

1     **Q. Please confirm the Board has approved the recovery of employee future benefit cost**  
2     **variances between test years through Newfoundland Power's Rate Stabilization**  
3     **Account. If confirmed, please explain why the cost recovery of variances in**  
4     **employee future benefit costs between test years is appropriate.**

5     A. It is confirmed.

6                   ***Background***

7     In Order No. P.U. 43 (2009), the Board approved the use by Newfoundland Power of a  
8     Pension Expense Variance Deferral Account ("PEVDA") to capture the difference  
9     between the annual pension expense approved for the test year revenue requirement and  
10    the actual pension expense computed in accordance with generally accepted accounting  
11    principles for any subsequent year to reflect changes in Newfoundland Power's annual  
12    pension expense due to changes in assumptions, in particular discount rates.

13    In Order No. P.U. 31 (2010), the Board approved the use by Newfoundland Power of an  
14    Other Post-Employment Benefits ("OPEBs") Cost Variance Deferral Account  
15    ("OPEVDA") to capture future changes in OPEBs costs from those included in rates to  
16    reflect changes in assumptions, such as discount rates. The operation of the OPEVDA is  
17    consistent with the PEVDA. Changes in discount rates, which are the result of changes  
18    in capital market conditions, are broadly accepted to be beyond the control of utility  
19    management.

20    The PEVDA and OPEVDA operate annually in a manner which is conceptually  
21    consistent with the operation of Newfoundland and Labrador Hydro's ("Hydro") rate  
22    stabilization plan (the "RSP").

23    The primary difference between the PEVDA and OPEVDA versus the RSP is that the  
24    PEVDA and OPEVDA make annual adjustments for Newfoundland Power's pension and  
25    OPEBs expense, respectively, and the RSP makes annual adjustments for Hydro's cost of  
26    fuel at Holyrood. The PEVDA, OPEVDA and RSP all adjust customer rates to reflect  
27    annual changes in costs based upon the most current test year parameters approved by the  
28    Board. Such regulatory mechanisms, which provide for annual adjustments for specified  
29    utility costs, are commonplace in Canadian utility practice.

30                   ***Appropriateness of Board Approval***

31    The Board approval of the PEVDA was appropriate for a number of reasons, including:

32    1. evidence concerning Newfoundland Power's PEVDA, including the variability in  
33      annual pension expense due to changes in assumptions, was reviewed by the Board in  
34      the context of the Company's 2010 general rate application;

1        2. the Board's consultant, Grant Thornton, reviewed Newfoundland Power's PEVDA  
2        proposal and concluded in evidence that it would limit the variability of the pension  
3        expense due to changes in assumptions, in particular discount rates; and  
4        3. the PEVDA was agreed upon in the settlement agreement between the Consumer  
5        Advocate and Newfoundland Power, which was facilitated by Board Hearing  
6        Counsel.

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8        The Board approval of the OPEVDA was appropriate for a number of reasons, including:  
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10        1. evidence concerning Newfoundland Power's OPEBs, including the variability in  
11        OPEBs, was reviewed by the Board in the context of the Company's 2010 general  
12        rate application;  
13        2. in Newfoundland Power's 2010 general rate application, the Board's consultant,  
14        Grant Thornton, concluded in evidence that while PEVDA addressed pension  
15        variability, the variability of OPEBs still existed;  
16        3. in Order No. P.U. 43 (2009), the Board ordered Newfoundland Power to submit a  
17        comprehensive proposal for adoption of the accrual method of accounting for other  
18        post-employment benefits costs as of January 1<sup>st</sup>, 2011; and  
19        4. the Board's consultant, Grant Thornton, in reviewing Newfoundland Power's  
20        application, concluded in evidence that the use of the OPEBs Cost Variance will limit  
21        the variability of the OPEBs cost due to changing assumptions, such as discount rates,  
22        as well as changes related to rate base effects.

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24        Approval of Newfoundland Power's recovery of variances in employee future benefit  
25        costs via the rate stabilization account was only given by the Board after its review of a  
26        comprehensive evidentiary record developed in the course of a general rate application.