

**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 Midland Power  
Utility Corporation for an order or orders approving or fixing just  
and reasonable distribution rates and other charges, to be effective  
May 1, 2012.

**AND IN THE MATTER OF** a Motion to Review and Vary by  
Midland Power Utility Corporation pursuant to the Ontario Energy  
Board's *Rules of Practice and Procedure* for a review of the  
Board's Decision and Order in proceeding EB-2011-0182.

**MIDLAND POWER UTILITY CORPORATION REPLY SUBMISSION**

**DELIVERED JUNE 1, 2012**

**INTRODUCTION:**

1. Midland Power Utility Corporation ("Midland") applied for distribution rates effective May 1, 2012 under the Ontario Energy Board's (the "Board's") 3rd Generation Incentive Regulation Mechanism rate making process. As part of that Application, Midland requested disposition of the balance in Account 1562 - Deferred PILS, in accordance with the Board's Decision and Order in its combined review proceeding on Account 1562 (EB-2008-0381) dated June 24, 2011 (the "Combined PILs Decision").
2. In preparing its SIMPIL models for the purpose of determining the PILs balance for disposition in rates, Midland based its calculations on the following maximum tax rates, as set out in the Combined PILs Decision:
  - 2001: 40.62%;
  - 2002: 38.62%;
  - 2003: 36.62%;
  - 2004: 36.12%; and
  - 2005: 36.12%
3. At pages 10-13 of its Application, in its Manager's Summary, Midland provided its

rationale for using the maximum true-up rates, consistent with the Board's findings in the Combined PILs Decision.

4. During the Interrogatory process, in Board Staff interrogatory No. 5(c), Board Staff made the following request:

"Board Staff requests Midland to determine the appropriate blended federal and Ontario income tax rates for each year based on the adjusted regulatory net income for tax purposes shown in the table and to provide all of the calculations. Board Staff has estimated the income tax rates to be approximately 18% for 2002, 26% for 2003, 30% for 2004 and 27% for 2005."

5. In its response to Interrogatory 5(c), delivered on January 27, 2012, Midland noted that Board Staff appeared to have used a tax rate half way between the minimum and maximum tax rates, notwithstanding that, as discussed in Midland's response to Question 5(a), the Combined PILs Decision had directed distributors to use a maximum blended tax rate. However, Midland determined the blended tax rate and showed the resulting calculations as requested by Board Staff. The taxable income reported on Midland's T2 tax returns was adjusted to remove any additions/deductions to taxable income resulting from regulatory asset changes. Tax rates for 2001 and 2002 were the minimum approved tax rates. Midland obtained blended tax rates from its external auditors for 2003 to 2005 based on these revised taxable incomes. The methodology for these calculations was discussed in the affidavit of Lorenzo Agostino, C.A., sworn May 17, 2012.<sup>1</sup>

6. In their February 10, 2012 submission on the Application, Board Staff commented on Midland's Application, including Midland's approach to Account 1562. Board Staff stated, in part:

"Midland created the receivable from ratepayers principally by choosing the maximum blended income tax rates in each year even though it was never subject to the maximum income tax rates. (at p.7)

...

Corporate taxpayers are eligible for the full federal small business deduction when taxable capital is below \$10 million. The small business deduction is phased out on a straight-line basis as taxable capital increases above \$10 million, and is completely eliminated when taxable capital reaches \$15 million. The taxpayer

---

<sup>1</sup> The Agostino affidavit can be found in Midland's Supplementary Motion Material delivered May 18, 2012

pays a lower rate of income tax than the maximum rate as long as taxable capital remains below \$15 million.

Board staff submits that Midland was not subject to the maximum income tax rates during the tax years 2001 through 2005 and, therefore, Board staff submits that Midland should not use these maximum income tax rates to calculate the variances it wants to collect from its ratepayers.

Board staff submits that Midland should use the income tax rates shown above in the table entitled 'Minimum Income Tax Rates in Percentages'." (at p.11)

7. In its reply submission dated February 24, 2012, Midland defended the use of maximum tax rates but submitted that in the event that the use of the maximum rates was not approved by the Board, the rates that should be used were the effective tax rates set out at page 11 of the Midland reply. Those rates (19.12% for 2001; 19.12% for 2002; 29.41% for 2003; 31.58% for 2004; and 29.7% for 2005) corresponded to the rates shown in the detailed calculations provided by Midland in response to Board Staff Interrogatory 5(c).

8. In its Decision and Order issued April 4, 2012, the Board summarized the issues relating to appropriate true-up tax rates. The Board also made the following comments on the effective tax rates shown by Midland in its reply submission:

"Midland did not provide an explanation of how it calculated these income tax rates, or why these tax rates would have been applicable to its tax position during the period under review. (at p.14)

...

The Board notes that Midland was not subject to the maximum taxation rates over the 2001 to 2005 period and that it was also eligible for the full small business deduction. The Board is not persuaded that the alternative taxation rates proposed by Midland should be used, as the evidentiary basis to support the proposed tax rates in 2003, 2004 and 2005 was not provided and the tax rates were not subject to discovery, as Midland filed these alternative tax rates in its reply submission. "

The Board agrees with the submission of Board staff that Midland should use the income tax rates shown in the table entitled 'Minimum Income Tax Rates in Percentages' provided in Board staff's submission based on in the Board's decision in the PILS Combined Proceeding on page 17." (at p.15)

9. The maximum rates proposed by Midland, if approved by the Board, would have resulted in the recovery of \$173,417, as at April 30, 2012, from Midland's customers (this was reduced to a recovery of \$164,412 during the interrogatory process). The minimum rates proposed by Board Staff and approved by the Board in its Decision result in the requirement that Midland pay \$483,400 to its customers. The rates presented by Midland in response to Board Staff Interrogatory No. 5(c) would result in

the payment by Midland of \$245,872 to its customers.

