



EB-2012-0052

IN THE MATTER OF the *Ontario Energy Board Act, 1998*,
S.O. 1998, c.15, Schedule B;

AND IN THE MATTER OF an application by Centre
Wellington Hydro Ltd. for an order or orders to dispose
Account 1562 – Deferred Payments in Lieu of Taxes
("Deferred PILS").

BEFORE: Karen Taylor
Presiding Member

Cynthia Chaplin
Vice Chair and Member

DECISION AND FINAL RATE ORDER **July 26, 2012**

Background

On December 23, 2010, the Board issued its Decision on the Combined PILS proceeding EB-2008-0381 ("Combined PILS Decision"). The Board indicated that the remaining distributors will be expected to apply for final disposition of Deferred PILS with their next general rates application, either IRM or cost of service.

The Board also indicated in the Combined PILS Decision that if the distributor files evidence in accordance with the various decisions made in the course of the Combined PILS proceeding, including the use of the updated SIMPIL model, the determination of the final account balance will be handled expeditiously and in a largely administrative manner. However, if a distributor files on a basis which differs from what is contemplated by the Combined PILS Decision, the application can take some time to

process, and therefore should not be included in an IRM application. Deviations from the Combined PILS Decision could include taking a different position on issues considered by the Board in the Combined PILs proceeding, addressing issues not arising in the Combined PILs proceeding or filing older SIMPIL models rather than the updated models containing the Excel worksheet 'TAXREC 3' as used by Halton Hills Hydro Inc.

Centre Wellington Hydro Ltd. ("CWHL") filed its Deferred PILs claim as part of its 2012 Incentive Rate Mechanism ("IRM") Application (EB-2011-0160), dated September 28, 2011. The Board determined that CWHL's application was not consistent with the various decisions made in the course of the Combined PILS proceeding. The inconsistencies identified related to use of tax rates in the true-up calculations that are not supported by the tax return evidence filed, the possible inclusion of regulatory assets in the true-up calculations and that the SIMPIL models were not balanced to tax returns in all years.

Therefore, the Board did not hear the request for disposition of Deferred PILs as part of CWHL's 2012 IRM application and noted that it would consider it on a stand-alone basis in a separate application which CWHL was expected to file by no later than April 1, 2012.

The Application

CWHL filed its stand alone Deferred PILs application on April 2, 2012. CWHL proposed a two-year disposition period. The Board assigned the application file number EB-2012-0052.

The Board issued a Notice of Application and Hearing and Procedural Order No.1, dated April 26, 2012, granting intervenor status and cost eligibility to the intervenors of record in CWHL's 2012 IRM proceeding. The Board noted that the Vulnerable Energy Consumers Coalition ("VECC") and School Energy Coalition ("SEC") were granted intervenor and cost eligibility status in the IRM proceeding.

The Deferred PILs evidence filed by CWHL in this proceeding includes tax returns, financial statements, Excel models from prior applications, calculations of amounts recovered from customers, SIMPIL¹ Excel worksheets and continuity schedules that

¹ Spreadsheet implementation model for payments-in-lieu of taxes

show the principal and interest amounts in the Deferred PILs balance. In pre-filed evidence CWHL applied to refund to customers a credit balance of \$190,313.54 consisting of a principal credit amount of \$163,068.80 plus related carrying charges of \$27,244.74.

Interest Expense

In response to Board staff IR #2, CWHL indicated that the interest expense, as reported in its audited financial statements, was comprised of interest on the note payable to the Township of Centre Wellington, interest on customer deposits, the fee for an IESO letter of credit and carrying charges on regulatory liabilities.

In its submission, Board staff submitted that interest on customer deposits should not be included in the excess interest claw-back calculations. Board staff submitted that CWHL should file revised SIMPIL models that include the removal of interest on customer deposits in interest expense.

In its reply submission, CWHL agreed with Board staff that interest on customer deposits should be excluded from the excess interest claw-back calculation and filed revised evidence reflecting that change.

