

## SECTION 3.10

### Variance Accounts for Income Tax, Pension and COVID-19

### 3.0 2021 Budget

On December 16, 2016, the Province of New Brunswick enacted amendments to the Gas Distribution Act, 1999 (“GDA”) including the following provision:

*52 (2.1) The Board may, in accordance with generally accepted public utility practice, make an order permitting the general franchise holder to create or establish a regulatory variance account in respect of the occurrence of an event for the purpose of minimizing the rate impact of the costs arising from the event.*

With this amendment, the concept of regulatory variance accounts was included in the regulatory framework.

The common use of variance accounts in regulatory rate making are primarily used to minimize impacts to revenue requirement and smoothen the changes to rates. The following proposed variance accounts will be used for those reasons and minimize impacts to ratepayers from year to year.

#### Variance Account for Income Tax

In its Decision dated December 19, 2019 for Matter No. 453, the Board approved the continuation of the deemed tax approach for the current franchise period, subject to any changes in Liberty’s current ownership structure. The Board also approved that under the deemed tax approach, Liberty may recover income taxes otherwise payable as if it were a corporation based on the applicable provisions of the *Income Tax Act*. Further, in its decision the Board noted that the expiring non-capital losses were \$34.2 million and that taxes would not be incurred until 2022.

Liberty has recently updated the analysis carried out by PricewaterhouseCoopers (“PwC”) last year with the 2019 actual earnings, as well as the forecast for 2020 and the budgeted net income for 2021 and has filed that analysis in this application. Liberty applied the income tax loss carry forward of \$40.4M which resulted from PwC’s final analysis, in the previous application. As a result of the updated earnings for 2019, 2020, and 2021, Liberty is now expected to be taxable in 2021. The estimated amount of cash tax expense, for 2021, is \$915,562, as noted in Table 1. The table also provides details related to the forecasted cash tax expense for 2022 to 2025.

# Review of the 2019 Regulatory Financial Statements/2021 Rate Application

Table 1  
Forecast Taxable Income

	Actual 2019	Forecasted 2020	Forecasted 2021	2022	2023	2024	2025
Book Income	\$ 15,121,593	\$ 9,424,000	\$ 12,195,000	\$ 13,397,316	\$ 13,527,022	\$ 13,644,119	\$ 13,750,967
Meals & entertainment	46,592	45,000	45,000	45,000	45,000	45,000	45,000
Book depreciation	10,750,006	6,928,000	7,237,000	7,691,487	8,185,346	8,593,520	8,945,607
Amortization of deferred development costs		2,919,000	3,193,000	3,222,418	3,238,872	3,238,872	3,240,205
Amortization of regulatory deferral account		3,846,000	3,846,000	3,846,000	3,846,000	3,846,000	3,846,000
Tax depreciation	(7,092,631)	(6,890,887)	(6,858,737)	(9,395,543)	(10,858,013)	(9,466,119)	(9,027,065)
Capitalized admin overhead	(3,417,729)	(3,812,453)	(4,840,466)	(5,018,748)	(4,945,750)	(4,975,320)	(5,074,827)
Non-deductible company pension plan	1,584,628						
Non-deductible OPEB accrual	40,500						
Incentive payment capitalized	(408,476)						
(gain)/loss on disposal of assets	41,485						
Contribution to deferred income plans	(403,348)						
Taxable income before losses	16,262,620	12,458,660	14,816,797	13,787,930	13,038,476	14,926,071	15,725,887
LCF used	(16,262,620)	(12,458,660)	(11,659,685)	-	-	-	-
Taxable income	-	-	3,157,112	13,787,930	13,038,476	14,926,071	15,725,887
Tax Rate			29%	29%	29%	29%	29%
Regulated cash tax expense	\$ -	\$ -	\$ 915,562	\$ 3,998,500	\$ 3,781,158	\$ 4,328,561	\$ 4,560,507

Liberty is requesting a variance account for the cash tax expense for 2021, as well as the forecasted cash taxes for 2022 through 2024. Liberty is requesting to defer the cash taxes of \$915,562 for 2021, by one year, to 2022. Due to timing of the availability of the actual cash tax expense for 2021, Liberty will include an estimate of cash taxes in the 2022 revenue requirement and true up the amount in 2023 once the actual cash tax expense is known. Liberty proposes to utilize a similar approach for the cash taxes for 2022 and beyond.

