

Parry Sound Power Corporation

Response to Board Staff Submission (EB-2012-0229)

Board Staff states in its submission that:

"The Board's PILs methodology is not the same as flow through taxes. Board staff 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. However, the analysis does demonstrate that PSPC would not be harmed by the Board selecting the minimum tax rates to re-calculate the balance in Account 1562."

PSPC is concerned about the implications of the Board Staff position. Board Staff explain (correctly, in PSPC'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."

Yet Board Staff continue to show these differences in an attempt to support the position That PSPC will not be harmed by using the minimum tax rates.

PSPC submits that this should not be a factor in the Board's consideration of this application. As acknowledged by Board Staff, it is not relevant to the issue, and PSPC notes that the Board Staff calculations are based on highly selective information. The taxable income for PSPC was significantly reduced in the early 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.

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.

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, PSPC 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

PSPC is not arguing that it was harmed from a cash flow perspective over these years. It is arguing that the use of effective tax rates for true up purposes is fairer than the use of arbitrary minimum tax rates.

Board Staff states in its submission that:

"The generic issue of which income tax rates would apply to distributors that were not subject to the maximum income tax rates was not decided in the Combined Proceeding. 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."

PSPCs review of Board decisions for those LDCs where the maximum true-up rates are not applicable reveal 4 prevalent alternatives:

- Effective tax rates using the 3 criteria identified in the Midland reference - eg Welland
- Actual tax rates - eg. Collus
- Modified actual - eg. Renfrew
- Minimum - eg. Midland

The issue is which option is the fairest for PSPC and its customers.

PSPC believes the use of an actual taxable income approach, and/or the use of a modified taxable income approach, is not appropriate to determine true-up rates. These approaches essentially true up every item that is different between the Determination of PILs that are included in rates and the actual tax return. On the other hand, the SIMPILS model methodology only selectively trues up certain items depending on how they are categorized on TAXREC, TAXREC2, and TAXREC3 tabs of the SIMPILS Model. In fact some items are trued up twice - once through the tax rate determination, and once through the SIMPILS model treatment of items categorized in the TAXREC and TAXREC2 tabs. TAXREC3 items are excluded from true-up. The determination of trueup rates using the actual taxable income approach or a modified taxable income approach employs a methodology that is inconsistent with the intent of the SIMPILS true-up process.

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 as seen by the differences between the effective rates determined by PSPCs external auditors based on regulatory taxable income and the minimum rates proposed by Board staff.

PSPC believes the fairest approach is to use the effective tax rates based on approved regulatory taxable income, consideration of the small business deduction, and the actual tax rates of the day. The unique characteristics of PSPC as reflected on the record would be taken into consideration. This approach would be reflective of how rates would have been set with perfect knowledge at the time of rate setting.

There is a significant and material financial impact difference to PSPC between utilizing minimum and effective true up income tax rates.

Board Staff states in its submission that:

"In interrogatory #1 Board staff requested that PSPC file the correspondence it received from its external auditors that show how the income tax rates were calculated. PSPC answered, "Appendix 1 provides the details supporting the determination of effective income tax rates by Parry Sound's external auditors for the period from 2002 to 2005." The evidence filed as Appendix 1 does not indicate that it was prepared by PSPC's auditors."

PSPC confirms that the spreadsheet provided in Appendix 1 was prepared by Mr. Lorenzo V Agostino, Tax Expert, BDO Canada LLP. PSPC will provide any additional support the Board may require.

Board Staff states in its submission that:

"PSPC filed applications for 2009, 2010, 2011 and 2012 rate adjustments. In these applications PSPC applied using the minimum income tax rates. Board staff submits that PSPC's own applications, and the evidence filed in this proceeding, demonstrate that the minimum income tax rates are appropriate tax rates to use in calculating Account 1562 deferred PILs amounts to be refunded to customers."

Board Staff refer to PSPCs 2009, 2010, 2011 and 2012 distribution rate adjustment applications, which are not part of the record in the current proceeding and do not relate to the years that are the subject matter of this proceeding or the Account 1562 reconciliation proceedings generally. PSPC submits that as a general matter, there is no basis for concluding that because a particular rate (the minimum rates) was 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.

Board Staff states in its submission that:

"Board staff has calculated a refund amount using the SIMPIL models and continuity schedules filed by PSPC as interrogatory response Appendices 8-12 and 17. These models allow the regulatory asset amount in the proxy to true up and have the revised billed amounts. Board staff inserted the minimum income tax rates in the SIMPIL models. Board staff calculated that the refund amount with interest to August 31, 2012 is \$250,041. Board staff requests that PSPC confirm that this is the correct calculation for the amount to be refunded should the Board approve the use of the minimum income tax rates and the other changes accepted by PSPC in response to interrogatories.

PSPC confirms that the Board Staff calculation is correct should the Board decide to utilize minimum tax rates for true-up purposes.