

Appendix B

Filing Guidelines for PILs Proxy

In reviewing the comments by stakeholders on the draft PILs spreadsheet previously posted on the Board's website, the Board makes the following comments.

In terms of the overall design of the PILs provision under first generation PBR, the Board wishes to reaffirm that:

- PILs will continue to be treated as a pass-through, as indicated in the Rates Handbook and by the Board in its correspondence of August 24, 2001.
- PILs will continue to be calculated on a flow-through basis, consistent with the Board's decision setting Hydro One's initial rate revenue requirement RP-1998-0001.
- Provision for PILs will be assessed on a stand-alone basis, consistent with the Board's practice in the natural gas industry.

The Board has decided that certain modifications should be made to the draft PILs spreadsheet issued for comment on December 5, 2001 (which is now superseded), including:

- The instructions regarding treatment of the interest deduction have been changed to ensure utilities that move to the capital structure authorized in the Rates Handbook at an early stage are not penalized.
- The instructions regarding the calculation of capital taxes have been clarified, so that parties understand that the full capital tax exemptions must be claimed by the regulated corporate entity (although allocation can occur between wires and non-wires activities undertaken by the regulated corporate entity).
- The instructions regarding the calculation of EBIT in 2002 onwards will not contain any reference to an IPI-X adjustment, since the 1st generation PBR is a price cap rather than revenue cap and earnings are not directly impacted by a price adjustment.

On December 21, 2001 the Board will post on its website (www.oeb.gov.on.ca) under "What's New?" the approved revised worksheet, entitled Spreadsheet Implementation Model For PILs ("SIMPIL").

The spreadsheet provides a consistent methodology for calculating both a 2001 and 2002 PILs amount for inclusion in the upcoming March 1, 2002 rates adjustment. In general, the methodology employs the wires-only earnings before interest and income ("EBIT") used in the establishment of the utility's unbundled rates, adjusted for incremental income associated with the implementation of MARR and for certain mandatory additions and deductions to determine income-related PILs. Capital-related PILs uses wires-only rate base, adjusted for exempt amounts.

The total PILs calculation consists of income taxes, Ontario Capital Tax and federal Large Corporations Tax ("LCT"). The LCT and income taxes are not deductible in computing income tax, therefore these tax amounts will be grossed up to permit the pass-through referred to in the Electricity Distribution Rate Handbook. By contrast, Ontario Capital Tax is a deductible expense for both Federal and Ontario income tax purposes; therefore, the actual amount (without gross-up) is the pass-through.

The attached comments and notes to the spreadsheet provide detailed, step-by-step instructions and should be reviewed carefully. The footnotes/explanations have been supplemented with document files containing a sample of a utility's filing sequence for 2001 and 2002 (in six parts), to assist utilities in their own preparation of the filing material. Utilities should consult their own tax advisors to determine how to complete a PILs calculation for Ministry of Finance purposes (for which a different set of rules are applicable).

The worksheet represents a full cycle filing requirement for PILs (over an 18 month period), from the inclusion of PILs in rates, to the deferral account allowance entry calculation, to the tax authority filing details (which will be used to support the "true-up" deferral account entry).

The blank spreadsheets provided are generic. Utilities should copy the spreadsheet once to prepare a 2001 PILs deferral account allowance, and make a second copy to create a 2002 PILs proxy for inclusion in the rate adjustment model.

In the workbook, there are three blank worksheets entitled "REGINFO", "TAXCALC" and "TAXREC". It is recommended that one workbook be created for 2001 and one for 2002. Different columns will be completed at different times during the period from now through June, 2003.

Utilities should then file, as part of their March 1, 2002 rates application, 6 hard copies of the 2001 and 2002 PILs spreadsheets, as well as an electronic copy of each on disk. The PILs worksheets will form part of the evidentiary material to be considered by the Board in order to approve just and reasonable rates for the rate year starting March 1, 2002. The resulting 2001 and 2002 PILs amounts should be entered in the appropriate sheet in the RAM Model as outlined in Appendix "A" and submitted to the Board no later than January 25, 2002.

Should you have questions regarding the PILs worksheets, please contact Duncan Skinner (416-440-8127 or skinnedu@oeb.gov.on.ca) or John Vrantsidis (416-440-7613 or vrantsjo@oeb.gov.on.ca).

Please note that the model is designed to address PILs imposed under section 93 of the *Electricity Act*. Contact the above staff regarding how it should be applied in the case of utilities paying proxy taxes under different rules, or paying regular corporate taxes.