

**Board Staff Submission**  
**West Coast Huron Energy Inc.**  
**2009 Electricity Distribution Rates Application**  
**Supplemental Evidence, September 17, 2009**  
**EB-2008-0248**

**INTRODUCTION**

West Coast Huron Energy Inc. (“West Coast Huron”) claimed as an expense for rate making purposes an Accrued Benefits Obligation (“ABO”) for Post Retirement Non-Pension Benefits (“PRNPB”) of \$150,000 in their 2009 test year. This was an out-of-period liability that was reported in the financial statements in the 2007 year. The \$150,000 was based on management’s estimate of a future obligation and not supported by an actuarial valuation. The evidence on this matter was both insufficient and unclear.

The Board in its Decision and Order dated June 17, 2009 disallowed this claim of \$150,000, finding the total O&M budget for the test year as \$1,544,350. The Board also declared the rates interim and allowed a 3 month period for West Coast Huron to submit additional evidence in support of this specific claim.

West Coast Huron filed supplemental evidence on September 17, 2009. Responses to interrogatories were completed and filed with the Board by October 5, 2009. The following is Board staff’s submission on the ABO and the determination of the revenue requirement based on the record.

**THE ACCRUED BENEFITS OBLIGATION**

The reporting of a company’s obligation for future benefits in a defined benefits plan should be disclosed on the financial statements as per CICA Section 3461. This shows the effect of the obligation on the company’s financial statements. An ABO is determined by an actuarial valuation using a standard methodology and a number of management provided estimates. These estimates are for variables such as future health care cost trends, CPI, average remaining working years of the employees and other financial and demographic factors regarding the work force.

West Coast Huron recorded an ABO of \$150,000 in their 2007 financial statements, and included this amount in their original 2009 COS rate application.

The \$150,000 was based on management's estimate and was not supported by an actuarial valuation.

In this supplemental filing, West Coast Huron submitted an actuarial valuation prepared by Dion Durrell + Associates Inc. (the "Actuary"). The Actuary estimated the ABO as of January 1, 2008 to be \$342,877 and suggested that it be amortized over 9 years at \$21,431 per year. The 9 year period corresponds to the average remaining service period of active employees expected to receive benefits under the benefit plan.

West Coast Huron is proposing to amortize \$150,000 of the \$342,877 over 4 years and the remaining \$192,877 over 9 years. This results in \$58,931 per year for the first 4 years and \$21,431 per year from year five to year nine.

While PRNPB is an allowable expense specified in the 2006 EDR Handbook<sup>1</sup>, Board staff has concerns about West Coast Huron's proposal. They are:

- The amount of the ABO to be recovered in rates; and
- Amortization of the ABO.

### **The amount of the ABO to be recovered in rates**

The components of the ABO are found on page 2 of the Valuation Report. Of the \$342,877 for the total ABO, \$191,000 is for "People in receipt of benefits". In response to Board staff's interrogatory 3 a), West Coast Huron defines this expense as the unrecorded liability related to employees who are currently receiving PRNPB. In other words, this \$191,000 pertains to retired employees.

Board staff investigated the prior treatment of ABO in its Interrogatory 2 b). Board staff asked why the CICA Section 3461 accounting standard had not been applied until now. West Coast Huron replied:

"The standard had not been applied until now due to error. The PRNPB was not setup because management did not realize that extent and material liability that existed. The auditors' pointed out the problem during the 2007 audit. Management immediately addressed the issue and decided to accrue the liability to meet the accounting standard."

In essence, West Coast Huron is requesting the Board to make up for out of period costs because of management error. Had West Coast Huron recognized the obligation for these past employees in 2000 when the CICA Section 3461 came into effect, they would have collected the amount over their average

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<sup>1</sup> RP-2004-0188, Report of the Board; 2006 Electricity Distribution Rate Handbook, May 11, 2005

remaining service for those employees. Since the employees are now retired, their service period has ended, and the appropriate obligation would have been essentially collected. To correct for management's error, West Coast Huron's proposal to recover the \$191,000 would cause the rate payers to bear the costs of retirees who are no longer serving West Coast Huron rate payers.

Board staff submits that the full \$191,000 would normally be excluded for rate making purposes since it is an out of period adjustment. However, Board staff suggests that during the early years of electricity deregulation in Ontario there was uncertainty of responsibilities by smaller utilities, and a rate freeze. However, responsibilities, particularly with respect to rate setting, were made much clearer with the 2006 EDR Handbook. In that handbook, the matter of an ABO was specifically addressed. That means that as the handbook was being developed through public consultations, the industry knew of what would be expected. Although Board staff is inclined to submit that none of the \$191,000 should be allowed, Staff suggest that the Board consider the situation that led up to this portion of the ABO related to retirees being proposed for recovery at this time.

### **Amortization of the ABO**

Board staff suggest that the amortizing any portion of the ABO for the \$191,000 which is for retired employees be a different amortization than that for the \$152,000 which is for current employees.

If the Board allows any portion of the \$191,000 for the post retirement benefits for existing retiree, then staff submits that it should be collected over the four years of the IRM period. Board staff submits that the longer it takes to meet this obligation for retired employees, the greater will be intergenerational subsidization.

As for the remaining obligation of \$152,000; that amount represents a cost determined as of January 1, 2008 for current employees. That amount should be collected pursuant to the CICA Section 3461. It should therefore should be amortized according to the Actuary's recommendation of 9 years, beginning in 2008. However, the portion determined to be for 2008 should not be recovered. For a total ABO for current employees of \$152,000, this translates into \$16,889 per year for 9 years for the remaining obligation ( $\$152,000 \div 9$ ). However, staff submits that West Coast only be allowed to collect \$16,889 in rates for 8 years from 2009 forward. This would disallow the 2008 out of period part of the amortization.

## REVENUE REQUIREMENT DETERMINATION

West Coast Huron filed the necessary calculations supporting a rate rider based on their proposal of amortizing \$150,000 over 4 years and the balance of the \$342,887 amortized over 9 years. Board Staff notes that West Coast Huron treated the resulting increase as a cost that affects the working cash allowance. The net effect of this working cash increase was to increase the rate base from the approved \$5,107,346 to \$5,116,121, and therefore to increase the related return and taxes.

Board staff submits that this is incorrect. The working cash allowance is the component of working capital that reflects the required cash on hand to run the business from a cash perspective on a daily basis; cash in hand for payroll, materials, and other cash outlays and revenue stream collected from ratepayers.

This amortize amount of \$16,889 is not a cash item. West Coast Huron in response to Board staff Interrogatory 2 c) submitted:

“There is certainly a cost in the current period because benefits and the earning of a future benefit reflects the true cost of labour of the current period. **But, there is no cash outlays (sic.) for these benefits until such time as employees retire and the utility is left with the obligation to pay the benefits.** [Emphasis Added]”

Board staff submits, that the working cash requirement should not be adjusted from the already approved level.

All of which is respectfully submitted.