

1 Q. Re: Page 2, lines 6-10 and page 8, lines 16-21. It is stated that the report accepts
2 Hydro's submission that the revenue requirement be based on the premise that
3 the island functions as an isolated system and that further comment on this
4 approach may be provided "once the details on the Off Island Purchases Deferral
5 account are made available".

6 Please list the details that in Mr. Bowman's opinion should be provided to allow
7 a full assessment of Hydro's proposed approach to revenue requirement.

8 A. In Mr. P.Bowman's view, Hydro's basic assertion is that the normal regulatory
9 principle that rates in a given year should track costs in that year should be set
10 aside in favour of a competing regulatory principle that rates should be stable. It is
11 entirely acceptable (and expected) that regulators must balance competing rate
12 objectives.

13 However, in this case there are two important considerations:

14 1) **Test year values:** While rates should be stable year over year, and
15 mechanisms to aid in stability are not uncommon (like the RSP), it is
16 uncommon to set rates with a clear disregard for the expected costs to
17 provide service in the test year. As a result, the threshold for accepting
18 Hydro's proposal should be relatively high. Consider that in 2002, Hydro
19 was facing material fuel price increases, so proposed to use an artificially
20 low \$20/bbl to set test year rates with the full knowledge that the higher
21 expected price of \$25.91/bbl was the more likely price to prevail and would
22 be deferred to the RSP. Hydro proposed such measure in the interests of
23 rate stability. The Board rejected this proposal in Decision P.U.7 (2003) and
24 indicated that ignoring test year costs was not in the public interest, noting:
25 "The Board is required to set rates based on forecast costs for a test period
26 and believes that the most prudent course of action is to set the fuel price
27 at or near the price forecasted for the test year." All this is provided for the
28 Board's consideration, with an explicit notation that Mr. P.Bowman has not
29 and cannot provide any legal interpretation of Hydro's approach in light of
30 the legislative framework for rate setting in Newfoundland and Labrador,
31 which obviously is an overriding consideration.

1 2) **Rate Stability:** If the assertion is that the normal principles regarding test
2 year costs are to be overridden in favour of a proposal that is said to be in
3 the interests of rate stability, it would seem there is at best limited evidence
4 available to date as to how much rate stability can be achieved by yielding
5 on the test year principle. For example, though it is clear funds should
6 accrue in the Off-Island Purchases Deferral Account, how would such funds
7 be ultimately used, over what period, and to what effect? Would the net
8 benefit be material, or de minimus? Would the same rate classes (and
9 generations of ratepayers) benefit as those who were disadvantaged by the
10 deferral in the first place? Are there issues of potential negative balances in
11 the account, which may reverse the considerations, and simply lead to
12 Hydro recovering costs to which it is otherwise debatably not entitled (again,
13 partially a legal issue).

14 The information to answer such questions appears to be too limited as yet to come
15 to a fully-informed opinion.