

1 **Q. Please restate Exhibit 8 using the assumption that the Company's allowed return on equity**
2 **in 2013, 2014 and 2015 is:**

3
4 **(a) 2.5% lower than assumed in Exhibit 8;**

5
6 **(b) 2% lower than assumed in Exhibit 8;**

7
8 **(c) 1.5% lower than assumed in Exhibit 8;**

9
10 **(d) 1.0% lower than assumed in Exhibit 8.**

11
12 **A.** Exhibit 8 shows the *pro forma* revenue requirement impacts on the Company of the sale
13 of 40% of Joint Use Support Structures and the 2011 Joint Use Agreement (the "2011
14 JUA"), as compared with a renewal of the 2001 Joint Use Facilities Partnership
15 Agreement ("JUFPA") to reflect current financial parameters.¹ The allowed return on
16 equity ("ROE") was 8.38% as approved in Order No. P.U. 32 (2010).

17
18 The scenarios requested in the question above focus only on the impact on the net present
19 value analysis if the allowed ROE decreases relative to 8.38%. This 8.38% allowed ROE
20 appears to be the lowest used in setting 2011 rates for electric utilities in Canada.² This
21 ROE is the lowest used to set Newfoundland Power's customer rates in over 3 decades.

22
23 Given the relatively low current allowed ROE for Newfoundland Power, the Company
24 has provided restatements of Exhibit 8 with both allowed ROEs lower than 8.38% and
25 higher than 8.38%. This will show the effects of changes in Newfoundland Power's
26 allowed ROEs in 2013 through 2015 upon *pro forma* revenue requirements in a
27 symmetrical fashion.

28
29 Attachment A provides a restatement of Exhibit 8 using the following 8 ROE scenarios
30 relative to the 8.38% assumed in Exhibit 8: $\pm 2.5\%$; $\pm 2\%$; $\pm 1.5\%$; and $\pm 1\%$.

¹ The primary financial parameters include current embedded costs of Support Structures and current cost of capital. The JUFPA was based upon 2000 embedded costs of Support Structures and 2001 cost of capital.

² Allowed 2011 ROEs for Canadian electric utilities are typically 1% to 1.5% higher than Newfoundland Power's 2011 allowed ROE. Current allowed ROEs include 9.75% in P.E.I. (Maritime Electric), 9.35% in Nova Scotia (Nova Scotia Power), 9.66% in Ontario (Hydro One), 9.0% in Alberta (All) and 9.9% in B.C. (FortisBC). Allowed 2011 ROEs for Alberta are currently under review.

Table 1 provides a summary of the levelized revenue requirement and the net present value (“NPV”) of the surplus (deficiency) for the 5 year period for each ROE scenario.

Table 1
Summary of Impacts of ROE Variability on Exhibit 8

ROE Scenario		Allowed ROE (%)	Levelized Revenue Requirement (\$000s)	NPV of Surplus (Deficiency) (\$000s)
1.	2.5% Lower	5.88	(345)	(1,445)
2.	2.0% Lower	6.38	(253)	(1,052)
3.	1.5% Lower	6.88	(160)	(661)
4.	1.0% Lower	7.38	(66)	(272)
Base	Exhibit 8	8.38	123	497
5.	1.0% Higher	9.38	315	1,256
6.	1.5% Higher	9.88	413	1,632
7.	2.0% Higher	10.38	511	2,006
8.	2.5% Higher	10.88	610	2,377

Table 1 indicates that a reduction in the allowed ROE in 2013 through 2015 reduces the NPV from the sale of the Joint Use Support Structures. An increase in the allowed ROE for the same period increases the NPV from the sale of the Joint Use Support Structures. This primarily reflects a simple dynamic. Cost savings associated with reduced returns on rate base (or cost of capital) resulting from the sale of Joint Use Support Structures will be *lower* at lower allowed ROEs. This will serve to reduce forecast customer benefits. Conversely, cost savings associated with reduced returns on rate base (or cost of capital) resulting from the sale of Joint Use Support Structures will be *higher* at higher allowed ROEs. This will serve to increase forecast customer benefits.

All of the assumptions referred to in this question assume an allowed ROE for Newfoundland Power which is lower than the Company’s embedded cost of debt.³ All of the assumptions referred to in this question assume an allowed ROE for Newfoundland Power which is materially lower than the Company’s current allowed ROE, which is at a historically low level. This question further assumes that future allowed ROEs for Newfoundland Power will be materially lower than those currently allowed for either Newfoundland Power or other electric utilities in Canada.

³ Newfoundland Power’s 2010 embedded cost of debt was 7.63% [see Return 25, line 20 of Newfoundland Power’s 2010 Annual Report to the Board of Commissioners of Public Utilities filed pursuant to ss. 59(2) of the *Public Utilities Act*]. This implies that debtholders are entitled to a higher return than common shareholders.