Income Tax Rates

In response to Board staff IR #4c, CWHL noted that it did not use actual taxable income to calculate the income tax rates in 2001 and 2002 because it had incurred tax losses. CWHL also indicated that it did not use actual taxable income to calculate the income tax rate in 2003 as it carried forward the losses from the previous year to reduce taxable income in 2003. CWHL stated that actual taxable income could not be used in those years as the value was either negative or distorted.

In response to Board IR #4d, CWHL noted that it believed the hybrid approach that it proposed to be appropriate. CWHL noted that the goal of the approach was to determine a tax rate that approaches the actual tax rate that would have been used had CWHL had taxable income in 2001, 2002 and 2003. CWHL stated that in order to do so an estimate of actual taxable income would be required which is why regulatory net income was used as a proxy for the actual taxable income to indicate the level of income expected to be achieved by the utility over those years.

Board staff submitted that a proper regulatory approach would use rate base as the proxy for taxable capital, regulatory taxable income and the tax return forms for 2001 through 2005 to calculate the blended income tax rates. Board staff noted that were CWHL to follow this method, there would be no business limit reduction since rate base as the proxy for taxable capital is less than \$10 million. Board staff submitted that using actual taxable capital which results in the business limit reduction should also require the use of actual taxable income to be internally consistent. CWHL did not have taxable income for 2001 and 2002 due to tax losses, but did have taxable income for 2003-2005.

Board staff submitted that a consistent approach would be more appropriate for the income tax rate calculations. Board staff submitted that, as CWHL considers the actual tax return approach to be inappropriate in 2001 and 2002 and distorted in 2003, that CWHL should consider using the regulatory approach of using rate base as the proxy for taxable capital and regulatory taxable income for the tax years 2001 through 2005 ("Scenario A"). Alternatively, Board staff suggested that CWHL consider using the minimum income tax rates as identified in the Combined PILs Decision ("Scenario B"). Board staff submitted that CWHL should file SIMPIL models for 2001-2005 and a revised continuity schedule for each of the two suggested scenarios in its reply submission.

CWHL filed revised evidence for each of the two scenarios requested by Board staff.

CWHL acknowledged Board staff's concern over the consistency of the approach used to calculate the income tax rates but stated that consistency should not be sought at the expense of accuracy. CWHL stated that rate base is not an appropriate proxy for taxable capital because it does not result in the use of the applicable legislated tax rate for the purposes of the true-up calculation in the SIMPIL models.

Regarding Board staff's proposed approach of using the minimum tax rates from the Combined PILs Decision, CWHL noted that it is not a small enough distributor that it can use the minimum tax rate on its tax returns and is not entitled to the full small business deduction. CWHL stated that the use of the minimum tax rates for 2001-2005 results in inaccurate true-ups and strongly objected to the use of that methodology.

CWHL also proposed a revised hybrid methodology as another option for the Board to consider ("Scenario C"). Under this hybrid approach, a regulatory model is used to

determine the tax rates in 2001, 2002 and 2003 and an “actual” model (i.e. based on actual taxable income) is used to determine the tax rates in 2004 and 2005.

CWHL requested that the Board approve the tax rates as determined in its application. Were the Board to find the use of the tax rates proposed in its application objectionable, CWHL requested that the Board consider the revised hybrid approach it proposed in its reply submission (Scenario C).

VECC and SEC did not file interrogatories or submissions.

The tables below summarize the refunds to rate payers and income tax rates for 2001-2005 under each of the scenarios discussed in Board staff’s and CHWL’s submissions.

