

Board of Commissioners of Public Utilities
Financial Consultants Report
Newfoundland Power Inc.
2008 Capital Budget Application
August 16, 2007

Grant Thornton 

August 16, 2007

Board of Commissioners of Public Utilities
120 Torbay Road
Prince Charles Building
St. John's, NL A1A 5B2

Attention: Ms. Doreen Dray

Dear Ms. Dray:

**Re: Newfoundland Power Inc.
2008 Capital Budget Application**

We have completed our review as requested in your letter dated July 25, 2007 relating to Newfoundland Power Inc.'s (the Company's) 2008 Capital Budget Application as it pertains to the calculation of the 2006 actual average rate base and the calculations of the 2007 and 2008 forecast deferred charges.

The results of our review for each required task are noted below:

2006 Average Rate Base Calculation

The actual average rate base for 2006 as calculated by the Company and provided in Schedule E of its Application is \$752,917,000 compared to \$745,446,000 for 2005. The increase of \$7,471,000 in 2006 is primarily due to an increase in net plant investment of \$20,079,000 resulting from additions during the year and an increase in average deferred charges of \$8,275,000. These increases were partially offset by the reduction in the average rate base for the unrecognized 2005 unbilled revenue balance of \$21,396,000 as required under P.U. 40 (2005) as well as the net transfer to the Purchased Power Unit Cost Variance Reserve of \$1,342,000 as required under P.U. 44 (2004). This calculation agrees with the information submitted to the Board in Return 3 of the Company's 2006 annual report.

Our procedures with respect to verifying the calculation of the average rate base were directed towards the verification of the data incorporated in the calculations and the methodology used by the Company. Specifically, the procedures which we performed included the following:

- agreed all carry-forward data to supporting documentation including audited financial statements and internal accounting records, where applicable;
- agreed component data (capital expenditures; depreciation; etc.) to supporting documentation;
- checked the clerical accuracy of the continuity of the rate base for 2006; and

.../pg. 2

Board of Commissioners of Public Utilities
page two...

- agreed the methodology used in the calculation of the average rate base to the Public Utilities Act to ensure it is in accordance with Board Orders and established policy and procedure.

Based upon the results of the above procedures we did not note any discrepancies in the calculation of the 2006 average rate base, and therefore conclude that the average rate base included in Schedule E of the Company's application is accurate and in accordance with P.U. 19 (2003), P.U. 44 (2004) and P.U. 40 (2005).

Forecast Deferred Charges

In compliance with P.U. 19 (2003), Newfoundland Power Inc. has filed evidence with the Board relating to its forecast deferred charges, including pension costs, to be included in the calculation of the forecast average rate base for 2007 and 2008.

We confirm that, as indicated by the Company, the actual deferred charges for 2006 of \$111,207,000 are higher than the forecast of \$108,608,000 that was filed in the Company's prior year Capital Budget Application. The increase of \$2,599,000 is primarily due to an increase in the Weather Normalization Account of \$2,810,000. The forecast balance assumed normal stream-flows and weather patterns for the majority of 2006, while the actual balance has been updated for actual stream-flows and weather patterns. The balance in this account agrees with the information submitted to the Board in Return 14 of the Company's 2006 annual report and approved by the Board under P.U. 12 (2007). The increase in the Weather Normalization Account was partially offset by a decrease of \$211,000 in deferred pension costs.

The 2006 balance for the remaining deferred charges accounts agree with the information submitted to the Board in Return 8 of the Company's 2006 annual report.

Forecast deferred charges for 2008 do not include the possible adjustments required for any of the Company's proposals with respect to deferred charges in its 2008 General Rate Application ("GRA"). In the 2008 GRA, the Company has requested approval for a number of changes which, if approved, will impact the 2008 forecast deferred charges balance. However, these issues will be dealt with in the GRA.

Board of Commissioners of Public Utilities
page three...

The deferred charges for forecast 2007 and 2008 as presented by the Company are as follows:

(\$000's)	Forecast 2006	Actual 2006	Forecast 2007	Forecast 2008
Deferred Pension Cost	\$ 90,333	\$ 90,122	\$ 96,656	\$ 99,764
Weather Normalization Account	8,998	11,808	10,683	10,683
Unamortized Debt Discount & Issue Expense	3,035	3,035	3,433	3,245
Unamortized Capital Stock Issue Expense	199	199	137	75
Deferred Retiring Allowances	134	133	-	-
Deferred Credit Facility Issue Costs	116	117	58	-
Deferred Depreciation Expense	5,793	5,793	11,586	11,586
Deferred Replacement Energy Cost	-	-	1,147	1,147
Total Deferred Charges	\$ 108,608	\$ 111,207	\$ 123,700	\$ 126,500

Source: Newfoundland Power Inc. - 2008 Capital Budget Application
Report on Deferred Charges and Rate Base - Table 1

Our comments with respect to the deferred charges are noted below:

Deferred Pension Costs

Deferred pension costs is the most significant component of the deferred charges and is the result of the pension funding exceeding the pension expense as determined in accordance with the recommendations of the Canadian Institute of Chartered Accountants (CICA).

According to the table below, the forecast pension plan funding for 2007 and 2008 is \$10,906,000 and \$5,418,000 and the forecast pension plan expense is \$4,372,000 and \$2,310,000 for 2007 and 2008 respectively. The difference between the funding and the expense as indicated below represents the increase in deferred pension costs forecast for 2007 and 2008.

