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January 21, 2011

Ontario Energy Board
2300 Yonge Street
P.O. Box 2319
Suite 2700
Toronto ON M4P 1E4

Attention: Ms Kirsten Walli
Board Secretary

Dear Ms. Walli:

Re: In the matter of a proceeding commenced by the Ontario Energy Board on its own motion to determine the accuracy of the final account balances with respect to account 1562 Deferred PILs (for the period October 1, 2001 to April 30, 2006) for certain 2008 and 2009 distribution rate applications before the Board
Board File: EB-2008-0381

With reference to above-noted matter, attached please find submissions filed on behalf of the Coalition of Large Distributors on Issue 10.

Sincerely,

George Vegh
GV:MAB
Att
c: Invenors on file

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

AND IN THE MATTER OF a proceeding commenced by the Ontario Energy Board on its own motion to determine the accuracy of the final account balances with respect to account 1562 Deferred PILs (for the period October 1, 2001 to April 30, 2006) for certain 2008 and 2009 distribution rate applications before the Board.

SUBMISSIONS BY THE COALITION OF LARGE DISTRIBUTORS ON ISSUE 10

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PART I: Introduction and Summary

1. These are the submissions of the Coalition of Large Distributors, namely Enersource Hydro Mississauga Inc., Horizon Utilities Corporation, Hydro Ottawa Limited., PowerStream Inc., Toronto Hydro-Electric System Limited and Veridian Connections Inc. (the "CLD"[1]) on Issue 10, which reads as follows:

> "How should the continued collection of the 2001 PILs amount in rates be considered in the operation of the PILs deferral account?"

2. The CLD submits that the 2001 PILs amounts themselves were approved in final orders for 2002 and thus were maintained until they were replaced in subsequent rate orders. The Board does not have the jurisdiction to retroactively deny recovery of the Board-approved 2001 PILs amounts.

3. However, the Board may dispose of the net differences between the deferred PILs amounts approved in rates and the amounts billed to customers for the period 2002-2004.

4. Board staff final submissions acknowledge that these amounts were approved in 2002 distribution rates, and "not by a separate rate rider with a sunset date for removal in rates. As such, Board staff is of the view, on a preliminary basis, that the Board-approved rates continued to be in force until the Board changed those rates in 2004."[2] This is consistent with the description of the purpose of Account 1562 in the Board staff discussion paper that accompanied the launch of this review as "designed to track and record: The variances resulting from the difference between the Board approved PILs amount and the amount of actual billings that relate to the recovery of PILs."[3]

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[1] References to CLD members include their predecessors.
[2] Board Staff Submission on the Unsettled Issues, December 24, 2010, Issue 10, p. 7.
[3] Staff Discussion Paper, Account 1562 – Deferred Payments in Lieu of Taxes: Methodology and Disposition of Balances for Electricity Distribution Companies affected by section 93 of the *Electricity Act, 1998*, EB-2007-0820

PART II: The Jurisdictional Issue – the 2002 Rate Orders and the Board-approved PILs Amounts.

5. The OEB issued orders setting distribution rates for CLD members (and all other distributors) for the 2002 rates year[4] All of these orders:

    - included an allowance for the 2001 Board-Approved PILs amount in base distribution rates;
    - were final in nature; and
    - remained in effect until changed by subsequent rate orders.

6. These orders, like many of the decisions made by the OEB in the period 2000-2001, were made on the assumption that the Board would continue to have general uninterrupted rate setting authority for distributors. When the 2002 rates were set, the Board and the sector expected that there would be several adjustments to revenue requirements in future rate orders, the first of which would have been effective in 2003. These adjustments would have included the determination of a new PILs amount and the third instalment of the market adjusted revenue requirement ("MARR").

7. The Bill 210 rate freeze prevented these adjustments from taking place as planned. Electricity distributors experienced considerable financial detriment because rates that were expected to be in place only for the 2002 rates year were in place for a longer period than that – the foregone revenue adjustment representing the third MARRs instalment

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(the "Staff Paper), at p. 5. See also p. 3, where the Staff Paper states that the purpose of the account is to track "The total difference between the expected amount included in rates and the amount collected." (emphasis added).

