

1 **Volume 1, Section 2 – Customer Operations**

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3 **Q. What is NP’s policy with respect to capitalization of salaries and benefits or other**  
4 **overheads? Please describe how the salary and benefit amounts to be capitalized are**  
5 **determined on an actual and a forecast basis.**

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7 A. The classification of expenditures as capital or operating is based on Generally Accepted  
8 Accounting Principles (GAAP), the Company’s System of Accounts and, where  
9 applicable, guidance from the Board.

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11 Salary, or labour, is budgeted and charged as (i) an operating cost, (ii) a direct capital  
12 expenditure or (iii) a cost that is rechargeable or recoverable from a third party, based on  
13 the nature of the work being budgeted or performed and on hourly rates by position  
14 classification. A payroll loading, or overhead, rate is applied to labour as it is budgeted  
15 and charged to allocate certain benefits and payroll overheads among operating, capital  
16 and recoverable accounts in a manner that is consistent with the actual labour charges.

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18 The payroll loading, or overhead, rate is developed as part of the annual budget process.  
19 Overheads included in the calculation include the Company’s estimated cost related to  
20 CPP, EI, payroll tax, workers’ compensation premiums and health benefit premiums.  
21 The total of these estimated costs is divided by the estimate of total annual labour to  
22 arrive at a percentage. This percentage is then applied to budgeted labour to arrive at  
23 total operating, capital and recoverable labour budgets. The same percentage is also  
24 applied to actual operating, capital and recoverable labour charges, as reported on  
25 timesheets.

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27 As the overhead rate is applied to actual labour charges, the recovery of estimated  
28 overheads is tracked and compared against actual costs incurred. Periodic adjustments  
29 are made, if required, so that the total amount of overheads allocated to operating, capital  
30 and recoverable accounts essentially equates to the actual overhead costs incurred during  
31 the year.

32  
33 Pension costs are accounted for in a manner that differs somewhat from other payroll  
34 overheads. That is, pension costs are not capitalized through the payroll loading, or  
35 overhead, rate process. Pension costs are captured initially as an operating expense, and  
36 a portion thereof is then capitalized through the General Expenses Capitalized (“GEC”)  
37 mechanism approved by the Board in Order No. P.U. 3 (1995-96).