Board of Commissioners of Public Utilities
page four...

(\$000's)	Forecast 2006	Actual 2006	Forecast 2007	Forecast 2008
Deferred Pension Costs, January 1	\$ 84,999	\$ 84,999	\$ 90,122	\$ 96,656
Pension Plan Funding				
- Current Service Funding	3,200	3,371	3,598	3,840
- Special Funding	7,391	7,540	7,308	1,578
Total Pension Plan Funding	10,591	10,911	10,906	5,418
Pension Plan Expense	(5,257)	(5,788)	(4,372)	(2,310)
Increase in Deferred Pension Costs	5,334	5,123	6,534	3,108
Deferred Pension Costs, December 31	\$ 90,333	\$ 90,122	\$ 96,656	\$ 99,764

Source: Newfoundland Power Inc. - 2008 Capital Budget Application
Report on Deferred Charges and Rate Base - Table 2

With regards to the pension plan funding for 2007 and 2008, we have reviewed this amount and agreed it to supporting documentation where appropriate. The 2007 and 2008 forecast current service funding is reasonable in comparison to 2006. The special funding consists of two components; a special funding requirement as determined by previous Board Orders and Letters of Approval; and special funding as determined by the Company's actuary in accordance with pension guidelines. The decrease in special funding in 2008 is due to the Company's past service obligations being fully funded.

The forecast pension expense for 2007 and 2008 is \$4,372,000 and \$2,310,000 respectively compared to an actual expense in 2006 of \$5,788,000. According to the Company, the primary reason for the decrease forecast for 2007 and 2008 is that the actuarial report filed with the 2008 GRA predicts that the defined benefit plan's past service obligations will be fully funded in 2008. This results in an increase in plan assets which increases returns resulting in a net decrease in pension expense. Based on our review of information provided by the Company, the forecast pension expense is calculated in accordance with the recommendations of the CICA and relevant Board Orders, and is determined in a manner consistent with prior years and Board Orders.

It is important to note that the final pension expense for 2008 cannot be determined until after December 31, 2007. In accordance with CICA recommendations, the 2008 expense will be determined based on the market value of pension plan assets as of December 31, 2007, and as well the discount rate that is required to be used in the calculation will be the actual market rate of interest at December 31, 2007.

Based on our review of forecast deferred pension costs, we confirm that we have not noted any discrepancies or unusual items. The information filed by the Company is consistent with prior years.

Board of Commissioners of Public Utilities
page five...

Weather Normalization Reserve

The changes in the forecast weather normalization reserve for 2007 reflects the amortization of the \$5.6 million non-reversing balance in the Hydro Production Normalization Reserve over a period of five years (\$1.126 million annually) as approved in P.U. 19 (2003). This balance will be fully amortized as of December 31, 2007. The 2007 and 2008 forecasts assume normal weather conditions from January 2007 through December 2008.

Based on our review of the forecast weather normalization reserve, we confirm that we have not noted any discrepancies or unusual items. The information filed by the Company is consistent with prior years.

Unamortized Debt Discount and Issue Expense

The increase in Unamortized Debt Discount and Issue Expense forecast for 2007 is due to the anticipated issue of Series AL First Mortgage Sinking Fund Bonds in August, 2007. At the time this Application was submitted, the Company anticipated issuing \$60 million in bonds with forecast issue cost equal to 1% of the face value (\$600,000). In July, 2007 the Board approved, under P.U. 24 (2007), the issue of up to \$75,000,000 Series AL First Mortgage Sinking Fund Bonds to be issued on or before December 31, 2007. The difference between the forecast Issue and the approved Issue will not have a significant impact on the balance included in Unamortized Debt Discount and Issue Expense.

Unamortized Capital Stock Issue Expense

The forecast decrease in this account represents the normal amortization of these costs.

Deferred Retiring Allowance

The deferred retiring allowance relates to the amortization of retiring allowances associated with the 2005 Early Retirement Program per P.U.49 (2004). This balance will be fully amortized in 2007.

Based on our review of forecast deferred retirement allowances, we confirm that we have not noted any discrepancies or unusual items, and the calculation of the allowance is consistent with approved Board Orders.

Deferred Credit Facility Issue Costs

The forecast decrease in this account represents the normal amortization of these costs.

Deferred Depreciation Expense

The deferral of depreciation expense relates to the increase in depreciation expense arising from the conclusion of the amortization period for the 2003 depreciation reserve variance. As approved in P.U.40 (2005) and P.U. 39 (2006), these costs are being deferred until the next General Rate Hearing when the recovery of these costs will be determined.

Board of Commissioners of Public Utilities
page six...

Based on our review of forecast deferred depreciation expense, we confirm that we have not noted any discrepancies or unusual items, and it is consistent with approved Board Orders.

Deferred Replacement Energy Costs

Under P.U. 39 (2006) the Board approved Newfoundland Power's application to defer for 2007, \$1,147,000 in after tax costs associated with the purchase of replacement energy during the refurbishment of the Rattling Brook hydroelectric plant. During the construction period the Company will have to purchase replacement energy to replace the normal production of the Rattling Brook plant while it is out of service.

Based on our review of forecast deferred replacement energy costs, we confirm that we have not noted any discrepancies or unusual items, and it is consistent with approved Board Orders.

I trust this is the information you requested. If you have any questions please contact me.

Yours truly,



Bill Brushett, FCA
Partner

/tg