[4] The rate orders are: Toronto Hydro-Electric System Limited, February 26, 2002 (RP-2002-0002; EB-2002-0011); Hydro Ottawa Limited, March 7, 2002 (RP-2002-0051); PowerStream Inc. (Comprised by Aurora Hydro (RP-2002-0061; EB-2002-0070), Markham Hydro (RP-2002-0079; EB-2002-0088), Richmond Hill Hydro (RP-2002-0083); EB-2002-0092); Hydro Vaughan (RP-2002-0056; EB-2002-0065), and Barrie Hydro (RP-2002-11; EB-2002-20)); Horizon Utilities Corporation (comprised of Hamilton Hydro (RP-2002-0014; EB-2002-0023) and St. Catherines Hydro (RP-2002-0045; EB-2002-0054)); Enersource Hydro Mississauga Inc. (RP-2001-0084; EB-2002-0093); Veridian Connections Inc. (comprised of Veridian Connections Inc. (RP-2002-0075; EB-2002-0084); Gravenhurst Hydro Electric Inc. (Interim Order effective June 1, 2002 (made final by the operation of Bill 210) (RP-2002-0060; EB-2001-0069); Brock Hydro (RP-2002-0099; EB-2002-0108); Port Hope Hydro (RP-2002-0076; EB-2002-0085); Belleville (RP-2002-0074; EB-2002-0083); and Scugog Hydro Energy Corporation RP-2002-0065; (RP-2002-0074)); CLD Exhibits, 20100209.

totalled approximately $78 million for CLD members alone. However, the law does not allow the Board to go back and readjust the gains and losses of distributors and ratepayers to reflect what the expectations would have been if the Board did have the power to set new rates during the rate freeze period. As a corollary of this, the Board cannot selectively go back and "cherry pick" which gains and losses it would like to readjust.

8. Under the Board's statutory jurisdiction, historic gains and losses incurred pursuant to final rate orders cannot be revisited in subsequent orders. This restriction follows from two unambiguous principles of law that apply to rate orders:

    1. Final rate orders remain in place until changed by subsequent rate orders; and

    2. Subsequent rate orders can only operate on a prospective basis.

    Each of these principles will be addressed in turn.

1. Final Rate Orders Remain in Effect until Changed by Subsequent Rate Orders

9. The 2002 rate orders were final orders, not interim orders. As a result, the rates they approved remained in place, and could not be changed, until replaced by a subsequent order. The fact that the Board's ability to make such an order was legally restricted by Bill 210 does not take away from the finality of the 2002 rate orders that it did make. Regardless of what expectations are when a final order is made, rates approved by that order remain in place until changed by a subsequent order.

10. In *Northwestern Utilities Ltd.* v. *Edmonton*,[5], the Supreme Court of Canada approved of the following statement of the Alberta Court of Appeal in *City of Calgary and Home Oil Co.* v. *Madison Natural Gas Co.* (1959), 19 D.L.R. (2d) 655 (at 661): "The powers of the Natural Gas Utilities Board have been quoted above and the Board's function was to determine 'the just and reasonable price' or prices to be paid. It was to deal with rates prospectively and having done so, so far as that particular application is concerned, it

[5] [1979] 1 S.C.R. 684

ceased to have any further control. To give the Board retrospective control would require clear language and there is here a complete absence of any intention to so empower the Board" (emphasis added).

11. It is this finality that distinguishes a final order (such as the 2002 rate orders) from an interim order. As the Supreme Court of Canada stated in *Bell Canada* v. *CRTC*[6], "one of the differences between interim and final orders must be that interim decisions may be reviewed and modified in a retrospective manner by a final decision....It is the interim nature of the order which makes it subject to further retrospective directions" (emphasis added).

12. The Board has recognized and applied the legal distinction between final and interim orders and has noted that, when obtaining a final order, "A party...would have the certainty that a final order will not be reviewed later by the Board."[7]

13. More recently, in setting rates for Barrie Hydro Distribution Inc. effective 2009, the Board agreed that changes in PILs calculations that occurred during the year in which a final rates order governed (2008), could not be taken into account for the period covered by that rate order: "the additional amounts Barrie collected in the 2008 rate year should remain with Barrie, as it appropriately reflected the Board Decision (EB-2007-0746) for that rate year."[8]

14. Similarly, in setting an order fixing Enersource Hydro Mississauga Inc.'s 2009 distribution rates, the Board agreed with Board staff's submission that "once the Board issues its final rate order in this case, the proceeding is over and the current panel does not have the power to declare these same rates interim at a later date."[9]

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[6] [1989] 1 S.C.R. 1722
[7] Notice of Proceeding in RP-2004-0203, October 5, 2004.
[8] EB-2008-0160, p. 4.
[9] EB-2008-0171, p. 6.