10. On April 24, 2012, Midland delivered the current Motion for a review and variance of the Board's Decision, in which Midland has sought (in part) the following relief:
  - a) A review and variance of that portion of the Board's Decision With Reasons dated April 4, 2012, in the matter of Midland's 2012 IRM application, relating to the Review and Disposition of Account 1562: Deferred Payments in Lieu of Taxes, in which the Board directed Midland as follows:

“The Board therefore directs Midland to enter (i.e., over-ride the formulas) in the SIMPIL models for the years 2001 to 2005 on sheet TAXCALC the income tax rates as shown in the table “Minimum Income Tax Rates in Percentages” in the decision of the Board in the combined proceeding, update its continuity schedule, and re-file the 2001 to 2005 active Excel SIMPIL models to support the entries in the continuity schedule”;<sup>2</sup>
  - b) The substitution of the taxation rates provided by Midland in its response to Board Staff Interrogatory No.5(c) and discussed in Midland's Reply submission, or similar rates based on the principle that the rates to be used should be reflective of how income taxes would have been determined for each of the rate applications in respect of which the true-up of that account is now taking place;
  - c) The Board's permission to file supplementary material related to this motion, as discussed below, within 14 days of the delivery of this Notice; and
  - d) An order staying the operation of that portion of the Board's Decision dated April 4, 2012 and the Rate Order dated April 20, 2012 related to Account 1562 pending the resolution of this motion, or an order allowing the revenue requirement impact of the motion to be tracked and recovered from ratepayers if the motion is successful.
11. On May 8, 2012, the Board issued Procedural Order No.1 (“PO#1”), in which it ordered, among other matters, that “Midland shall file with the Board any additional material in support of its Motion by no later than May 18, 2012.” Board Staff and VECC were directed to deliver their submissions, if any, by Friday, May 25, 2012,

---

<sup>2</sup> Decision with Reasons, EB-2011-0182, April 4, 2012, at p.15

and Midland's reply submission, if any, was to be delivered by Tuesday, May 29, 2012.

12. Midland filed its additional motion material on May 18, 2012. That material consisted of the affidavits of Lorenzo Agostino and James Hopeson. The Board Staff submission was delivered Friday, May 25, 2012. The VECC submission was delivered late in the evening of Monday, May 28, 2012. By letter dated May 29, 2012, Midland requested a brief extension of the deadline for filing its reply, to Friday, June 1, 2012. By Procedural Order No.2, issued May 29, 2012 ("PO#2), the Board granted the extension.
13. Midland offers the following submissions in reply to the Board Staff and VECC submissions. Midland also repeats and relies on the statements and submissions made in its original and supplementary motion material. Midland's comments will be set out as follows:
  - The Threshold Question;
  - The Merits of the Motion; and
  - Regulatory Consistency
14. Midland maintains that the Board erred in fact, in finding that there was no evidentiary basis for the alternative tax rates shown in Midland's reply submission; and that the Board erred in the adoption of the minimum tax rates for Midland.

#### **THE THRESHOLD QUESTION:**

15. At page 3 of PO#1, the Board advised that "the most expeditious way of dealing with this Motion is to consider concurrently the threshold question of whether the matter should be reviewed (as contemplated in the Board's *Rules of Practice and Procedure*) and the merits of the Motion."
16. In the cover letter to its supplementary motion material, Midland advised that it would address any Board Staff and intervenor submissions in this regard in its reply submission, but that at paragraphs 11 and 12 of its April 24, 2012 Motion, it had identified what it respectfully submitted were errors in the Board's April 4, 2012 Decision. These include

errors in fact (for example, in finding that there was no evidentiary basis for the alternative tax rates shown in Midland's reply submission when, in fact, Midland did provide detailed calculations to support those effective corporate tax rates in response to Board Staff IR 5(c) as part of the discovery process). They also include errors in the application of minimum tax rates to Midland in the absence of an evidentiary basis for doing so and in a manner inconsistent with both the Board's approach in the Combined PILs proceeding and with the Board's decisions in other Account 1562-related applications filed by distributors in similar circumstances to those of Welland. Midland submitted that this matter should be reviewed, and maintains that the threshold question should be answered in the affirmative.

- *Board Staff and VECC submissions*

17. Board Staff cite Rule 45.01 of the Board's *Rules of Practice and Procedure* (the "Rules"), which provides that "In respect of a motion brought under Rule 42.01, the Board may determine, with or without a hearing, a threshold question of whether the matter should be reviewed before conducting any review on the merits", as the basis for the Board's consideration of the threshold question. Midland acknowledges that the Board may consider the threshold question.

18. Board Staff quote Rule 44.01(a), which provides as follows:

"Every notice of a motion made under Rule 42.01, in addition to the requirements under Rule 8.02, shall:

- (a) set out the grounds for the motion that raise a question as to the correctness of the order or decision, which grounds may include:
  - (i) error in fact;
  - (ii) change in circumstances;
  - (iii) new facts that have arisen;
  - (iv) facts that were not previously placed in evidence in the proceeding and could not have been discovered by reasonable diligence at the time."

19. Board Staff discuss the Board's articulation of the threshold test in its May 22, 2007 Decision on a number of review motions in respect of its Natural Gas Electricity Interface Review ("NGEIR") Decision (EB-2006-0332/0338/0340). Board Staff describe the Board's finding in that matter as follows:

"The Board, in the NGEIR Decision, stated that the purpose of the threshold question is to determine whether the grounds put forward by the moving party raised a question as to the correctness of the order or

the decision, and whether there was enough substance to the issues raised such that a review based on those issues could result in the Board varying, cancelling or suspending the decision.”