Starting in 2022, Liberty will be fully taxable and as such proposes to amortize the cash tax expense over two years, so as to lessen the pressure on rates and provide a smoothing of the revenue requirement over that period of time, which will be offset by anticipated Single End Use Franchise (“SEUF”) fees. Table 2 provides details related to the anticipated income taxes for inclusion in revenue requirement for the period 2021 to 2025, based on this amortization period. The amount to defer and/or to amortize will be updated annually based on the actual corporate income tax filing information and as actual amounts from the SEUF payments are known and received. The SEUF information provided in the tables are estimates based on the best information available at this time. However, as these funds are based on a new process as defined by the GDA that has not yet run a full cycle, funds are variable depending on consumption amounts as confirmed by a 3<sup>rd</sup> party and no funds have yet been received by the utility under this methodology. With variable amounts, no certainty related to the SEUF funds receivable or amounts are assured. Although Liberty is

requesting a maximum two year amortization, tax amounts may be amortized more quickly as the revenue requirement allows in order to ensure the smoothest possible impact to revenue requirement. Significant changes to revenue requirement from year to year is not ideal for promotion of rate stability and customer satisfaction. Liberty attempts to minimize the impacts to revenue requirement.

Table 2  
Tax Variance Account Amortization

Line No.		2021	2022	2023	2024	2025
		1	2	3	4	5
1						
2	Number of Years (Amort)	2				
3	Forecast Taxes	\$ 915,562	\$ 3,998,500	\$ 3,781,158	\$ 4,328,561	\$ 4,560,507
4	Amounts included in RR by year	2021	-	915,562	-	-
5		2022	1,999,250	1,999,250	-	-
6		2023		1,890,579	1,890,579	-
7		2024			2,164,280	2,164,280
8						
9		\$ -	\$ 2,914,812	\$ 3,889,829	\$ 4,054,859	\$ 6,724,788

Table 3 shows the forecast revenue requirement for the period 2021 to 2025, including the proposed tax variance amounts.

Table 3  
Revenue Requirement Summary

	2021	2022	2023	2024	2025
Rate Base	\$ 268,861,366	\$ 271,739,664	\$ 274,593,068	\$ 277,232,824	\$ 279,597,215
O&M Expenses	11,818,523	11,989,829	11,813,147	11,883,485	12,121,155
Other Expenses	3,385,991	3,087,823	3,087,823	3,087,823	3,087,823
Depreciation & Amortization	10,427,981	10,457,762	10,249,367	10,405,199	10,772,094
Regulatory Cost of Debt	4,909,034	4,979,950	5,028,164	5,071,690	5,111,407
Regulatory Return on Equity	13,206,532	13,397,316	13,527,022	13,644,119	13,750,967
Revenue Requirement Before Taxes	43,748,062	43,912,680	43,705,523	44,092,316	44,843,446
Taxes (variance account amounts)	-	2,914,812	3,889,829	4,054,859	6,724,788
Deferral (fixed)	3,846,154	3,846,154	3,846,154	3,846,154	3,846,154
SEUF Fees	-	(3,083,330)	(3,083,330)	(3,083,330)	(3,700,000)
Revenue Requirement After Taxes	47,594,215	47,590,316	48,358,175	48,909,999	51,714,387

Liberty's transactions in this proposed variance account will be reported on in future rate applications. No carrying charges will be applied to this variance account.

### Variance Account for Pension

As part of its revenue requirement, Liberty includes defined benefit pension costs based on the cash contribution approach.

