Q. What is the annual impact on Newfoundland Power Inc.'s retail rates resulting from the proposed capital expenditures in the 2007 Capital Budget (other than the Rattling Brook Refurbishment) for the years 2007 through 2016?

A. The annual impact on retail rates of the proposed capital expenditures for the years 2007 through 2016 will be determined in Newfoundland Power's general rate proceedings which establish rates through this period. Therefore, the impact on retail rates requested cannot be determined at this time. While the actual future retail rate impacts cannot be determined, *pro forma* estimates of revenue requirement impacts might be of some use.

The proposed capital expenditure in the 2007 Capital Budget other than the Rattling Brook Refurbishment amounts to $43,346,000.[1] This capital expenditure will tend to increase the Company's cost of capital (return on rate base), depreciation and income tax cost in each year over the life of each asset.

Table 1 provides the *pro forma* revenue requirement for each year over the period 2007 to 2016 associated with $43,346,000 in capital expenditure in 2007. The table also provides the *pro forma* revenue requirement expressed as a percentage of estimated 2007 customer billings[2] ($501,550,000). The percentage ranges up to 1.1% over the 2007 to 2016 period and declines thereafter as the depreciated value of the plant declines over time.

Table 1
***Pro Forma* Revenue Requirement Impact**
2007-2016

Year	Revenue Requirement ($)	Percentage of 2007 Customer Billing
2007	482,000	0.1%
2008	4,844,000	1.0%
2009	5,538,000	1.1%
2010	5,531,000	1.1%
2011	5,473,000	1.1%
2012	4,919,000	0.9%
2013	4,602,000	0.9%
2014	4,508,000	0.9%
2015	4,410,000	0.9%
2016	4,308,000	0.9%

[1] $62,166,000 – $18,820,000 = $43,346,000
[2] Forecast Billings to Customers including the Rate Stabilization Adjustment and Municipal Tax Adjustment.

Table 1 only includes the *pro forma* impact of the capital expenditures on return on rate base, depreciation and income taxes. While these impacts tend to put upward pressure on retail rates, they do not capture the total effects on retail rates of capital expenditures. Capital expenditures impact operating costs. Through replacement of deteriorated plant, the cost of making emergency repairs due to equipment failure is reduced. In addition, many capital expenditures enable efficiencies through technology. These types of effects tend to mitigate the upward *pro forma* impacts set out in Table 1.

Retail rates are designed to recover the Company's *total* revenue requirement. The total revenue requirement includes costs other than those associated with capital investment. In addition, changes in sales volumes affect the relationship between costs and retail rates. Consequently, the increase in *pro forma* revenue requirement impacts shown in Table 1 is not necessarily indicative of an equivalent, or any, increase in retail rates.

The Company's capital expenditures since 1996 have totalled $490 million dollars. If the impact of increases in purchased power costs is excluded, the net impact on retail rates of changes in Newfoundland Power's revenue requirement over that same period has essentially been flat.