20. Having cited the applicable Rules and described the Board’s findings in the NGEIR Decision, Board Staff make four comments with respect to the Midland motion, which Midland has attempted to summarize as follows:

- Board Staff assert that Midland has “nullified” the arguments made in its motion by stating that the Board erred by not giving more weight to the income tax rates provided by Midland in response to Board Staff interrogatory #5(c) and by adopting the minimum tax rates to be used in calculating the revised amount for disposition, but then submitting in the motion that the rates used in response to Board Staff Interrogatory #5(c) are incorrect and that the rates that should be used are the revised rates provided by its auditors and included in its motion material. Board Staff go on to assert that:

“The Board would have considered the alternative tax rates submitted by Midland in response to Board staff interrogatory #5c and in its Decision the Board opted not to apply them. The present Motion requests that the Board vary its Decision by applying slightly revised tax rates but still similar to those provided in interrogatory #5c. In Board staff’s view, the Motion is an attempt by Midland to reiterate the argument made in its reply submission in the original Application (which the Board did not adopt).”

- Board Staff assert that Midland “did not provide the Board with complete evidence in the EB-2011-0182 proceeding to support the use of these revised income tax rates [the rates provided in response to Board Staff Interrogatory #5(c)]”, and that certain rates provided in that response (for 2003-2005) were counterintuitive because they were higher than the maximum Ontario tax rates for those years;
- Board Staff refer to Midland’s 2009, 2010, 2011 and 2012 distribution rate adjustment applications, which (with the exception of the 2012 application) are not part of the record in the current proceeding (either the motion or the underlying application) and do not relate to the years that are the subject matter of this proceeding or the Account 1562 reconciliation proceedings generally, to support an assertion that because the minimum tax rate was used for each of 2009 through 2012, “Midland’s own applications demonstrate that the minimum income tax rates are the correct tax rates to be used in calculating the balance in Midland’s Account 1562

deferred PILs”; and

- Board staff submit that the current proceeding is a prudence review of evidence specific to Midland, and not a generic proceeding. The Board’s purpose with respect to the PILs component of Midland’s application was to determine a re-calculated balance on a final basis for Account 1562 deferred PILs as of April 30, 2012, and for the Board to approve rate riders on a final basis. The introduction of new evidence from other distributors’ cases does not assist in the prudence review of Midland’s evidence. Each distributor’s prudence review is based on its unique tax evidence and prior Board decisions pertaining to that distributor. Accordingly, Board Staff submit that that evidence should be dismissed.

21. VECC submits that “Midland really seeks to recast the record of PILs recoveries and allowance as unfair, although it seems clear that the Board proceeded in a prudent fashion given the information it had before it to fashion just and reasonable rates. While knowledge gained in the passage of time and experience is useful for regulators on a prospective basis, it must play very little role in adjusting past decisions to meet discovered facts. VECC suggests that Midland has failed to meet the threshold test to allow its motion to proceed.”

- *Midland’s reply*

22. With respect to Rule 44.01(a) quoted above, Midland submits that its Notice of Motion complied with the Rule. Midland clearly set out the grounds for its motion that raised a question as to the correctness of the Board’s Decision. In its motion, Midland has submitted that the Board has erred in a number of ways in its determination that Midland is to use the minimum rates and in its rejection of the alternative rates set out in Midland’s response to Board Staff Interrogatory No. 5(c). Specifically:

- a) Midland respectfully submits that the Board erred in fact, in finding that there was no evidentiary basis for the alternative tax rates shown in Midland’s reply submission. In fact, Midland did provide detailed calculations to support those effective corporate tax rates in response to Board Staff IR 5(c) as part of the discovery process. These



rate derivations were specifically requested by Board staff based on a revised taxable income adjusted for regulatory asset changes. The rates were explained in Midland's interrogatory response, and all necessary calculations were shown as required; and

b) Midland respectfully submits that the Board erred in its adoption of the minimum rates for Midland. The arbitrary use of minimum rates assumes that any distributor having less than \$10 million in taxable capital and receiving the full small business deduction will pay minimum rates. This is incorrect, and is inconsistent with the Board's approach in the Combined PILs proceeding and with its decisions in other Account 1562-related applications. All of the three applicants in the Combined PILs proceeding had a level of taxable income which put them in the highest weighted average tax bracket. The measure of taxable income was the level of regulatory taxable income used in the PILS determination models to calculate the amount of PILS that were included in rates. They also had levels of taxable capital which precluded them from taking advantage of lower tax rates resulting from application of the small business deduction. The approval of tax rates also reflected the change to federal and provincial income tax rates on a year by year specific basis relative to the tax rates that were used to calculate PILS that were included in rates. As a result the Board approved effective maximum tax rates for the three applicants taking into consideration the following three key factors:

- The level of taxable income was set equal to regulatory taxable income used in the PILs determination models which were used to calculate the amount of PILs that were included in rates;
- The level of taxable capital as per the actual Federal T2 tax returns was used to determine if small business reductions to tax rates were appropriate; and
- The actual level of legislated annual federal and provincial income tax rates was used for the specific years.<sup>3</sup>

Midland understands the minimum tax rates to have been approved using the same approach. Those rates also represent the effective tax rates for smaller utilities (with

---

<sup>3</sup> See paragraph 20 of the Hopeson affidavit, at Tab 1 of the May 18, 2012 Supplementary Motion Material.

lower levels of taxable income and the ability to maximize the small business deduction to reduce tax rates). This approach properly reflects the intent of the SIMPILS process to capture changes in legislated tax rates. The PILs included in rates were determined well in advance of the actual tax years using proxies for what the actual tax rates would be. Utilizing the actual tax rates that would be applicable to the same level of regulatory net income as used to set PILs in rates properly captures the changes in legislation. This captures the difference between the rates used to determine PILs included in rates and what the PILs would have been if they were set in the actual tax year with full knowledge of any changes in tax rates. For those distributors that do not have characteristics that would allow them to utilize the approved minimum or maximum rates, the correct approach, which is consistent with the Board's Combined PILs Decision, is to apply the 3 key factors outlined above to utility specific values. The alternative effective rates proposed by Midland in response to Board Staff Interrogatory No. 5(c) are directionally more reflective of the correct approach.