1 Due to the timing of the acquisition from Enbridge on October 1, 2019 and the filing of the 2020  
2 general rate application on August 2, 2019, Liberty included defined benefit pension cash  
3 contributions as determined under the then existing Enbridge pension plan, based on the actuarial  
4 valuation report completed by Mercer as at December 31, 2018. The report is being filed and can  
5 be found as Appendix 3.10A. This amount, \$490,900, was included as part of O&M in the 2020  
6 revenue requirement.

7 As part of the terms and conditions related to the acquisition of Liberty, Algonquin Power &  
8 Utilities Corp. agreed to maintain a substantially similar defined benefit pension plan for the  
9 employees of Liberty, for a period of one year post acquisition. An actuarial valuation report as  
10 at December 31, 2019, was completed by Mercer based on the new, interim defined pension benefit  
11 plan ("Interim Plan") and determined the amount of required contributions for 2020 to be  
12 \$1,545,000. The report is being filed and can be found as Appendix 3.10B. While the new Liberty  
13 pension plan is substantially similar to the prior Enbridge pension plan, there are reasons for the  
14 difference in the required company contributions.

15 The assumptions that the Enbridge pension plan uses in determining the cost of their overall  
16 pension plan for all employees would be materially different than what Liberty is using for this  
17 Interim Plan given the different circumstances of the plans and the membership composition. The  
18 Enbridge plan has a much larger membership including both active and inactive members, is an  
19 open plan, has obligations (and assets) with respect to past service and the key interest rate  
20 assumption is set based on future long-term outlook of expected returns per the plan's asset mix. In  
21 comparison, the Interim Plan only has active members (only made up of the New Brunswick  
22 employees) that are overall a more mature/long service group than the overall Enbridge plan  
23 membership, is a closed plan and has no past service obligations (or assets) to start. The interest  
24 rate assumption used in the actuarial funding valuation of the Interim Plan is significantly lower  
25 than the rate used by Enbridge since it reflects a more conservative asset mix given the expected  
26 investment time horizon of the Interim Plan.

27 In particular, the interest rate used to determine the required cash contributions for the Interim Plan  
28 based on the initial funding valuation Mercer prepared was 2.45%. In comparison, based on

information provided during the due diligence process as part of the acquisition process, Mercer understood that Enbridge used an interest rate of about 6% in the funding valuation of its pension plan. A lower interest rate used for the Interim Plan means a higher pension cost (e.g. for every 1% lower interest rate assumption, the annual pension cost can be roughly 25% higher).

As a result of the timing of the acquisition and the differences of all the funding factors as described above, there is a difference of \$1,054,100 between the 2020 Budget costs and Actual costs. This variance is non-recurring, as Liberty plans to move the New Brunswick employees from the Interim Plan to a defined contribution plan effective October 1, 2020. Defined contribution plans are lower cost and more predictable and stable than defined benefit pension plans, which have much greater risk of cost variability due to interest rate and stock market risks. Moving to the defined contribution plan will greatly reduce the ongoing costs and revenue requirement as compared to the ongoing costs associated with the Interim Plan and the prior Enbridge defined benefit pension and defined contribution plans. The five-year average annual pension costs included in the regulatory budgets under the Enbridge plans was approximately \$810,000. In comparison, the amount budgeted for the Liberty defined contribution plan for 2021 is \$477,000, or a \$333,000 savings to customers in NB. This level of expense is expected to be relatively consistent, with little variability, moving forward beyond 2021.

Liberty is requesting a variance account for the \$1,054,100 difference in the amount budgeted for the 2020 pension cash contributions and the actual cash contributions for 2020. In order to alleviate pressure on rates, Liberty requests to amortize this amount over a five-year period, including \$210,820 in the 2021 revenue requirement for recovery.

When coupling the annual amortization of the proposed \$1,054,100 pension deferral with the \$477,000 cost of the defined contribution plan, the total 2021 cost is \$687,820, or a \$122,180 savings as compared to the average of the Enbridge plans. The table below illustrates the savings.

