

1 **Volume 1, Section 1 - Introduction**  
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- 3 **Q. (page 5, line 23 and page 6, lines 1-2) “The Board’s use of regulatory mechanisms**  
4 **has complemented Newfoundland Power’s cost stability and provided for**  
5 **transparent least cost regulation in the circumstances that presented themselves**  
6 **over the past decade”.**
- 7 **a. Please identify the specific characteristics of the regulatory mechanisms that in**  
8 **NP’s view have increased transparency while providing for least cost**  
9 **regulation?**
- 10 **b. How does NP define least cost regulation?**
- 11 **c. Does NP believe that use of a formulaic adjustment mechanism for all of its**  
12 **cost components thus avoiding GRAs would result in least cost regulation?**
- 13 **d. Provide NP’s assessment of the pros and cons of such “regulatory**  
14 **mechanisms” including those practiced in other Canadian jurisdictions.**
- 15 **e. Would a performance-based regulatory mechanism for NP provide a more**  
16 **optimal solution in terms of providing least cost regulation? Why, or why not?**
- 17
- 18 **A. (a)** A description of the regulatory mechanisms currently in use is provided in response  
19 to Request for Information CA-NP-21.

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21 A description of how each mechanism has increased transparency while providing  
22 for least cost regulation is provided below.

23

24 *Automatic Adjustment Formula*

25 The Automatic Adjustment Formula (the “Formula”) reduces regulatory cost and  
26 increases efficiency by reducing regulatory lag. A cost of capital proceeding is not  
27 required to ensure rates reasonably reflect costs every time there is a need to adjust  
28 rates as a result of changing market conditions. The Formula also meets the need of  
29 public transparency as well, because the Formula is understandable. If long-term bond  
30 yields change materially, the Company’s return on equity is adjusted. This approach is  
31 understandable by customers.

32

33 *Excess Earnings Account*

34 The Excess Earnings Account provides customers with certainty that the Company  
35 cannot earn in excess of the upper limit of the allowed range of return on rate base  
36 as determined by the Board. The Excess Earnings Account is transparent largely  
37 because an earnings limit is understandable.

38

39 *Weather Normalization Reserve*

40 The purpose of the Weather Normalization Reserve is to stabilize rates for  
41 customers and earnings for the Company. The reserve avoids the requirement for  
42 regulatory proceedings by removing the earnings volatility related to the effects of  
43 abnormal weather and hydrology. The removal of weather and hydrology effects in  
44 financial results and financial forecasts is understandable.

1 The reserve is viewed as strength in regulation by the rating agencies in determining  
2 Newfoundland Power's creditworthiness. Maintaining Newfoundland Power's  
3 creditworthiness is consistent with the provision of service to customers on a least cost  
4 basis.

5  
6 *Rate Stabilization Account*

7 The primary purpose of the Rate Stabilization Account (the "RSA") is to permit the  
8 Company to flow-through to customers the fluctuations between the estimated and  
9 actual charges from Hydro for the cost of fuel generated at Holyrood.

10  
11 The RSA avoids regulatory proceedings to deal with fuel cost variations which both  
12 reduce cost and regulatory lag to customers. The adjustment to rates that occurs on  
13 July 1<sup>st</sup> of each year to reflect the actual cost of fuel during the year is a concept that  
14 is understandable by customers.

15  
16 This RSA is also viewed as strength in regulation by the rating agencies in  
17 determining Newfoundland Power's creditworthiness. Maintaining Newfoundland  
18 Power's creditworthiness is consistent with the provision of service to customers on a  
19 least cost basis.

20  
21 *Purchased Power Unit Cost Variance Reserve*

22 The Purchased Power Unit Cost Variance Reserve (the PPUCVR) provides an  
23 incentive to the Company to undertake reasonable initiatives to minimize peak  
24 demand. Providing an incentive to the utility to reduce peak demand on the system  
25 to potentially avoid future system expansion is understandable to customers.  
26 Savings that result from such initiatives are consistent with the provision of least  
27 cost service to customers.

- 28  
29 (b) Least cost regulation should provide efficient processes to effectively provide for:  
30 (i) the recovery of the reasonable cost to serve, (ii) the approval of the capital  
31 investments required to provide safe and adequate service to its customers, and (iii)  
32 the establishment of rates consistent with generally accepted ratemaking principles.
- 33  
34 (c) Newfoundland Power does not believe that avoiding general rate proceedings by the  
35 use of a formulaic adjustment mechanism for *all* of cost components would  
36 necessarily result in least cost regulation. Periodic rate reviews are necessary to  
37 ensure the reasonable long-term balancing of costs and rates.
- 38  
39 (d) Newfoundland Power has not conducted a comprehensive review of the regulatory  
40 mechanisms in other Canadian jurisdictions. Therefore, the Company is not  
41 currently in a position to provide an informed assessment on the pros and cons of  
42 the regulatory mechanisms used in other jurisdictions.
- 43

- 1           (e) Whether least cost regulation would be provided by a performance-based regulatory  
2           mechanism for Newfoundland Power would, in Newfoundland Power's view,  
3           depend on the regulatory mechanism put in place.