2. Subsequent Rate Orders Only Operate on a Prospective Basis

15. A rate order may only be prospective in nature. It cannot be used to "recapture" over or under earnings during a period in which a previous rate order was in place. Applying that here, the Board is not in a position today to recover any "over earnings" (or conversely to compensate distributors for "under earnings" resulting from the loss of their third MARRs adjustment) during the period that the 2002 rate orders were in place.

16. This proposition was unequivocally put forward by a majority of the Supreme Court of Canada in *ATCO Gas & Pipelines Ltd. v. Alberta (Energy & Utilities Board)*:[10]

> "From my discussion above regarding the property interest, the Board was in no position to proceed with an implicit refund by allocating to ratepayers the profits from the asset sale because it considered ratepayers had paid excessive rates for services in the past. As such, the City's first argument must fail. The Board was seeking to rectify what it perceived as a historic over-compensation to the utility by ratepayers. There is no power granted in the various statutes for the Board to execute such a refund in respect of an erroneous perception of past compensation. It is well established throughout the various provinces that utilities boards do not have the authority to retroactively change rates (*Northwestern, 1979,* p. 691; *Re Coseka Resources Ltd. and Saratoga Processing Co.* (1981), 126 D.L.R. (3d) at p. 715, leave to appeal refused, [1981] 2 S.C.R. vii; *Re Dow Chemical Canada Inc.* (C.A.), at pp. 734-735). But more importantly, it cannot even be said that there was over-compensation: the rate-setting process is a speculative procedure in which both the ratepayers and the shareholders jointly carry their share of the risk related to the business of the utility (See MacAvoy and Sidak, at pp. 238-39)" (Emphasis added).

17. As a result, although the Board and the parties expected that rates approved in the 2002 rate orders would be revisited for new orders effective for the 2003 rate year, that expectation does not provide jurisdiction to go back now and change orders that approved those rates.

[10] [2006] S.C.J. No. 4, at para. 71.

3. The Relevance of Deferral Accounts

18. Because Account 1562 is a deferral account, it is helpful to address the legal characteristics of deferral accounts generally and how Account 1562 operated in this case.

19. The Board has defined deferral accounts as "accounting devices intended to allow an entity to capture and record in an identifiable location an aspect of operations, the final quantum and disposition of which is dependent on some future unknown event."[11]

20. Unlike final rate orders, deferral accounts do not create or alter legal rates. Thus, in establishing deferral accounts, the Board explicitly states that utilities are routinely "cautioned that this approval does not provide any assurance, either explicit or implicit, that the amounts recorded in the accounts will be recovered from rate payers."[12] By contrast, when it comes to final rates, the Board has stated that a utility "would have the certainty that a final order will not be reviewed later by the Board."[13]

21. This is recognized in the Supreme Court of Canada's decision in *Bell Canada v. Bell Aliant Regional Communications*.[14] That decision addressed the CRTC's authority to dispose of an earnings-sharing deferral account under an incentive regulation scheme. Specifically, the scheme created a formula that set rates and captured the difference between those rates (less productivity offset) and amounts actually collected. As the Supreme Court described it, the deferral account recorded "the difference between the rates *actually* charged, not including the decrease mandated by the Price Caps Decision formula [i.e., the offset], and the rates as *otherwise determined* through the formula."[15] The Supreme Court of Canada put it as follows:

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[11] See: Order setting 2007 and 2008 Transmission Rates for Hydro One, August 16, 2007 (EB-2006-0501), p. 5.
[12] See, for example, the Board's Decisions in the rate cases for Hydro One Networks, Inc. (EB-2009-0416) and Great Lakes Power Transmission (EB-2009-0409) as quoted from in the Board's August 26, 2010 Policy Statement in "Framework for Transmission Project Development Plans" (EB-2010-0059).
[13] Notice of Proceeding in RP-2004-0203, October 5, 2004.
[14] 2009 SCC 40.
[15] At paragraph 6.