1	Interim Plan 2020 costs in excess of amount in rates	\$ 1,054,100
2	Proposed 5-year Amortization	5
3	Annual expense of Interim Plan for 2021-2025	\$ 210,820
4	2021 cost of Defined Contribution Plan	\$ 477,000
5	Total cost of Liberty Plans	\$ 687,820
6	Average cost of Enbridge Defined Contribution and Defined Benefit Pension Plans	\$ 810,000
7	Annual Savings under new Liberty Plan	\$ 122,180

Given the expected ongoing savings as compared to the Enbridge plans costs, including the effect of amortizing the additional 2020 costs over five years, Liberty deems it appropriate and cost justified to create a variance account to defer and recover this unanticipated difference over a five year period.

Liberty's transactions in this proposed variance account will be reported on in future rate applications. No carrying charges will be applied to this variance account.

### **Variance Account for COVID-19**

On March 19, 2020, the Province of New Brunswick declared a state of emergency under the *Emergency Measures Act* and issued a mandatory order in response to the threat posed by COVID-19 to public health and safety. As with similar measures taken by other provinces and governments around the world, New Brunswick's state of emergency and mandatory order are having profound impacts on the daily lives of all New Brunswickers, as well as on New Brunswick-based businesses and other organizations. This is an unprecedented world event that is resulting in unprecedented actions.

As a result of the threats posed by COVID-19 to public health, public safety and the economy, a number of utilities across North America immediately altered their policies related to customer disconnections, late payment fees, late charges, etc. in order to provide relief for customers. Additionally, these same utilities also incurred additional safety protocol expenses related to additional supplies, equipment, procedures.

Liberty is requesting approval of a COVID-19 variance account in order to recover costs related to the following items:

- Incremental costs including Bad Debts
- Additional safety supplies such as masks, hand sanitizer, Tyvek suits
- Additional office cleaning costs for all three locations
- Incremental lost revenues resulting from actions taken to provide relief to customers including uncharged Late Payment Fees

Liberty requests approval of the variance account to recover 2020 and 2021 expenses at this time. Amortization into revenue requirement to be determined at a future proceeding in order to assess all revenue requirement items and determine the most appropriate term in order to lessen the impact to ratepayers.

The table below provides details related to expenses incurred to date including a Forecast to the end of the year.

### COVID-19 Related Expenses and Lost Revenue

June 30, 2020  
(\$ actual)

	Actuals				June Total Actuals	Forecast							Total
	March	April	May	June		July	August	September	October	November	December	Total Forecast	
<b>Expenses:</b>													
Safety Related Supplies	0	40,558	45,459	10,977	96,994	4,333	4,333	3,333	3,333	3,333	3,333	22,000	118,994
Regional Allocation	0	18,697	28,471	388	47,556	0	0	0	0	0	0	0	47,556
Subtotal	0	59,255	73,930	11,365	144,550	4,333	4,333	3,333	3,333	3,333	3,333	22,000	166,550
<b>Lost Revenue:</b>													
Late Payment Penalties waived	26,717	40,643	36,379	29,985	133,723	33,431	33,431	16,715	16,715	16,715	16,715	133,723	267,445
Subtotal	26,717	40,643	36,379	29,985	133,723	33,431	33,431	16,715	16,715	16,715	16,715	133,723	267,445
<b>TOTAL</b>	<b>\$ 26,717</b>	<b>\$ 99,898</b>	<b>\$ 110,309</b>	<b>\$ 41,350</b>	<b>\$ 278,273</b>	<b>\$ 37,764</b>	<b>\$ 37,764</b>	<b>\$ 20,049</b>	<b>\$ 20,049</b>	<b>\$ 20,049</b>	<b>\$ 20,049</b>	<b>\$ 155,723</b>	<b>\$ 433,995</b>

Liberty's transactions in this proposed variance account will be reported on in future rate applications. Carrying charges will be applied to this variance account at the short term borrowing rate which is currently at 2%.