

June 10, 2009

Ms. Kirsten Walli
Board Secretary,
Ontario Energy Board
2300 Yonge Street, Suite 2700
P.O. Box 2319
Toronto, Ontario M4P 1E4

Via RESS and by courier

Dear Ms. Walli:

Re: EB - 2007- 0820: Account 1562 Deferred Payments in Lieu of Taxes

The Electricity Distributors Association (EDA) is the voice of Ontario's local distribution companies (LDCs). The EDA represents the interests of over 80 publicly and privately owned LDCs in Ontario.

The EDA has consulted with its members through the EDA's Finance Council on the issue of further procedural steps that this proceeding should take. The attached comments summarize the consensus reached by the members on this subject.

The relevant regulatory principles and precedents quoted in the attachment were provided, at the request of the EDA, by Ms. Kathleen McShane, President, Foster Associates, Inc.

Yours truly,

"original signed"

Maurice Tucci
Policy Director, Distribution & Regulation

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EDA's Recommendations on Further Procedural Steps for The Combined Proceeding - Disposition of Account 1562 Balances

Background

The Ontario Energy Board (the "Board") announced a combined proceeding in March 2008 to determine the methodology to be used for the calculation and disposition of balances in account 1562 – Deferred PILs. The combined proceeding is expected to determine accurate balances in account 1562 for the cost of service applicants that have requested disposition of account 1562 in their 2008 rate applications. In addition, the combined proceeding is expected to provide guidance for the remaining distributors (LDCs) for use in their subsequent applications.

In August 2008, the Board staff issued a discussion paper summarizing the principles established by the Board to date with respect to the determination of the account 1562 balances and also identified matters that require clarification. Later in January 2009, the intervenors reviewed the staff discussion paper and submitted their responses to the issues raised in the paper.

In November 2008, the Board nominated three LDCs as applicants to this proceeding and directed them to file evidence regarding their account 1562 balances.

In January 2009, a technical conference was held for the purpose of reviewing outstanding matters. Participating utilities at the conference emphasized that they had followed the filing guidelines and instructions as promulgated by the Board from time to time with respect to this account and making any changes to the underlying principles retroactively is absolutely unfair. On the other hand, some participants recommended that the Board should consider making a decision on the principles underlying the models and guidelines pertaining to this account before considering disposition of the account balances.

Subsequently, the Board staff and the intervenors submitted interrogatories to the applicants in February 2009 for seeking clarifications on the evidence submitted by them. The applicants filed their responses to the interrogatories in May 2009.

EDA's Recommendation on Further Procedural Steps

The EDA has reviewed the interrogatory responses submitted by the applicants and concluded that the applicants indeed have used a variety of interpretations of the available guidance in submitting their SIMPIL models in the past. PILs were new to the industry, during the time period under discussion, and LDCs prudently interpreted the methodology and completed their filings. PILs is a complex issue that requires detailed guidelines, as were implemented in the 2006 EDR Handbook.

Further, the EDA came to the conclusion that it would be highly difficult for the Board to deal with the disposition of 1562 account balances because of differing interpretations of the guidance provided by the staff in the past. Therefore, the EDA recommends taking the following steps in this combined proceeding:

1. The Board staff, with the assistance of the feedback already provided by intervenors and the applicants, should prepare a position paper on all outstanding matters identified in the staff paper as requiring clarification. In doing so, the Board staff should ensure that the assumptions made while building the SIMPIL models in the past are in no way changed. The Board staff should be mindful of the fact that changing the assumptions (on which the SIMPIL models were built) will amount to rebuilding the SIMPIL models retroactively. However, furnishing amplification to the guidance that was already provided in those years (2001 to 2005) would ensure consistent interpretation by all LDCs in the same manner.
2. The intervenors and the applicants may be afforded another opportunity to provide their feedback on the matters that have been clarified in the position paper.
3. Informed by the feedback provided by intervenors, applicants and the staff, the Board will make a decision on all the identified outstanding issues. However, the Board should be mindful that the methodology used by the Board staff in preparing the SIMPIL model is underpinned by certain principles which should not be changed retroactively. Further, the EDA recommends that the Board adopt the following principles, which were established by

the Board itself in previous proceedings, for making a decision on all the outstanding issues related to disposition of Account 1562.

