

1 **Q. Newfoundland Power Inc. (NP) applied, in the General Rate Application filed**
2 **October 11, 2002, for approval “to amortize over a 3 year period an accumulated**
3 **reserve variance of \$17.2 million identified in the Depreciation Study filed with the**
4 **Application” while also requesting that 2003 and 2004 be treated as test years and**
5 **that the Automatic Adjustment Formula be applied to years 2005 to 2007. Based on**
6 **the above, NP must have been considering options available to deal with the shortfall**
7 **in revenue requirement in the 2006 and 2007 years. Please outline what options**
8 **were considered at the time.**

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10 A. In the General Rate Application filed October 11, 2002, (the “2003 GRA”),
11 Newfoundland Power applied for approval to (i) amortize an accumulated reserve
12 variance of \$17.2 million over the period 2003 through 2005 (the “Depreciation True-
13 up”) and (ii) continue the use of an automatic adjustment formula (the “Formula”)
14 through 2007.

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16 Both the proposal concerning the Depreciation True-up and use of the Formula provided
17 benefits to Newfoundland Power’s customers. The Depreciation True-up reduced
18 revenue required from customers’ rates from 2003 through 2005. The Formula ensured
19 that changes in Newfoundland Power’s cost of equity are reflected annually in
20 customers’ rates without the expense of a cost of capital hearing.

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22 At the hearing of the 2003 GRA, it was recognized that termination of the Depreciation
23 True-up in 2006 would create a shortfall. While cost management was indicated to be a
24 key part of the Company’s overall strategy of rate stability, no specific options were
25 identified to deal with the anticipated 2006 shortfall at that time.¹

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27 During the 2003 GRA hearing it was also recognized that the Board’s approval of the use
28 of the Formula did not preclude the Company from requesting relief depending on
29 prevailing circumstances at any time. The purpose of the Formula is to ensure that
30 changes in the cost of equity (as opposed to all costs) are reflected annually in customers’
31 rates. Newfoundland Power is not proposing any changes to the normal functioning of
32 the Formula in the 2006 Accounting Policy Application.

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34 Since the hearing of the 2003 GRA, Newfoundland Power has been able to resolve the
35 longstanding dispute between it and the Canada Revenue Agency. The resolution of this
36 dispute in June 2005 has provided an effective option for dealing with the 2006 shortfall
37 identified in the 2003 GRA, without a GRA and without impacting customer rates.

¹ This issue was the subject of cross-examination of Newfoundland Power’s Vice-President, Finance and Chief Financial Officer, see: Transcript, March 13, 2003, pp. 153, *et seq.*