- c) In addition to the errors set out above, Midland has also submitted that the Board's Decision in this Application is inconsistent with its decisions in respect of other distributors in similar circumstances. In the Notice of Motion, Midland cited the example of Welland Hydro Electric System Corp. ("Welland"). In the affidavit of James Hopeson, which formed part of Midland's supplementary motion material, that case (EB-2011-0202), as well as those of Hydro Hawkesbury Inc. (EB-2011-0173) and Renfrew Hydro Inc. (EB-2011-0195), were discussed. In particular, Hawkesbury and Renfrew were examples of distributors with rate bases of less than \$10 million in respect of which the Board did not use minimum tax rates. Welland was an example of the Board's acceptance of regulatory taxable income as the basis for the determination of applicable tax rates. The excerpt below is taken from the Board Staff submission dated January 9, 2012:

"For the 2002, 2003 and 2004 tax years, Welland calculated the income tax rates to be used in the true-up calculations in the SIMPIL models by selecting the regulatory taxable income from its 2002 rate application and determining how much tax would have applied to that amount of taxable income in

2002, 2003 and 2004. For the 2005 tax year, Welland used the regulatory taxable income from its 2005 rate application to calculate the taxes payable on that amount, and thereby derived the income tax rate used in the 2005 SIMPIL worksheets.

Staff submits that given the tax facts in Welland's case, and the tax losses during the period, Welland's methodology for determining the income tax rates used in the SIMPIL model true-up calculations is a reasonable alternative because the approach was symmetrical with how income taxes would have been determined for each of the rate applications."

- d) Additionally, while Midland acknowledged that the decision of another panel cannot bind the panel in the current proceeding, Midland submitted that by issuing conflicting decisions in similar fact situations, the Board has created significant uncertainty in the proper understanding of the Board's Combined PILs Decision. This is an important issue, in that it will still affect the clearance of Account 1562 balances for other Ontario electricity distributors.

23. Midland has identified what it submits are a number of errors in the Board's Decision of April 24, 2012. As for whether these errors "warrant review", Midland notes that at page 18 of the NGEIR Decision,<sup>4</sup> the Board wrote:

"Therefore, the grounds must 'raise a question as to the correctness of the order or decision'. In the panel's view, the purpose of the threshold test is to determine whether the grounds raise such a question. This panel must also decide whether there is enough substance to the issues raised such that a review based on those issues could result in the Board deciding that the decision should be varied, cancelled or suspended.

With respect to the question of the correctness of the decision, the Board agrees with the parties who argued that there must be an identifiable error in the decision and that a review is not an opportunity for a party to reargue the case.

In demonstrating that there is an error, the applicant must be able to show that the findings are contrary to the evidence that was before the panel, that the panel failed to address a material issue, that the panel made inconsistent findings, or something of a similar nature. It is not enough to argue that conflicting evidence should have been interpreted differently.

The applicant must also be able to demonstrate that the alleged error is material and relevant to the outcome of the decision, and that if the error is corrected, the reviewing panel would change the outcome of the decision."

24. Midland submits that the evidence before the panel in the 2012 IRM Application confirmed that minimum tax rates were not appropriate for Midland. With respect to the materiality of the errors and their relevance to the outcome of the Decision, Midland

---

<sup>4</sup> Available at:

[http://www.rds.ontarioenergyboard.ca/webdrawer/webdrawer.dll/webdrawer/rec/180773/view/dec\\_reasons\\_NGEIR\\_motion\\_EB-2005-0551\\_EB-2006-0322%20EB-2006-0338%20EB-2006-0340\\_20070522.PDF](http://www.rds.ontarioenergyboard.ca/webdrawer/webdrawer.dll/webdrawer/rec/180773/view/dec_reasons_NGEIR_motion_EB-2005-0551_EB-2006-0322%20EB-2006-0338%20EB-2006-0340_20070522.PDF)

submits that its Account 1562 claim was a significant element of its 2012 IRM Application. While Midland had initially requested the recovery of \$173,418 from its customers (which was amended to a recovery of \$164,412 through the interrogatory process), and that was modified to approximately \$246,000 payable to its customers in its reply submission in the original proceeding the Board's Decision imposed a further \$237,528 payment obligation on Midland, for a total obligation of \$483,400 as at April 30, 2012. By way of comparison, Midland notes that its materiality threshold in a cost of service application would be \$50,000,<sup>5</sup> and its materiality threshold in the context of SIMPILs calculations would be \$10,264, as determined from the SIMPILS models (.25% x ratebase of \$8,211,325 x 50% equity component). Midland submits that the amount at issue in this motion far exceeds either of those two values and is clearly material, and the errors identified by Midland are relevant to the outcome of the Decision.

