

DE 03-238

UNITIL ENERGY SYSTEMS, INC.

Petition for the Deferral of Post-Retirement
Benefits Other than Pension

Order Nisi Approving Requested Accounting Treatment

O R D E R N O. 24,269

January 30, 2004

I. **PROCEDURAL HISTORY**

On December 19, 2003, Unitil Energy Systems, Inc. (Unitil), filed with the New Hampshire Public Utilities Commission (Commission) a Petition for the Deferral of Post-Retirement Benefits Other than Pension. In its petition, Unitil is seeking an accounting order authorizing it to defer post-retirement benefits other than pension (PBOP) expenses booked in accordance with Statement of Financial Accounting Standards No. 106 (SFAS 106), *Employers Accounting for Postretirement Benefits Other than Pensions*. According to Unitil, such accounting treatment represents a change from Unitil's existing practice of recording PBOP expenses on a pay-as-you-go basis and is necessitated by the recent issuance of the Financial Accounting Standards Board's Interpretation No. 46 (FIN 46), *Consolidation of Variable Interest Entities*.

The Commission Staff (Staff) issued information requests to Unitil on January 8, 2004, and Unitil provided

responses to those questions on January 15, 2004. On January 27, 2004, Staff provided a recommendation to the Commission.

II. UNITIL'S POSITION

Prior to October 1, 2003, Unitil's retirees received their PBOP benefits principally from the Unitil Retiree Trust (URT), a special purpose entity formed as a trust that, according to Unitil, does not meet the definition of an employee benefit plan. Due to its structure as a special purpose entity, Unitil states that the URT was not subject to the provisions of SFAS 106.

In a generic Commission proceeding, DA 92-199, the Commission issued *Report and Order Addressing FAS 106 Accounting for Post-Retirement Benefits Other Than Pensions* 78 NHPUC 211 (1993) (hereinafter referred to as Order No. 20,806). That order approved a Stipulation among the Staff, the Office of Consumer Advocate and a number of utilities that set out the agreed-upon methodology and timing for adopting and implementing SFAS 106 and required that companies account for PBOP costs on an accrual basis. Although Unitil participated in that proceeding, it states that it did not join in the Stipulation because the URT special purpose entity was not subject to SFAS 106. Thus, Unitil had been recording annual PBOP expense as the amount funded by Unitil to the URT on a pay-as-you-go basis.

The accounting change that led to the current petition is the FASB's issuance of FIN 46 in January 2003.¹ FIN 46 requires that Unitil, as the Primary Beneficiary (as defined in FIN 46) of a variable interest entity (URT in this case) must include the assets, liabilities and financial results of URT in its consolidated financial statements. "As [a] result, effective in the fourth quarter of 2003, the Company has assumed the obligations of URT to provide PBOP benefits to the Company's retirees and accounts for these liabilities in its consolidated financial statements in conformity with SFAS 106 and GAAP." Petition, paragraph 4.

Now that Unitil has assumed the obligations of the URT and accounts for liabilities in accordance with SFAS 106, it requests that the Commission approve accounting treatment for its PBOP obligations in a manner similar to that approved in Order No. 20,806. Specifically, in paragraph 4 of its petition, Unitil cites the following provisions from Order No. 20,806 and Stipulation with which it intends to comply:

1. Forty-five days prior to implementation of rate recovery, each utility must submit to the Commission documentation in support of its SFAS 106 expense and APBO².

¹ FIN 46 was subsequently revised in December 2003. According to its response to data request #1, Unitil states that "[t]he revisions made in December 2003 . . . do not have any impact on and/or require any changes to UES' petition."

² "APBO" stands for accumulated post-retirement benefits obligation which is the accumulated amount of benefits earned by employees up to a particular date.

2. Each utility (with certain exceptions)³ agreed to utilize an external irrevocable trust outside of the company's control for the purpose of funding PBOP. The trustee must be independent of the company and authorized to make only those investments which are consistent with sound investment policies for funds of this nature.
3. Each utility (with certain exceptions) must make annual contributions to the external trust fund in amounts not less than their full accrual SFAS 106 expense.
4. Each utility utilizing an external trust, in whole or in part, must use a trust which provides that any disbursements made from the trust are limited to payments for the benefit of employees pursuant to the company's post-retirement plans, payments for expenses of the trust and refunds to customers pursuant to a Commission approved refund plan in the event the funds are not paid to employees. The amount to be refunded must be net of applicable taxes and amounts transferred to other employee benefit plans, in accordance with SFAS 87 and GAAP.
5. Each utility must maximize the use of income tax deductions for contributions to its external trust for funding PBOPs.

³ The "exceptions" referred to are certain companies that were identified as "Special Circumstance Companies" in Order No. 20,806. The distinction is not relevant for purposes of Unitil's Petition.

Deferred tax assets resulting from non-tax deductible contributions shall be allowed as rate base additions.

