Volume 2, Tab 4 – A Report on Employee Future Benefits

Q. CA-NP 201 (pages 7-8) "The Transitional Obligation is the actuarially determined difference between (i) the total OPEBs expense that would have recognized by the Company pursuant to the Accrual Method since January 1, 2000, and (ii) the total OPEB's expense recognized since that date under the Cash Method. It represents legacy OPEB's costs that have not yet been recovered from customers. As at the proposed January 1, 2008 adoption date from the Accrual Method of accounting for OPEBs the forecast Transitional Obligation is approximately $34.1 million." Please explain why NP did not propose adoption of the Accrual Method of accounting for OPEB costs as soon as practicable subsequent to January 1, 2000 so as to avoid the build up of the Transitional Obligation.

A. ***A. Introductory***

Newfoundland Power's OPEBs liabilities are a part of its cost of providing service to its customers.

Commencing in 2000, the Canadian Institute of Chartered Accountants (the "CICA") recommended that OPEB liabilities be *recognized for accounting purposes* under the Accrual Method. Prior to this recommendation, most businesses, including regulated utilities, recognized OPEB liabilities under the Cash Method.

The difference in accounting methods for OPEBs does not impact the aggregate amount of the OPEBs liabilities to be recognized or recovered as part of a utility's cost of service.

Accordingly, the central issue related to OPEBs from a cost of service perspective relates to the timing of recognition, or recovery from customers, of Newfoundland Power's OPEB liabilities.

B. The 2003 GRA

The Company's accounting policy for OPEBs was addressed in its 2003 general rate application. In that Application, the Company proposed that it remain on the Cash Method of accounting for OPEBs. This was consistent with generally accepted accounting principles.

The Board approved Newfoundland Power's proposal to remain on the Cash Method of accounting in Order No. P.U. 19 (2003). At page 83 of that Order the Board stated:

> "To avoid rate impact on consumers the Board is prepared to accept NP's proposal to continue with using the cash basis for recognizing expenses for other employee future benefits."

> "The Board is concerned about the potential liability for employee future benefits and is of the view that NP should explore using the accrual method of accounting for these benefits. The Board recognizes that there are significant transitional obligations associated with this change in accounting policy but once the transitional obligation has been met these costs should decrease. NP should continue to monitor its obligations with respect to employee future benefits and corresponding regulatory practice. The Board will direct NP to propose a plan at its next general rate application for moving towards the accrual method of accounting for employee future benefits as recommended by CICA. The Board emphasizes such a plan should be presented to the Board as an alternative to the existing method and should address the transitional impact with a view to fulfilling NP's obligation to its employees while at the same time moderating its impact on rates. The Board will then be in a position to consider this alternative accrual method and its specific impacts at the next hearing."

C. The Current Application

In this Application, Newfoundland Power has proposed a plan for moving from the Cash Method to the Accrual Method of accounting for OPEBs. The plan addresses transitional impacts while moderating rate impacts. This is what was ordered by the Board in Order No. P.U. 19 (2003).

Newfoundland Power's proposed plan for transitioning to the Accrual Method of accounting for OPEBs provides a reasonable means of addressing recovery of the overall OPEB liabilities.

Newfoundland Power's proposals in both the 2003 GRA and the current application have not had the effect of increasing the aggregate amount of OPEBs liabilities required to be recovered from its customers.