25. Finally, Midland submits that (to use the words of the Board in the NGEIR Decision) "there is enough substance to the issues raised such that a review based on those issues could result in the Board deciding that the decision should be varied, cancelled or suspended". Midland submits that correcting those errors and the tax rates applicable to Midland for the subject years would change the outcome of the Decision.
26. With respect to the specific matters identified by Board Staff in their discussion of the threshold question, Midland respectfully disagrees with the submissions of Board Staff and offers the following submissions:
  - a) Midland respectfully disagrees with the Board Staff suggestion that Midland has "nullified" the arguments in its motion. As discussed in the cover letter to the Midland supplementary motion material, at page 3 of PO#1, the Board stated that "The Board will not grant Midland permission to file new evidence regarding tax rates as identified in paragraph 15 of the Motion." Midland took that finding into consideration in preparing its additional motion material. However, Midland notes

---

<sup>5</sup> Under section 2.4.4 of Chapter 2 of the Board's June 22, 2011 Filing Requirements for Transmission and Distribution Applications, the materiality threshold for a distributor with a distribution revenue requirement less than or equal to \$10 million is \$50,000.

that item (b) of its request for relief in its Notice of Motion stated:

“The substitution of the taxation rates provided by Midland in its response to Board Staff Interrogatory No.5(c) and discussed in Midland’s Reply submission, or similar rates based on the principle that the rates to be used should be reflective of how income taxes would have been determined for each of the rate applications in respect of which the true-up of that account is now taking place”

At paragraph 15 of its Notice of Motion, Midland stated, in part:

“In order to ensure the most accurate calculation possible and to allow for Board Staff and Board scrutiny of those calculations, Midland proposes that if the Board accepts its proposed approach to the calculation of the rates (that is, that Midland’s rates should fall between the minimum and maximum set out in the Combined PILs Decision), it would file its calculations of the rates in a manner similar to a draft rate order. Those rates would then be subject to review and comment by Board staff and a reply by Midland, with the Board making the final determination on the rates at that time.”

If the Board accepts Midland’s submissions on the inappropriateness of minimum tax rates in Midland’s circumstances, then the tax rates on which the Account 1562 true-up is based will change. The rates provided in Midland’s response to Board staff Interrogatory #5(c) are directionally much closer to the appropriate rates for Midland, and are far more appropriate than the Board’s use of minimum rates, and it is open to the Board to adopt them. However, Midland’s understanding is that they are still not accurate. Midland acknowledges that the Board does not wish to hear evidence on updated calculations of the tax rates at this time, but Midland respectfully suggests that it is important to ensure that the rates used in the final calculation of the amount for disposition are as accurate as possible. Midland maintains that the approach set out in the extract from paragraph 15, above, is an appropriate approach to any updated calculations of tax rates, in that it allows for the most accurate calculation of rates to be used, and those calculations will be subject to review by Board staff, VECC and the Board itself. Midland remains prepared to address those calculations at a time to be determined by the Board. Of primary importance in this motion is the error in applying minimum rates to Midland. The fact that the rates ultimately determined by the Board to be correct may not be as set out in Midland’s response to Board Staff Interrogatory 5(c) is not an appropriate ground for rejecting the motion as not having met the threshold test.

b) With respect to the Board Staff assertion that Midland “did not provide the Board

with complete evidence in the EB-2011-0182 proceeding to support the use of these revised income tax rates [the rates provided in response to Board Staff Interrogatory #5(c)]”, and that certain rates provided in that response (for 2003-2005) were counterintuitive because they were higher than the maximum Ontario tax rates for those years, Midland reiterates that the fundamental issue is that the Board erred in assigning the minimum rates to Midland. Midland has proposed a reasonable and appropriate approach to determining the correct rates, and that approach provides for scrutiny of Midland’s detailed calculations in that regard. Additionally, having discussed this matter with its auditors, Midland submits that the income tax rate of 12.5% for 2003 and 14% for 2004 and 2005 quoted by Board Staff would not be the maximum Ontario rates for the periods in question. Midland submits that Board Staff have failed to observe the impact of the Ontario surtax on the income tax rates for the periods in question. Under the Ontario tax system, in 2003, 2004 and 2005, Ontario recaptures the benefit of the provincial small business deduction through a surtax on taxable income in excess of the Ontario small business limit, which was identified in Exhibit B of the affidavit of Lorenzo Agostino dated May 17, 2012. For the 2003 taxation year any taxable income earned in excess of the small business limit of \$320,000 and up to approximately \$799,650 would be subject to a tax rate of 17.17%, which is calculated by adding the base income tax rate of 12.5% plus an additional surtax rate of 4.67%. For the 2004 and 2005 taxation years any taxable income earned in excess of the small business limit of \$400,000 and up to approximately \$1,128,050 would be subject to a tax rate of 18.67%, which is calculated by adding the base income tax rate of 14% plus an additional surtax rate of 4.67%. The rates cited by Midland for those years are correct.

- c) With respect to the Board Staff assertion that because the minimum tax rate was used for each of 2009 through 2012, “Midland’s own applications demonstrate that the minimum income tax rates are the correct tax rates to be used in calculating the balance in Midland’s Account 1562 deferred PILs”, Midland submits that as a general matter, there is no basis for concluding that because a particular rate (the minimum rates) applied in years that are outside the scope of this Account 1562 proceeding,

then the same minimum rates will apply to the years that are within the scope of the proceeding.

- d) Finally, with respect to the Board Staff comment about references to other distributors' Account 1562 disposition applications, Midland submits that the point of those references is to support Midland's assertion that it has not been treated in a manner consistent with other distributors in similar circumstances. It is entirely reasonable to anticipate that the Board will act in a similar manner in similar circumstances, and as will be discussed later in this submission, the Board itself has spoken of the desirability of regulatory consistency. In its Decision in the Combined Proceeding (at page 2), the Board states:

"The Notice of the combined proceeding included a statement of the Board's expectation that the decision resulting from the combined proceeding would be used to determine the final account balances with respect to account 1562 Deferred PILs for the remaining distributors."

Midland understands that the unique characteristics of individual LDCs must also be taken into consideration. Midland asserts that true-up rates should be derived using the principles established in the Combined Proceeding whereby rates were determined based on regulatory taxable income, the ability to utilize small business tax reductions as determined by taxable capital levels, and the legislated federal and provincial income tax brackets and rates of the day. Applying utility specific values will result in a unique set of rates for each LDC which would be reflective of how rates would have been set with perfect knowledge. It is not reasonable to suggest that Midland should not discuss the Board's decisions in other applications, nor should that be considered a basis for answering the threshold question in the negative.