- a) **Prohibition against retroactive ratemaking.** The Board has on numerous occasions accepted as a fundamental principle that retroactive ratemaking is to be avoided, for example, in its Decision for Union Gas in EB-2005-0211/EB-2006-0081, citing *Northwestern Utilities Ltd. v. City of Edmonton*, (1979) 1 S.C.R. 684 at 699.

In RP-2005-0013/EB-2005-0031, Decision and Order, Great Lakes Power, February 2006, the OEB concluded:

“As the Board has stated in numerous cases, the Board does not endorse retroactive ratemaking. The Board must be mindful of the negative implications of retroactive rates. When investors and consumers cannot be assured that final rates are indeed final, the resultant risks increases costs for everyone. In addition, intergenerational inequities arise, with today’s consumers paying the costs of past events. In this case, it is not appropriate for either the utility or its ratepayers to bear the implications of a retroactive rate change. To burden the utility would be contrary to the regulatory compact. To burden the ratepayers would be wrong, especially given the length of the retroactivity.” (page 7)

In the same decision the OEB stated:

“The Ontario Energy Board Act, 1998 does not contain any provisions that deal specifically with retroactive ratemaking, and the Board is therefore not empowered to alter a final rate order retroactively. Furthermore, the Act requires that balances in deferral accounts should be reviewed by the Board at least annually. We infer from this that there is a policy against adverse impacts and inter-generational inequity that might be caused by out-of-period rate adjustments.” (page 8)

Final balances in the accounts to be disposed of should not reflect retroactive ratemaking. Specifically, the methodologies which were adopted for the purpose of past rate years should not be retroactively altered, e.g., by implementing a new model in 2009 which would be used to re-determine balances in Account 1562 which date from models and guidance implemented and relied upon by the distributors in prior rate years.

- b) **Prudence should not be judged with 20/20 hindsight.** The determination of the final balances in Account 1562 should be based on the Board's definition of prudence. Any finding of imprudence with respect to cost recovery must be based on information that could have reasonably been available at the time. In RP-2005-0013/EB-2005-0031, Decision and Order, Great Lakes Power, February 2006, the OEB stated:

“The Board addressed the prudence test in its Decision in the Enbridge case regarding the prudence of the Alliance contracts (footnote omitted).

The test is well known but its worth repeating in the context of these proceedings. The first principle is this; when a utility makes decisions in operating its business, the regulator assumes that those decisions, whether they relate to investments or otherwise, are prudent. In other words, there is a burden on those challenging the prudence to demonstrate, on reasonable grounds, that there has been a lack of prudence.

The second principle is that, in analysing whether the utility was prudent or not, the Board must look at the facts and circumstances that were known or ought to be known to the utility at the time the decision was made. In other words, hindsight should not be used to determine prudence.” (page 20)

- c) **Avoidance of single issue ratemaking.** In EB-2007-0663, Decision and Order, Welland Hydro, December 24, 2007 with respect to Welland Hydro's request for an adjustment to 2007 rates to reflect the elimination of historical loss-carry forwards and to adjust 2007 rates to reflect a “normal” level of PILs expense, the Board noted that:

“SEC views the application as a single-issue rate adjustment and suggests that on that basis it should be rejected. The Board is mindful of selectivity and does not condone it.” (page 4)

The issue of selectivity arises specifically with respect to consideration of the retention in rates during 2003 and 2004 of a 15 month provision for PILs expense due to the imposition of the rate freeze required by Bill 210. Due to the rate freeze, the distribution utilities were effectively deprived of the opportunity to earn a fair return. To single out the ‘15 month provision for PILs expense’ during the rate freeze period, without due consideration of other elements of the revenue requirement which the distributors did not receive, would constitute unreasonable selectivity.

d) **The stand-alone principle.** PILs expenses should be based on the revenues, costs and expenses associated only with the distribution activities, as indicated in the OEB Staff Discussion Paper: Account 1562-Deferred Payments in Lieu of Taxes. The stand-alone principle was, as per the Staff Discussion Paper, affirmed by the first PILs instructions issued in 2001, articulated in the Report of the Board in RP-2004-0188 and set out in the 2006 Electricity Distributors Rate Handbook. The applicability of the stand-alone principle to the determination of the PILs expense to be included in rates extends to the determination of balances in Account 1562.

4. Once the Board's decision is available, the applicants may be asked to refile SIMPIL models in accordance with the Board's decision, and the balances can then be disposed of after verifying that the models filed accurately represent the account balances.
5. The remaining LDCs seeking disposition of account 1562, should also be directed to refile their SIMPIL models in accordance with the Board's decision.