

Supplementary Direct Evidence of Tony Morris

- Q. Mr. Morris, I understand that you have assumed responsibility for the testimony of Ms. Grewal as it relates to deferral accounts and changes made to the application in light of the evidentiary update.
- A. That is correct.
- Q. And further, I understand you are prepared to elaborate on BC Hydro's proposal as it relates to the extent and manner of any prudency review by this Commission of any amount contained in the deferral accounts.
- A. Yes. BC Hydro proposes that the Commission should be advised annually of what amounts have been placed in the deferral accounts and prudency reviews of those amounts should occur at least at every revenue requirement hearing and between revenue requirement hearings if deemed advisable by the Commission.
- Q. When the Commission conducts a prudency review of amounts in the deferral accounts, do you believe it should review all amounts on the same basis?
- A. No, I do not. I believe it should apply the same standard of review to each category of expense in the deferral accounts as it would have when setting a revenue requirement prospectively. Thus, the BCTC Transition Deferral Account should be subject to little or no prudency review because it will be a product of the Commission's decision on BCTC's revenue requirement application and as such the issue of prudency does not arise. With respect to the trade income deferral account, prudency should only be an issue in the very limited way that the forecast of Powerex's net income is in issue in these proceedings. On the other hand, the amounts in the HDA and the NHDA would be subject to prudency review to the same extent they are subject to reasonableness review in a proceeding such as this one.
- Q. How will your financial statements be affected by the Commission's determination of prudency with respect to amounts placed in the deferral accounts?
- A. Once the Commission has determined any amount placed in a deferral account to be imprudent, GAAP would require BC Hydro to write off the expense. Any amounts that the Commission determined had been prudently incurred would remain in the deferral account until the Commission has determined the manner in which they could be recovered in rates.
- Q. Would the amounts determined to be prudent be recovered in rates as soon as the Commission made its prudency determination?

- A. Not usually. Normally we would not expect there to be any connection between the Commission's prudency review and a decision to clear all or part of the deferral accounts by adjusting the revenue requirement in a particular year to reflect amounts in the account.

We believe the prudency review should happen close enough to the events giving rise to the deferral amount to allow for meaningful review. After that review has occurred and amounts are deemed appropriate for inclusion in the revenue requirement, they should only be taken into the revenue requirement if the Commission is persuaded on application that the account should be fully or partially cleared because the amount that has accumulated is unlikely to be offset by events in future years and should begin to be reflected in rates to avoid the potential for a significant impact on rates in future years.

- Q. Would the deferral account be cleared all at once?

- A. Not normally. We would expect the Commission to look at all the deferral accounts together rather than as separate accounts. The Commission could determine that all or part of the total account should be taken into rates over whatever period of time it determined appropriate. We would expect the Commission to order the recovery of negative amounts in the account (i.e. caused by expenses higher than those forecast, covered by the deferral account) over sufficient years to avoid significant rate fluctuations in any one year and to employ positive amounts (i.e. amounts caused by revenues or expenses lower than those forecast covered by the deferral account) to avoid the need for future rate increases.

- Q. Can you provide an example of how you see the deferral account working?

- A. Yes. Exhibit A attached to my evidence illustrates how the account might work. I am prepared to walk through that exhibit when I appear before the Commission.

EXHIBIT A

Impact of Regulatory review of Deferral Account charges

Note	A	B	C	D
	Year x Approved	Year x Actual	Year x+1 ALL DA Approved	Year x+2 Some DA Approved
(\$ million)				
Revenues	\$2,500	\$2,500	\$2,500	\$2,500
Rate change from DA review			50	30
Costs	2,100	2,200	2,100	2,100
Net Income before DA	400	300	450	430
DA transfers to (from)	0	100	(50)	(30)
Net Income for approved costs	400	400	400	400
Unapproved DA write off				(20)
Net Income for the year	\$400	\$400	\$0	\$380
Under(over) earning compared to allowed Net Income	\$0	\$0	\$0	\$20
Deferral Account (DA)balance	\$0	\$100	\$50	\$0

Notes

- The approved Net Income (or return on equity) is assumed at \$400.
- 1 Column A In Year 1 the regulator allows a Net Income of \$400.
 - 2 Column B. The actual costs for year 1 exceeded plan by \$100 and were included in a deferral account(DA). The Net Income equals the approved amount and there is a balance of \$100 in the DA.
 - 3 Column C The Company applies to bring the \$100 DA balance into income equally over years x+1 and x+2. This is done by increasing customer rates. In Year x+1 rates increase by \$50 as does Net Income before DA, but the transfer out of the DA brings Net Income back to the approved \$400.
 - 4 Column D For Year x+2 the regulator determines that \$20 in the DA was not prudently incurred and thus only \$30 of the \$50 balance in the DA is recovered in rates. The remaining DA balance of \$20 must be written-off and the Company underearns by \$20 and is short of its NI by this amount.
 - 5 This is similar to the regulator preapproving an ROE in a revenue requirement application as per Column A of \$400. The Company may then spend \$20 on unapproved items- whether or not the spending is prudent this amount would be for the account of the shareholder in the absence of a DA.