27. With respect to VECC's assertion that "it seems clear that the Board proceeded in a prudent fashion given the information it had before it to fashion just and reasonable rates", Midland respectfully disagrees and, as is clear from this motion, Midland submits that there were errors in the Board's Decision.
28. With respect to VECC's statement that "While knowledge gained in the passage of time and experience is useful for regulators on a prospective basis, it must play very little role

in adjusting past decisions to meet discovered facts”, Midland has two comments. First, this is not a matter of “adjusting a past decision to meet discovered facts”. This motion involves the correction of errors in the Board’s Decision, and in addressing this matter, Midland is using existing information already on the public record. While it is true that Midland provided additional calculations of the applicable tax rates in its original motion material, the Board determined in PO#1 that it did not wish to deal with that material, and Midland has abided by that determination in its additional motion material and in this submission. Midland maintains that if the Board allows this motion, it will be important to use tax rates that are as accurate as possible, and Midland has commented on how this can be done. Second, Midland submits that the time to correct the tax rates to be used for Midland is now. The knowledge did exist to determine more appropriate true-ups rates. The knowledge can be derived from the Combined Proceeding and other Decisions of the Board. Midland respectfully submits that there will be limited future value in knowledge gained through this PILs approval process as the Account 1562 Deferred PILs disposition process is effectively a one-time activity covering the historical years of 2001 to 2005.

29. For all of the foregoing reasons, Midland reiterates that the threshold question should be answered in the affirmative.

**THE MERITS OF THE MOTION:**

30. Midland has discussed the errors it believes the Board has made in its Decision in the subject proceeding in its Notice of Motion and has repeated that discussion above for the Board’s reference. Midland does not propose to repeat them here. Board Staff have identified the following three areas for further submission in the event that the Board proceeds to consider the merits of the Motion:
- Inconsistencies in RRR filings;
  - The “No-Harm” Principle; and
  - The Relevance of the Combined Proceeding (EB-2008-0381)
31. Midland will address these matters below.



- **Inconsistencies in RRR filings:**

- *Board Staff submissions*

32. On page 8 of the Board Staff submission, Board Staff submit that "...the balance in Account 1562 reported by Midland in its most recent 2011 RRR filings in April 2012 appears to be inconsistent with the position Midland has stated in this Motion."

- *Midland's reply*

33. The combined proceeding clarified several issues regarding how the Account 1562 deferred PILs balance should be calculated. Midland submitted its Application believing that it had followed the principles established in the proceeding. The only issue of discrepancy remaining – appropriate true-up rates – is the focus of this Motion. The Board has accepted all other aspects of Midland's PILs determination.

34. The RRR filings reflected a best efforts approach to the determination of the 1562 balance in the absence of any specific guidance which arose from the combined proceeding. For example, the RRR values reflected true ups of regulatory asset adjustments which the combined proceeding clarified as not appropriate as they only reflected timing differences. Midland was not in a position to revise its historical filings to align with its revised continuity schedule until after the Board issued its June 2011 Decision in the Combined Proceeding. Rather than revise its filings Midland decided to let the issue be resolved through the rate adjustment/approval process.

35. Midland submits that the inconsistency with previous RRR filings should not be a factor in reviewing this motion.

- **The "No-Harm" Principle**

- *Board Staff submissions*

36. On page 8 of the Board Staff submission, under the heading of the "No Harm Principle", Board Staff suggest that Midland is not harmed by the decision to use minimum true-up rates as recoveries from customers have been greater than taxes actually paid over the PILS period of 2001 to 2005.

- *Midland's reply*

37. Midland is concerned about the implications of the Board Staff position. Board Staff explain (correctly, in Midland's submission) that:

“Board staff understands that the Board's PILs methodology is not the same as flow through taxes. Board staff also understands that a total true up of the amounts collected from ratepayers and the amounts actually paid in taxes to the government was not the intent of the PILs Account 1562 methodology and Board staff would not argue for such an outcome.”

38. Yet Board Staff continue to show these differences in an attempt to support the position that Midland was not harmed.

39. Midland submits that this should not be a factor in the Board's consideration of this motion. As acknowledged by Board Staff, it is not relevant to the issue, and Midland notes that the Board Staff calculations are based on highly selective information. The taxable income for Midland was significantly reduced in these years due to regulatory asset deductions to taxable income. This timing difference resulted in significant increases to taxable income and taxes paid in succeeding years which are not part of the PILs disposition period.

40. The following table demonstrates the impact of timing differences related to taxable income recognition of regulatory asset balances. Payment of taxes was \$804,325 greater than approved recoveries of taxes over the 2006 to 2008 period

<b>PILS Approved in Rates</b>		<b><u>2006 EDR</u></b>	<b><u>2007 IRM</u></b>	<b><u>2008</u></b>	<b><u>Total</u></b>
EDR 2006 Model	Sheet 5.1 Service Rev Adj	\$ 168,350			
2007 IRM Model	Sheet 8 - Dx IRM Adj		\$ 169,899		
2008 IRM Model	Sheet 6A Fed Tax Adj Factor			\$ 144,847	
<b>Taxes Paid</b>	Per Corporate Tax Returns	\$ 432,950	\$ 584,784	\$ 269,687	
	<b><i>Excesss of Payments vs Recoveries</i></b>	<b>\$ 264,600</b>	<b>\$ 414,885</b>	<b>\$ 124,840</b>	<b>\$ 804,325</b>

41. The PILs Combined Proceeding established the principle that any adjustments related to regulatory assets should be excluded from the Account 1562 PILs determination process as they represented timing differences only.