1 Given the foregoing, the assumptions referred to in this question are not, in the
2 Company's view, realistic. Newfoundland Power observes, however, that an increase in
3 allowed ROE of 1% to 9.38% for 2013 through 2015 more than doubles the additional
4 benefits associated with the sale of 40% of the Joint Use Support Structures and the 2011
5 JUA. In the Company's view, this is indicative of, amongst other things, the conservative
6 assessment of customer benefits contained in Exhibit 8.⁴

⁴ For information on further *potential* benefits associated with the new Joint Use regime, please refer to the Response to Request for Information PUB-NP-35.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 5.88% (-2.5%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(2,876,684)	(2,935,225)	(2,996,267)
Income Taxes ⁴	(405,268)	(699,771)	(499,760)	(509,930)	(520,535)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(6,557,023)	(6,733,240)	(6,915,536)
Surplus (Deficiency)	918,976	156,699	(906,362)	(904,498)	(893,837)
Levelized Revenue Requirement⁶	(344,540)				
Net Present Value of Surplus (Deficiency)⁷	(1,445,125)				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **6.22%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 6.38% (-2.0%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(2,980,728)	(3,041,386)	(3,104,635)
Income Taxes ⁴	(405,268)	(699,771)	(542,257)	(553,292)	(564,798)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(6,703,564)	(6,882,763)	(7,068,167)
Surplus (Deficiency)	918,976	156,699	(759,821)	(754,975)	(741,206)
Levelized Revenue Requirement⁶	(252,584)				
Net Present Value of Surplus (Deficiency)⁷	(1,051,644)				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **6.45%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 6.88% (-1.5%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(3,084,771)	(3,147,546)	(3,213,003)
Income Taxes ⁴	(405,268)	(699,771)	(584,753)	(596,653)	(609,061)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(6,850,103)	(7,032,284)	(7,220,798)
Surplus (Deficiency)	918,976	156,699	(613,282)	(605,454)	(588,575)
Levelized Revenue Requirement⁶	(159,869)				
Net Present Value of Surplus (Deficiency)⁷	(660,741)				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **6.67%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 7.38% (-1.0%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(3,188,814)	(3,253,707)	(3,321,372)
Income Taxes ⁴	(405,268)	(699,771)	(627,250)	(640,014)	(653,324)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(6,996,643)	(7,181,806)	(7,373,430)
Surplus (Deficiency)	918,976	156,699	(466,742)	(455,932)	(435,943)
Levelized Revenue Requirement⁶	(66,387)				
Net Present Value of Surplus (Deficiency)⁷	(272,371)				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **6.90%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 9.38% (+1.0%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(3,604,988)	(3,678,350)	(3,754,846)
Income Taxes ⁴	(405,268)	(699,771)	(797,236)	(813,460)	(830,377)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(7,582,803)	(7,779,895)	(7,983,957)
Surplus (Deficiency)	918,976	156,699	119,418	142,157	174,584
Levelized Revenue Requirement⁶	315,250				
Net Present Value of Surplus (Deficiency)⁷	1,256,226				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **7.80%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 9.88% (+1.5%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(3,709,031)	(3,784,510)	(3,863,214)
Income Taxes ⁴	(405,268)	(699,771)	(839,733)	(856,821)	(874,640)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(7,729,343)	(7,929,416)	(8,136,588)
Surplus (Deficiency)	918,976	156,699	265,958	291,678	327,215
Levelized Revenue Requirement⁶	412,601				
Net Present Value of Surplus (Deficiency)⁷	1,632,288				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **8.02%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 10.38% (+2.0%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(3,813,075)	(3,890,671)	(3,971,582)
Income Taxes ⁴	(405,268)	(699,771)	(882,229)	(900,183)	(918,903)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(7,875,883)	(8,078,939)	(8,289,219)
Surplus (Deficiency)	918,976	156,699	412,498	441,201	479,846
Levelized Revenue Requirement⁶	510,735				
Net Present Value of Surplus (Deficiency)⁷	2,005,967				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **8.25%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.

Joint Use Regime Effective 2011
Pro forma Revenue Requirement Analysis
Cost of Equity of 10.88% (+2.5%)
2011-2015
(\$)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Incremental Revenues¹	(3,295,995)	(6,173,074)	(7,463,385)	(7,637,738)	(7,809,373)
Incremental Costs					
Depreciation Expense ²	(2,494,753)	(2,581,966)	(2,673,539)	(2,771,391)	(2,873,158)
Cost of Capital ³	(1,314,950)	(2,650,264)	(3,917,118)	(3,996,832)	(4,079,951)
Income Taxes ⁴	(405,268)	(699,771)	(924,726)	(943,544)	(963,166)
Operating Expenses ⁵	-	(397,772)	(507,040)	(516,694)	(525,576)
Total Incremental Costs	(4,214,971)	(6,329,773)	(8,022,423)	(8,228,461)	(8,441,851)
Surplus (Deficiency)	918,976	156,699	559,038	590,723	632,478
Levelized Revenue Requirement⁶	609,655				
Net Present Value of Surplus (Deficiency)⁷	2,377,288				

Notes:

¹ The forecast reduction in incremental revenues includes reductions in attachment rental revenues for 2011-2015, offset in 2011 and 2012 by recoveries from Bell Aliant in those years.

² The forecast reduction in depreciation reflects the sale of Joint Use Support Structures in 2011 and an annual reduction in pole installation costs for 2011 to 2015. The composite depreciation rate for distribution assets is 3.14%.

³ The forecast reduction in cost of capital is based on a capital structure of 55% debt/45% equity and assumes an incremental cost of capital of 5.83% in 2011 and 2012, and **8.47%** thereafter. The sale of Joint Use Support Structures will reduce Newfoundland Power's average rate base by approximately \$46 million.

⁴ The forecast reduction in income taxes primarily reflects the reduction in the cost of capital.

⁵ The forecast reduction in incremental operating costs includes increased Joint Use administration costs of approximately \$100,000 per year beginning in 2012; approximately \$200,000 operating cost savings per year commencing in 2013 as a result of the 2011 JUA (50% of which is forecast to be realized in 2012); as well as decreased vegetation management costs related to distribution poles of approximately \$400,000 per year.

⁶ This is the levelization of the annual revenue surplus (deficiency) from 2011 to 2015.

⁷ This is the net present value of the annual surplus (deficiency) from 2011 to 2015.