Q. **2013 General Rate Application, Deferral and Recovery Mechanisms**

What weight, in Hydro's opinion, should the Board give in considering Hydro's request for approval of cost deferral and recovery mechanisms to the fact that Government has given direction on the rate of return for Hydro?

A. The Lieutenant Governor in Council is authorized by section 5.1 of the *Electrical Power Control Act, 1994* to direct the Board upon a utility's rate of return. In Hydro's present GRA, the rate of return it is to be permitted to earn is set by directive.

There is often a connection between the business risk of a utility and the rate of return it is permitted to earn by the utility's regulator. Cost deferral and recovery mechanisms are often deployed by regulators to attenuate the instability of earnings that can occur from short-run business risks (such as with Newfoundland Power). Examples of deferral and recovery mechanisms used or approved by the Board include:

Hydro

- Rate Stabilization Plan;
- Deferred Foreign Exchange Losses;
- Deferred Major Extraordinary Repairs;
- Deferred Study Costs;
- Deferred Energy Conservation Costs; and
- Deferred Purchased Power Savings.

Newfoundland Power

- Rate Stabilization Account (RSA);
- Revenue Shortfall Deferral;
- Weather Normalization Account, with both a reversing and non-reversing mechanism;
- Amortization True-Up Deferral;
- Pension Deferral;
- Replacement Energy Deferral;
- Deferred GRA Costs;
- Conservation and Demand Management Deferral;
- Municipal Tax Liability;
- Unbilled Revenue;
- Purchased Power Unit Cost Variance Reserve;
- Future Removal and Site Restoration Provision;
- Demand Management Incentive Account (DMI);
- Pension Expense Variance Deferral Account (PEVDA);
- Energy Supply Cost Variance Reserve (ESCVR);
- Other Post Employment Benefits (OPEBS) Variance Deferral Account;
- Cost Recovery Deferral Account; and
- Cost of Capital Deferral.

However, Hydro submits that, in considering how the Board should assess the appropriateness of cost deferrals, the Board should consider the outcome that was intended in the directive.

It is not reasonable to assume that the purpose of the directive was to be neutral in its effect on Hydro's earnings, nor is it reasonable to assume that the object of

Government was to impose upon Hydro an increased amount of business risk. If either or both of those outcomes were Government's intentions, it could have accomplished those goals more directly by, in the first case, directing the Board to hold Hydro's earnings at its last approved level or, in the second case, by directing the Board specifically as to deferral and recovery mechanisms. Government chose to do neither; it chose to direct the Board on Hydro's rate of return.

Hydro submits that the directive should be interpreted in accordance with principles used to interpret statutes. The *Interpretation Act*, RSNL 1990 Chapter I-19, provides guidance. Section 16 reads as follows:

Rule of construction

> ***16.*** *Every Act and every regulation and every provision of an Act or regulation shall be considered remedial and shall receive the liberal construction and interpretation that best ensures the attainment of the objects of the Act, regulation, or provision according to its true meaning.*

Interpreting the directive as including an intention of increasing the business risk of the utility so as to negate the increased rate of return could be seen as striving to cancel, as opposed to achieve, the remedial purpose of the directive. In Hydro's view, the Board is required to implement the directive in a manner which is most conducive to the attainment of its objects and, as there is no other indication in the directive as to changes to be made as to Hydro's business risks, the Board should consider all other aspects of Hydro's earnings profile in a manner which is "blind" as to the impact of the directive. This means it should consider the deferral and recovery mechanism, and the business risk issues faced by Hydro, as if Hydro's allowed rate of return had not changed from the last Order from the Board arising from Hydro's GRA.