

1 **Q. 2013-2014 General Rate Application, Company Evidence**

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3 **Pg. 3-15, lines 1-7 and pg. 3-38, lines 11-12 - It is stated that the automatic**  
4 **adjustment formula should be discontinued as it does not accurately estimate the**  
5 **appropriate return on equity under current financial market considerations. Please**  
6 **confirm that it is Newfoundland Power's position that the formula did work**  
7 **properly until the current unsettled financial market conditions arose,**  
8 **approximately 2008, and that the state of the current financial markets, specifically**  
9 **the significant decline in the risk free rate, is the only reason for the proposal to**  
10 **discontinue or abandon the formula.**

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12 **A.** At the time the Board adopted the Formula in 1998 the principal benefits were expected  
13 to be reduced costs resulting from less frequent reviews of cost of capital and reduced  
14 regulatory uncertainty. During the decade ending in 2007, the Formula, for the most part,  
15 appeared to broadly achieve the regulatory objectives described above.

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17 However, since 2008, the Formula has failed to produce either fewer reviews of  
18 Newfoundland Power's cost of capital or reduced regulatory uncertainty. The Formula  
19 has instead produced estimates of Newfoundland Power's cost of equity which have  
20 triggered successive re-examinations of the Company's cost of capital and the operation  
21 of the Formula.

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23 The decline in the risk free rate is only one aspect of the Formula's shortcomings in  
24 current financial markets. Another aspect is the equity risk premium used in the Formula  
25 is insufficient given current financial market conditions.

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27 The Company proposes that the Formula should be discontinued as it does not accurately  
28 estimate the appropriate return on equity under current financial market conditions.