42. The Board Staff assertion is additionally unfair – as Board Staff effectively

acknowledge, there will always be differences between revenues and expenses approved for rate making purposes vs. revenues and expenses used for tax purposes, or between revenues and expenses approved for rate making purposes and actual revenues and expenses. In addition to the exclusion of regulatory asset adjustments addressed above, Midland notes that the tax implications of the following items are not trued up under the approved SIMPIL methodology, all of which creates a difference between the regulatory determination of PILs and the amount of PILs actually paid:

- Revenues
- Depreciation vs capital cost allowance
- All items categorized on TAXREC 3 tabs of the SIMPIL true-up models

43. Midland is not arguing that it was harmed from a cash flow perspective over these years. It is arguing that inappropriate true-up tax rates were approved for purposes of determining the Account 1562 Deferred PILs balance. This issue is properly the subject matter of Midland's Application and this motion; the staff comments are not.

- **The Relevance of the Combined Proceeding (EB-2008-0381)**
- *Board Staff submissions*

44. The Board Staff discussion of this matter can be found at pages 9-11 of the Board Staff submission. Midland wishes to address the following three matters arising out of that discussion.

45. First, in the section titled "Relevance of the Combined Proceeding" Board Staff appear to be suggesting that the principles established in the Combined Proceeding only apply to the three applicants in that proceeding. Midland's application is not generic, and a decision must be based on Midland's specific tax facts and evidence.

46. Second, at pages 10 and 11 of their submission, Board Staff make the following statements with respect to the Board's Decision on true-up rates:

"In conducting the prudence review of the re-calculation of the balance in Account 1562, the Board has to consider many inputs that a distributor used throughout its evidence. The income tax rates are one of many important inputs in the calculations." (at p.10)

...

“Board staff submits that the Board selected a well-reasoned regulatory solution to the complex tax rate issue for Midland due to a lack of clarity on the record with respect to the most correct tax rates applicable to Midland’s circumstances.” (at p.11)

47. Third, at page 10 of their submission, Board Staff state:

“The Board has used rate base as a proxy for taxable paid-up capital in the PILs calculations since the 2002 application.<sup>17</sup> A taxpayer is eligible for the full amount of the federal small business deduction when taxable capital is below \$10 million. The small business rate is available to the taxpayer and the minimum income tax rate applies.

<sup>17</sup> See PILs application instructions and footnotes issued in December 2001 and updated January 18, 2002.”

- *Midland’s reply*

48. With respect to the first matter, while Board Staff appear to suggest that principles established in the Combined Proceeding only apply to the three applicants in that proceeding, Midland submits that the principles established in the Combined Proceeding that were used to determine appropriate true-up rates (that is, the use of the 3 criteria discussed above) should be used for Midland and other distributors as well. For the Board’s reference, those principles, as discussed at paragraph 20 of the Hopeson affidavit, are:

- The level of taxable income was set equal to regulatory taxable income used in the PILs determination models which were used to calculate the amount of PILs that were included in rates;
- The level of taxable capital as per the actual Federal T2 tax returns was used to determine if small business reductions to tax rates were appropriate; and
- The actual level of legislated annual federal and provincial income tax rates was used for the specific years.

This is consistent with the Board’s own “expectation that the decision resulting from the combined proceeding would be used to determine the final account balances with respect to account 1562 Deferred PILs for the remaining distributors. Applying Midland’s specific facts will result in a different set of rates which may or may not reflect the minimum and maximum approved true-up rates.

49. The evidence on the record includes 3 different sets of tax rates:

- Maximum rates as used in the Application;

- Board Staff Interrogatory 5(c) rates; and
- Minimum rates as adopted by the Board in its Decision and Order

The use of Interrogatory 5(c) rates, although not considered correct by Midland, is directionally much more correct than the use of minimum rates. If the final decision is to be based on the evidentiary record as it currently exists these would be the most correct rates.

50. With respect to the second matter, the use of minimum rates implies a level of taxable income for each of the years in question for which there is no support on the record. The Decision does not contain any factual rationale as to why minimum rates were deemed appropriate by the Board.
51. As illustrated in Exhibit B to the May 17, 2012 affidavit of Lorenzo Agostino, minimum tax rates are applicable to the following levels of taxable income:
- 2003 – zero to \$225,000;
  - 2004 – zero to \$248,644; and
  - 2005 – zero to \$300,000
52. Midland's regulatory taxable income exceeded those levels in each of 2003, 2004 and 2005, as shown in the following table:

#### **Midland Taxable Income Scenarios**

	<b>Record Reference</b>	<b><u>2003</u></b>	<b><u>2004</u></b>	<b><u>2005</u></b>
Regulatory Taxable income	SIMPIL Models	478,348	478,348	637,399
IR 5c) Taxable Income	Midland Response to Board Staff Interrogatory 5c)	535,435	815,286	718,264
Taxable Income subject to minimum tax rate of 18.62%	Exhibit B - Agostino Affidavit	\$0 to \$225,000	\$0 to \$248,644	\$0 to \$300,000

53. It is clear from the foregoing that Midland's regulatory taxable income in these years, which is on the record in this proceeding, whether based on Midland's SIMPIL filings or its response to Board Staff Interrogatory 5(c), is considerably in excess of the income levels that would result in minimum tax rates. In addition, please see the following

comments on the third matter noted above, which provide clarification based on the affidavit of Mr. Agostino<sup>6</sup> that the effective tax rates are fluid and continue to increase as taxable income increases above the small business limits.

54. Additionally, as noted previously, Midland reiterates that there was no lack of clarity on the record with respect to the determination of tax rates in Midland's response to Board Staff Interrogatory 5(c), and that they are directionally more correct than minimum tax rates.

