (1998-99) at
14 p.102, *et.seq.*; P.U. 19 (2003), at p. 62 *et.seq.*; and P.U. 32 (2007) at p. 26 *et.seq.*).
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16 The Formula adjusts consumer rates to reflect changes in the forecast cost of equity on an
17 annual basis based upon changes in long-term Canada bond yields. In the absence of the
18 Formula, such adjustments to consumer rates would occur after a hearing into the matter.
19 The Board has the discretion to convene a hearing into Newfoundland Power’s cost of
20 capital whether a formula exists or not. This, in fact, occurred in 1998 when the Board
21 convened such a hearing.
22

23 Maintenance of Newfoundland Power’s financial integrity is central to its ability to
24 deliver least cost, reliable service to customers. To the extent that continued use of the
25 Formula fails to accurately reflect an appropriate return on equity, it presents a risk to the
26 Company’s continued financial integrity.
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28 To the extent that discontinuing use of the Formula results in a greater frequency of
29 examinations of Newfoundland Power’s cost of capital, it could result in additional
30 regulatory costs to consumers.
31

32 Determination of the cost of capital or return is a central issue for both Newfoundland
33 Power and its customers. Changes in financial market conditions suggest that the
34 continued use of the Formula will not accurately reflect an appropriate return on equity.