"In my view, the credits ordered out of the deferral accounts in the case before us are neither retroactive nor retrospective. They do not vary the original rate as approved, which included the deferral accounts, nor do they seek to remedy a deficiency in the rate order through later measures, since these credits or reductions were contemplated as a possible disposition of the deferral account balances from the beginning."[16]

22. As a result, in that decision, the Court looked to the original order authorizing rate recovery to determine the rights and obligations of the utility. As the Court stated: "we are not dealing with the variation of final rates…[I]t was known at the outset that Bell Canada would be obliged to use the balance of its deferral account in accordance with the CRTC's subsequent direction."[17]

23. The distinction between final rates and deferral accounts that record actual revenues and expenditures is also illustrated in the approach of the Board and the Court in the *GLPL* decision. That case addressed whether GLPL was entitled to recover $2.8 million from a deferral account. The account was approved in an interim order that was made prior to the passage of Bill 210 (and that therefore became a final order as a result of Bill 210). The $2.8 million figure represented an amount that GLPL claimed to have foregone as a result of a voluntary rate mitigation plan. Although GLPL's initial rate application included a proposed revenue requirement of $12.7 million, which included the $2.8 million figure, the revenue requirement that was approved by the Board was for $9.8 million – which did not include $2.8 million. According to the Board, the fact that the order establishing the deferral account did not include a final revenue requirement was fatal to GLPL's case: "The GLPL distribution rates approved by the Board and attached as Appendix A to its May 13, 2002 Interim Decision and Order did not reflect a revenue requirement of $12.7 million."[18] The Court of Appeal agreed. It stated: "It is of significance that the 2002 order was interim in nature and approved the rates proposed by GLPL necessary to recover the $9.8 million."[19]

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[16] At paragraph 63.
[17] At Paragraph 61.

24. As a result, in the *GLPL* case the OEB refused recovery of amounts that were recorded in deferral accounts in an interim order and which were never included in a final rate order. It did not address the recovery of amounts approved in rates in a final rate order, which is the relevant situation respecting the 2001 Board-approved PILs amount.

25. In the context of Account 1562, none of the orders approving the recovery of the 2001 Board-approved PILs amounts suggested that the Board intended to provide subsequent direction on the disposition of these amounts.

26. The Board (and Board staff) have described the nature of Account 1562 on several occasions. They have always recognized that Account 1562 recorded differences between amounts approved in rates and actual amounts recovered from customers. A limited number of items, specifically identified in Board documents, were subject to a true-up. At no point was it ever suggested that Account 1562 would be somehow used to reverse the amount of the 2001 Board-approved PILs amount that were already approved for recovery in base distribution rates.

27. For example, the April 2003 "Accounting Procedures Handbook Frequently Asked Questions" states:[20]

> "The Deferred Payments in Lieu of Taxes Variance Account 1562 is established to track and record the variances that results from the difference between the Board approved PILs amount and the actual billings that relate to the recovery of PILs."

28. Similarly, the Staff Discussion Paper accompanying this proceeding described Account 1562 as follows:[21]

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[18] Great Lakes Power Limited Application for 2007 Rates (EB-2007-0744), October 30, 2008.
[19] Great Lakes Power Limited v. Ontario Energy Board (Court File No. 610/08), July 21, 2009, paragraph 37.
[20] April 2003 "Accounting Procedures Handbook Frequently Asked Questions", p. 1 (emphasis added).
[21] Staff Discussion Paper, Account 1562 – Deferred Payments in Lieu of Taxes: Methodology and Disposition of Balances for Electricity Distribution Companies affected by section 93 of the *Electricity Act, 1998*, EB-2007-0820 (the "Staff Paper), at p. 5 (emphasis added). See also p. 3, where the Staff Paper states that the purpose of the account is to track "The total difference between the expected amount included in rates and the amount collected." (emphasis added).

- "Entries to Account 1562 are designed to track and record:
    - The variances resulting from the difference between the Board-approved PILs amount and the amount of actual billings that relate to the recovery of PILs."

29. An account that tracks differences in amounts approved in rates and actual amounts recovered from customers cannot be used to change amounts that were approved in base distribution rates.

PART IV: Conclusion

30. In conclusion, for the reasons set out in Part II, the Board does not have the jurisdiction to retroactively seek to deny recovery of Board-approved PILs amounts for 2001. As a result, the 2001 PILs amounts themselves were collected under final rate orders and cannot be retroactively adjusted. However, the Board may dispose of the net differences between the deferred PILs amounts approved in rates and the amounts billed to customers for the period 2002-2004.

All of Which is Respectfully Submitted

Date: January 21, 2011.

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