55. With respect to the third matter, as noted above, Board Staff make the following assertion:

assert that a taxpayer is "eligible for the full amount of the federal small business deduction when taxable capital is below \$10 million. The small business rate is available to the taxpayer and the minimum income tax rate applies".

56. Midland respectfully submits that Board Staff have failed to account for the fact that the federal and provincial small business rates only apply to taxable income up to the business limit. This matter is addressed in paragraphs 9 and 10 of the May 17, 2012 Agostino affidavit, and in Exhibit B thereto. Taxable income earned in excess of the business limit would be subject to a higher rate of income tax than the minimum income tax rate referred to by Board Staff.

57. In short, if the taxpayer is not at the maximum or minimum rates, it is somewhere between those, and the effective weighted average tax rates change as taxable income changes.

#### **REGULATORY CONSISTENCY:**

58. In its original motion material and in the affidavit of James Hopeson, Midland has referred to three other Decisions of the Board in Account 1562-related applications. In the Notice of Motion, Midland cited the example of Welland Hydro Electric System Corp. ("Welland"). In the affidavit of James Hopeson, which formed part of Midland's supplementary motion material, that case (EB-2011-0202), as well as those of Hydro

---

<sup>6</sup> Agostino Affidavit sworn May 17, 2012, at paragraphs 9 and 10

Hawkesbury Inc. (EB-2011-0173) and Renfrew Hydro Inc. (EB-2011-0195), were discussed. In particular, Hawkesbury and Renfrew were examples of distributors with rate bases of less than \$10 million in respect of which the Board did not use minimum tax rates for Account 1562 disposition. Welland was an example of the Board's acceptance of regulatory taxable income as the basis for the determination of applicable tax rates. The Board also used regulatory taxable income as the basis for the determination of applicable tax rates for the three applicants in the Combined Proceeding.

59. As noted above in the context of the threshold question, Midland acknowledges that the decision of another panel cannot bind the panel in the current proceeding, but by issuing conflicting decisions in similar fact situations, the Board has created significant uncertainty in the proper understanding of the Board's Combined PILs Decision. It is entirely reasonable to anticipate that the Board will act in a similar manner in similar circumstances. As the Board observed at page 2 of its Decision in the Combined Proceeding, "The Notice of the combined proceeding included a statement of the Board's expectation that the decision resulting from the combined proceeding would be used to determine the final account balances with respect to account 1562 Deferred PILs for the remaining distributors. The process for the disposition of account 1562 Deferred PILs for the remaining distributors is set out at the end of this decision." It is not reasonable for Board Staff to suggest that Midland should not discuss the Board's decisions in other similar applications.
60. The Board itself has recognized the value of regulatory consistency in decision making. As it wrote in a Decision in EB-2011-0256, a proceeding involving the Municipality of Bluewater:

"...the Board recognizes the value of consistency in decision-making. Departures from established decisions should only be made on the basis of reasoned principle. However, panels of the Board are not and cannot be thought to be bound to the decisions of proceeding panels. Each panel must make its decision on the basis of the facts before it and the relevant policies and principles affecting the decision."<sup>7</sup>

---

<sup>7</sup> EB-2011-0256, Decision dated August 29, 2011, at page 5

61. Midland submits that there is no reasonable basis for treating Midland differently from other distributors in similar circumstances, including Hawkesbury and Renfrew, or for diverging from the principles established in the Combined Proceeding.
62. If it is appropriate to treat Midland consistently with other distributors in similar circumstances (Midland submits that it is), then the appropriate disposition of this motion is to vary the 2012 IRM Decision and to allow the relief requested by Midland.

**CONCLUSION:**

63. For all of the foregoing reasons, Midland respectfully submits that the threshold question has been answered in the affirmative, and that the Board should grant the following relief requested in this Motion:
  - a) A review and variance of that portion of the Board's Decision With Reasons dated April 4, 2012, in the matter of Midland's 2012 IRM application, relating to the Review and Disposition of Account 1562: Deferred Payments in Lieu of Taxes, in which the Board directed Midland as follows:

“The Board therefore directs Midland to enter (i.e., over-ride the formulas) in the SIMPIL models for the years 2001 to 2005 on sheet TAXCALC the income tax rates as shown in the table “Minimum Income Tax Rates in Percentages” in the decision of the Board in the combined proceeding, update its continuity schedule, and re-file the 2001 to 2005 active Excel SIMPIL models to support the entries in the continuity schedule”;<sup>8</sup>
  - b) The substitution of the taxation rates provided by Midland in its response to Board Staff Interrogatory No.5(c) and discussed in Midland's Reply submission, or similar rates based on the principle that the rates to be used should be reflective of how income taxes would have been determined for each of the rate applications in respect of which the true-up of that account is now taking place; and
  - c) An order staying the operation of that portion of the Board's Decision dated April 4, 2012 and the Rate Order dated April 20, 2012 related to Account 1562 pending the resolution of this motion, or an order allowing the revenue requirement impact of the

---

<sup>8</sup> Decision with Reasons, EB-2011-0182, April 4, 2012, at p.15



motion to be tracked and recovered from ratepayers if the motion is successful.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 1<sup>ST</sup> DAY OF JUNE, 2012

Midland Power Utility Corporation  
By its Counsel

Borden Ladner Gervais LLP  
40 King Street West  
Suite 4100  
Toronto, ON M5H 3Y5

James C. Sidlofsky  
(T) (416) 367-6277  
(F) (416) 361-2751  
(E) jsidlofsky@blg.com

TO: Ontario Energy Board  
P.O. Box 2319  
26<sup>th</sup> Floor  
2300 Yonge Street  
Toronto ON M4P 1E4

Tel: (416) 481-1967  
Fax: (416) 440-7656

AND TO: Intervenor of Record