Table 1

Refunds to Customers	
Original Evidence: Actual taxable capital and regulatory taxable income is used for each year to determine the income tax rates.	190,314
Scenario A: Rate base is proxy for taxable capital and regulatory taxable income is used to determine the income tax rates.	267,652
Scenario B: Rate base is proxy for taxable capital and minimum tax rates are used.	434,852
Scenario C: Rate base used as taxable capital in 2001-2003 and regulatory taxable income. Actual taxable capital used in 2004-2005 and actual taxable income.	215,023

Income Tax Rates					
Scenario	2001	2002	2003	2004	2005
Original evidence	32.13%	29.91%	27.18%	24.59%	24.93%
Scenario A	32.13%	28.56%	24.91%	21.28%	20.29%
Scenario B	19.12%	19.12%	18.62%	18.62%	18.62%
Scenario C	32.13%	28.56%	24.91%	24.59%	24.93%

Board Findings

The Board finds that it is appropriate to use a consistent regulatory approach to determine the disposition balance for Account 1562. As set out Table 1, the consistent regulatory approach, or Scenario A, uses rate base as a proxy for taxable capital and regulatory taxable income to determine the applicable income tax rates for all years. From a ratemaking perspective, the Board is concerned with regulated balances, not balances that are constructed for taxation purposes. Tax accounting and regulatory accounting have different purposes and from a rate making perspective, the Board is concerned with the latter and not the former.

The Board notes that Account 1562 is not to be used to true-up PILs proxy amounts collected with the PILs amounts actually paid - rather, Account 1562 is to be used to track the difference between the amount of the 2001 PILs and 2002 PILs proxies included in rates and the actual amounts recovered from customers.

The Board finds that the hybrid approach, Scenario C, is inappropriate because it is asymmetric in favour of the utility and inconsistent with the purpose of Account 1562. Under Scenario C, customers would not get a credit for years one to three when no actual taxes were paid, and in years four and five, when actual taxable capital is greater than rate base, the effective actual tax rate is higher than what would have been allowed in rates.

The Board also finds that, based on the evidentiary record for the proceeding, the use of the consistent regulatory approach to determine taxation rates for the purposes of the true-up is more appropriate than the use of minimum taxation rates put forth as an alternative by Board staff.

The Board notes that CWHL agreed with Board staff that interest on customer deposits should be excluded from the interest claw-back calculation and that this change has been reflected in the revised evidence filed by CWHL.

The Board approves the disposition of a credit balance of \$267,652 in Account 1562.

Implementation

In order to minimize the number of intra-period rate changes, the Board finds that it is appropriate to align the term of the disposition rate rider with CWHL's 2014 IRM application. The Board approves the disposition of a \$267,652 credit balance in Account 1562 over a 21 month period, commencing August 1, 2012 and ending April 30, 2014.

Cost Awards

VECC and SEC were found to be eligible for an award of costs. However, neither party participated in the proceeding, and therefore the Board will not award costs to either party.

THE BOARD ORDERS THAT:

1. CWHL shall file with the Board, and shall also forward to VECC and SEC, a draft Rate Order attaching a proposed Tariff of Rates and Charges reflecting the Board's findings in this Decision and Order, within **7 days** of the date of this Decision and Order. The draft Rate Order shall also include customer rate impacts and detailed supporting information showing the calculation of the final rates.
2. VECC, SEC and Board staff shall file any comments on the draft Rate Order with the Board and forward to CWHL within **5 days** of the date of filing of the draft Rate Order.
3. CWHL shall file with the Board and forward to VECC and SEC responses to any comments on its draft Rate Order within **3 days** of the date of receipt of the submission.
4. CWHL shall pay the Board's costs incidental to this proceeding upon receipt of the Board's invoice.

All filings to the Board must quote file number **EB-2012-0052**, be made through the Board's web portal at, www.errr.ontarioenergyboard.ca and consist of two paper copies and one electronic copy in searchable / unrestricted PDF format. Filings must clearly state the sender's name, postal address and telephone number, fax number and e-mail

address. Parties must use the document naming conventions and document submission standards outlined in the RESS Document Guideline found at www.ontarioenergyboard.ca. If the web portal is not available parties may email their document to the address below. Those who do not have internet access are required to submit all filings on a CD in PDF format, along with two paper copies. Those who do not have computer access are required to file 2 paper copies.

DATED at Toronto, July 26, 2012

ONTARIO ENERGY BOARD

Original Signed By

Kirsten Walli
Board Secretary