Q. McShane states on pages 13 and 14 of her evidence "Hydro elected to charge retained earnings for the entire amount of the transitional obligation, thus creating a liability for future employee benefits. By comparison, many Canadian utilities are amortizing the transitional obligation over the remaining employee service life, as permitted under the CICA guidelines, and seeking to recover the transitional obligation from rate payers over the amortization period."

(a) Why has Hydro chosen this approach in accounting for future employee benefits?

(b) Provide a projection of the impact on revenue requirement for each year from 2002 to 2006 if Hydro had elected to amortize the transitional obligation over the remaining employee service life.

(c) Provide a projection of the impact on revenue requirement for each year from 2002 to 2006 if Hydro had elected to account for employee future benefits on a cash basis rather than an accrual basis of accounting.

A. (a) In 2000 Hydro complied with the Canadian Institute of Chartered Accountants (CICA) recommendation to account for Employee Future Benefits (EFB) on an accrual rather than a cash basis. The accrual method provided for two options to account for EFBs, namely the Retroactive Application approach or the Prospective Application approach. Hydro has chosen the Retroactive Application approach and has charged retained earnings for the entire amount of the transitional obligation for future employee benefits in 2000. It was felt that an adjustment to retained earnings achieves the best matching of costs and revenues, since the transitional balance has arisen from employee service in prior periods and is not related to the activity of current or future periods. In addition adoption of the prospective approach would have resulted in a higher revenue requirement as outlined in (b) below.

(b) If Hydro had elected to amortize the transitional obligation over the remaining employee service life the revenue requirement in each of the years 2002 to 2006 would have to increase by approximately $1.8 million.

(c) Based on a projection of future retirements, the amount that would be included in revenue requirement on a cash basis is estimated to be as follows:

2002	1,199,000
2003	1,074,000
2004	1,174,000
2005	1,215,000
2006	1,648,000