

1 **Q. Reference: Section 4.0 Cost Recovery Alternatives**

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3 **Please comment on the advantages and disadvantages of a third option:**  
4 **Determining on an annual basis the current value of the accrued OPEBs obligation,**  
5 **the accumulated reserve and the shortfall in the reserve, and then**

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7 **defining the total OPEBs cost to be included in rates as:**

8  
9  **$(O - R)/N$**

10  
11 **where:**

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13 **O is the current OPEBs obligation,**

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15 **R is the current reserve (accumulated excess in OPEBs costs recovered in rates**  
16 **minus actual cash OPEBs costs, and**

17  
18 **N is the number of years remaining in the amortization term.**

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20 **Under this option, the rate base effect could be addressed by treating the**  
21 **accumulated reserve as an offset to rate base directly.**

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23 **A. A. Calculation of 2011 OPEBs Costs**

24 Newfoundland Power interprets the value of  $(O - R)/N$ , or the total OPEBs costs to be  
25 recovered in rates in 2011, to be \$4,156,000, where:

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27  $O = \$62,334,000$  (OPEBs accrued obligation at January 1, 2011)

28  $R = \$0$  (accumulated excess in OPEBs costs recovered in rates minus actual cash  
29 OPEBs costs at January 1, 2011<sup>1</sup>)

30  $N = 15$  years

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32 **B. Observations**

33 The total OPEBs costs to be recovered in rates in 2011, as defined in the question, of  
34 approximately \$4.2 million is not calculated in accordance with any relevant accounting  
35 standard. It is less than the amount which would be required to recover the Company's  
36 accrued 2011 OPEBs costs of \$5.7 million under current Canadian GAAP or \$4.3 million  
37 under IFRS.

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39 Since the total OPEBs costs proposed by the question to be recovered in 2011 rates (and  
40 recorded for regulatory purposes) is less than the amount required to be recorded for  
41 financial reporting purposes, then the transitional balance, or regulatory asset, will  
42 continue to grow in 2011. This implies that increased annual OPEBs cost recovery will

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<sup>1</sup> This difference is not a *reserve*. See the Response to Request for Information CA-NP-3.

1 be required in later years of the amortization period to permit recovery of the transitional  
2 balance, or regulatory asset, within that period.

3  
4 The denominator in the calculation, or N, is effectively a declining value in each  
5 successive year of the amortization period. This implies that changes in assumptions in  
6 later years of the amortization period (when N is a lower value) will tend to have a  
7 greater impact on annual OPEBs costs to be recovered in rates. For example, the impact  
8 upon the accrued OPEBs obligation of discount rate changes in year 14 of a 15 year  
9 amortization period will be fully recoverable in annual OPEBs costs in year 15 of the  
10 period.

### 11 **C. Comments**

12 In Order No. P.U. 43 (2009), the Board, in effect, ordered Newfoundland Power to file a  
13 comprehensive proposal for the adoption of the accrual method of accounting for OPEBs  
14 costs as of January 1, 2011. The proposal was specifically ordered to include  
15 recommendations and alternatives in relation to (i) a deferral mechanism to capture  
16 annual variances arise from changes in the discount rate and other assumptions, and (ii)  
17 recovery of the transitional balance associated with the adoption of accrual accounting for  
18 OPEBs costs.<sup>2</sup>

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20  
21 The definition of OPEBs costs to be included in rates as contained in the question, if  
22 adopted, would:

- 23 (i) not permit the adoption of the accrual method of accounting for OPEBs  
24 costs as of January 1, 2011;  
25 (ii) not provide for any recovery of the transitional balance associated with the  
26 adoption of accrual accounting for OPEBs costs in 2011; and  
27 (iii) not address a deferral mechanism to capture annual variances which arise  
28 from changes in the discount rate and other assumptions.

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30 This definition does not comply with Order No. P.U. 43 (2009).

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<sup>2</sup> The requirements of Order No. P.U. 43 (2009) broadly reflect the recommendation of the Consumer Advocate's expert witness, Mr. John Todd, who indicated "My recommendation to the Board would be to direct the Company to bring back a proposal for resolving the transitional obligation and moving to the accrual method in a manner that mitigates the rate impact and addresses intergenerational equities as effectively as possible." (2010 GRA, Mr. Todd, Transcript, October 27, 2009, page 128, lines 6-12)