Volume 1, Section 3 – Finance

Q. (Section 3.3.2: Financial Targets, and Exhibit 5, page 3 of 8, and in connection with the Company's outstanding preference shares)

a. The outstanding preference share balance has declined each year from 2002 through 2006; why is it not projected to decline further during 2007 and 2008?

b. What positive role, if any, do the preference shares play in the Company's capital structure?

c. What is (are) the dividend (coupon) rate(s) on these preference shares?

d. Given that the Company considers these preference shares to be a form of "relatively high cost debt capital" (CA-554, NP 2003GRA), does the Company have any flexibility to redeem or repurchase some or all of these shares and, if so, does the Company have the intention to do so in the foreseeable future? If not, why not?

A. (a) The decline in the number of First Preference Shares since 2002 relate to repurchases of Series D and G shares. Newfoundland Power has the limited opportunity to repurchase up to 10,000 Series D and up to 18,000 Series G First Preference Shares each year, at or below par. Typically, the Company has purchased small lots from estates.

As future repurchases are dependent upon whether shareholders wish to sell their shares, further declines in 2007 and 2008 have not been forecast. During the 10 year period 1993-2002, there were six years during which no shares were repurchased.

(b) Preference shares are effectively a form of debt and are treated that way by accounting bodies and credit rating agencies. The role of the Company's First Preference Shares and its other debt instruments serve to finance the Company's rate base, thereby enabling the provision of service to customers.

As the Company is required to maintain a level of common equity in its capital structure that is not in excess of 45% for ratemaking purposes, it must obtain the remaining 55% of its financing requirements through debt. The weighted average cost of debt represented by First Preference Shares is forecast to be 6.27% for 2008. This compares to a weighted average cost of 7.69% for the Company's remaining debt instruments.[1]

[1] See *Volume 1, Exhibit 10* in Newfoundland Power's Application.

(c) The dividend rate on each of the Company's First Preference Share issues are as follows:

Series A	-	5.50%
Series B	-	5.25%
Series D	-	7.25%
Series G	-	7.60%

(d) Details with respect to redemption and repurchase provisions associated with each of the Company's First Preference Share issues are provided in the Company's response to CA-NP-120.

Within the limits set out in the Company's response to part a of this question, Newfoundland Power currently expects that it would repurchase Series D and G First Preference Shares to the extent that the shareholders wished to sell their shares.

The forecast level of preferred equity in the Company's proposed 2008 capital structure is comparable to that approved by the Board for rate setting in Order Nos. P.U. 16 (1998 and 1999) and P.U. 19 (2003). Even if Newfoundland Power forecast to repurchase/redeem all of its First Preference Shares in 2008, its proposed 2008 weighted average cost of capital would not fall below the proposed 8.82% due to the fact that this form of debt represents only 1.15% of the Company's capital structure.

The Company currently does not intend to redeem any of its First Preference Shares.