6. Each utility must file an annual report on the status of the company's PBOP plan, including a descriptive summary of all actions taken to mitigate the costs of the plan and any updated assumptions. Each utility must also file for Commission approval prior to making any major changes to its PBOP plan(s).

In addition to the above requirements, Order No. 20,806 specifically allowed utilities to defer and amortize the following components of PBOP liability: a) the unrecognized APBO, amortized over twenty years, and b) the PBOP expenses incurred between the date of adoption of SFAS 106 and the date of implementation of rate recovery, amortized over a period of five years.

Consistent with above provisions, Unitil states that it has established new irrevocable trusts for making tax-deductible contributions for its PBOP obligations. Unitil further states in its petition that it is not seeking any change to its rates at this time. Rather, Unitil "expects to file its documentation and request for recovery by April 1, 2004, which request will be subject to review by all parties and approval by the Commission." Petition, paragraph 9. Unitil states that its proposal for rate recovery will include all of the provisions described above.

As the request for rate recovery will be filed at a later date, Unitil is requesting at this time "an accounting order, prior to the close of its books for 2003, authorizing it to defer PBOP expenses booked under SFAS 106, including the amortization of its APBO, consistent with the Commission's Order No. 20,806 and subject to review by the Commission prior to rate recovery." Petition, paragraph 8. In more specific terms, Unitil is requesting approval to defer "the difference between the amount of PBOP expenses that are included in base rates and the amounts that must be booked in accordance with SFAS 106, incurred . . . between the effective date of the Company's adoption of FIN 46 (October 1, 2003) and the date of implementation of new rates reflecting PBOP expenses." Id.

III. STAFF RECOMMENDATION

After reviewing the filing and conducting discovery, Staff filed a memorandum with the Commission on January 27, 2004 recommending that Unitil's petition be approved. Staff noted that Unitil's request is consistent with accounting changes undertaken by other utilities in the early 1990s and is necessitated by a change in accounting rules for certain special purpose entities.

IV. COMMISSION ANALYSIS

After reviewing Unitil's petition, Order No. 20,806, the Stipulation in DA 92-199 and Staff's recommendation, we will

approve Unitil's petition. The request is consistent with the requirements of Order No. 20,806 and mirrors accounting changes implemented by other utilities upon their earlier adoption of SFAS 106. In our earlier order, we adopted the full accrual method of recognizing PBOP expenses for ratemaking purposes, stating that "PBOPs are earned by employees during their working lives, not after they retire. The accrual method matches the actual cost of service, setting aside PBOPs as they are earned, better than does the pay-as-you-go method." Report and order Addressing FAS 106 Accounting for Post Retirement Benefits Other Than Pensions, 78 NHPUC 211, 213 (1993). That logic still holds true.

We note, however, that contrary to Unitil's expected April 1 filing date, in order to conform with the forty-five day requirement in provision #1 above, Unitil must file the necessary information no later than March 15, 2004. This date is required because Unitil seeks to implement any rate change related to this subject on May 1, 2004 to coincide with other rate adjustments/reconciliations that are scheduled to take effect on that date pursuant to the provisions of Unitil's Restructuring Settlement in DE 01-247.

We emphasize that Unitil is not at this time seeking any change to its rates as a result of the requested accounting order. Unitil does, however, plan to file a proposal for rate

recovery in the near future. In issuing this accounting order, we are not pre-approving the recovery of a specific amount of PBOP expenses in future rates, and are in no way changing our existing policies or precedents on what constitutes a recoverable operating expense. Any request in future rate proceedings for recovery of PBOP expenses will be subject to Commission review. In such a case, Unitil will bear the burden of demonstrating that any PBOP expense is reasonable in amount, prudently incurred and appropriate for recovery in rates.

Based upon the foregoing, it is hereby

ORDERED NISI, that subject to the effective date below, Unitil's petition is approved; and it is

FURTHER ORDERED, that the Petitioner shall cause a copy of this Order Nisi to be published once in a statewide newspaper of general circulation or of circulation in those portions of the state where operations are conducted, such publication to be no later than February 9, 2004 and to be documented by affidavit filed with this office on or before February 23, 2004; and it is

FURTHER ORDERED, that all persons interested in responding to this petition be notified that they may submit their comments or file a written request for a hearing on this matter before the Commission no later than February 16, 2004; and it is

FURTHER ORDERED, that any party interested in responding to such comments or request for hearing shall do so no later than February 23, 2004; and it is

FURTHER ORDERED, that this Order Nisi shall be effective March 1, 2004, unless the Petitioner fails to satisfy the publication obligation set forth above or the Commission provides otherwise in a supplemental order issued prior to the effective date.

By order of the Public Utilities Commission of New Hampshire this thirtieth day of January, 2004.

Thomas B. Getz
Chairman

Susan S. Geiger
Commissioner

Graham J. Morrison
Commissioner

Attested by:

Michelle A. Caraway
Assistant Executive Director