



EB-2007-0723

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 PUC
Distribution Inc., pursuant to section 78 of the Ontario
Energy Board Act seeking approval to amend electricity
distribution rates.

BEFORE: Paul Vlahos
Presiding Member

Paul Sommerville
Member

DECISION AND ORDER

The Application

On August 15, 2007, PUC Distribution Inc. ("PUC Distribution") filed an application with the Ontario Energy Board, (the "Board") under section 78 of the Ontario Energy Board Act, 1998, S.O. 1998, c.15 (Schedule B) to adjust its electricity distribution rates. The Board has assigned the application File No. EB-2007-0723.

The 2007 distribution rates for PUC Distribution, as for most other electricity distribution utilities in the Province, were established through the application of a formulaic mechanism on the 2006 rates, known as the 2nd Generation Incentive Regulation Mechanism. PUC Distribution's current application sought to correct what it considered to be an anomaly in its 2007 rates process.

Specifically, in the development of its 2007 rates the use of PUC Distribution's 2006 approved rates was inappropriate to allow for the full recovery of its expected 2007 Payments in Lieu of Taxes (PILs) for the following reasons:

1. the 2006 rates reflected an amount for a loss carry-forward of \$978,338 whereas only \$255,942 would be available in 2007;
2. there was no allowance in the 2006 rates to incorporate, as part of the PILs calculation, the \$1,450,000 in regulatory assets currently being received by the utility;
3. as a result of a change in the March 22, 2007 Ontario Budget, PUC Distribution's actual debt equity ratio (90/10) was replaced by a deemed debt equity ratio (50/50) in the calculation of PILS payable, effectively reducing the allowable deductible interest and increasing the resulting PILs liability.

Notice of Application was published on September 15, 2007. One party, the Vulnerable Energy Consumers Coalition ("VECC"), filed a request for intervention, which was granted.

On September 21, 2007, the Board issued an Interim Rate Order declaring PUC Distribution's current distribution rates interim, effective September 1, 2007.

The Board issued Procedural Order No. 1 on October 2, 2007, to allow parties to seek further information by way of interrogatories.

Interrogatories were served by Board staff and VECC on October 9, 2007. PUC Distribution responded to the interrogatories on October 21, 2007, and filed further information on November 26, 2007.

The Board issued Procedural Order No. 2 on November 13, 2007 in which the Board announced that it would proceed by way of a written hearing and set out the time schedule for submissions. VECC and Board Staff filed submissions on November 26, 2007 and November 29, 2007, respectively. PUC Distribution filed a reply submission on December 7, 2007.

The Board summarizes the submission below only to the extent necessary to provide context to its findings.

Submissions by Parties

VECC noted that the Board's 2nd Generation Incentive Regulation Mechanism made limited provision for adjustments to rates where factors beyond the control of the utility operated to unreasonably affect rates, known as Z-Factor adjustments. In VECC's view, only the interest adjustment incorporating the change in tax policy meets the definition of a Z-Factor, as that term is used in the Board Report establishing the 2006 Electricity Distribution Rate Handbook. In VECC's view, if PUC wanted the Board to consider the other adjustments it should have addressed them through a complete forward test year application, particularly where those adjustments proposed to incorporate 2007 budgeted values into the determination of PILs.

Board Staff submitted that PUC Distribution's request for the adjustment to 2007 rates to reflect the elimination of historical loss-carry forwards has been supported by PUC Distribution's evidence and is reasonable. Board Staff submitted that as a result of the change in the basis for the assessment of the amount of PILS payable in the March 22 Budget referenced above, use of the 2006 taxable net income as a basis for forecasting the 2007 taxable net income understates the 2007 forecast.

Both VECC and Board submitted that PUC Distribution's proposed inclusion of Regulatory Assets recovery amounts in calculating PILs is not consistent with Board policy and that the Board has already rejected this request by PUC Distribution when it set 2006 rates.

VECC argued that PUC Distribution's request to have the rates retroactive to May 1, 2007 is inappropriate and noted that, in similar circumstances, EnWin Utilities Limited had not made such request, to prevent retroactive ratemaking.

Board Findings

The Board finds that PUC Distribution's request for an adjustment to 2007 rates to reflect the reduction of the loss carry-forwards present in the 2006 rates is supported by PUC Distribution's evidence and submissions. The relief requested is tax-related and it addresses the fact that there is no provision in the current rates charged by PUC

Distribution for material changes in income taxes. This is an anomaly and a request to rectify it does not constitute, in the Board's view, any deviation from the letter or the spirit of Z-factor adjustments permitted by the Board as documented in the Board Report. The change in the Provincial Budget does affect PUC Distribution's interest for 2007 and the Board accepts the proposed adjustment. The Board also finds that using 2007 budgeted values is appropriate in these circumstances.

However, the provision for PILs should reflect the proper input with respect to Regulatory Assets. The Board has previously determined that Regulatory Asset recoveries should not be included in the PILs calculation for rate setting purposes. The Board Report establishing the 2006 Electricity Distribution Rate Handbook makes that quite clear. At page 61, the Report states:

A PILs or tax provision is not needed for the recovery of deferred regulatory asset costs, because the distributors have deducted, or will deduct, these costs in calculating taxable income in their tax returns.

In its decision dealing with a previous application by PUC Distribution Inc. (RP-2005-0020) for 2006 rates the Board reaffirmed its policy by and stating as follows:

The applicant included in the Revenue Requirement an amount of \$1,055,925 for its PILs costs in 2006. In making this calculation, PUC included as an addition to its net income the amount of \$1,486,250, which is the Regulatory Assets Recovery in 2006. The Board does not accept that this is a component of net income in 2006. Rather, it is a delayed recovery of costs of previous years that would have already been expensed for tax purposes.

The new evidence and arguments provided by PUC Distribution does not persuade the Board to deviate from its policy, which has been applied to all other electricity distributors.

PUC Distribution has requested that the new rates be implemented September 1, 2007 with a deferral account or other mechanism which would, in effect, make rates retroactive to May 1, 2007.

The issue of retroactivity has been dealt with by the Supreme Court of Canada in *Bell Canada v. Canada (Canadian Radio-Television and Telecommunications Commission)*

[1989] S.C.J. No. 68. The Court's decision in that case recognizes a tribunal's authority to order changes to rates reaching back to the date that the rates were declared interim, but no further. In granting interim rates for PUC Distribution effective September 1, 2007, the Board emphasized in its Interim Rate Order that "this action should in no way be construed as predictive, in any degree, of the final determination of this application". The Board is of the view that rate increases in this case should not be effective for any period prior to the time when ratepayers were actually informed of the potential rate increase or the effective date on which the rates were declared interim or the date of the order pursuant to which the rates were declared interim, whichever comes later. The effective date of the interim rates was September 1, 2007. The Notice was published on September 15, 2007. The date of the Interim Order declaring rates interim was September 21, 2007. Therefore the Board finds that the effective date for the adjusted rates is September 21, 2007.

Given the date of this Decision and the need for PUC Distribution to provide a proposed Tariff of Rates and Charges as part of a Draft Rate Order, the Board finds that February 1, 2008 will be the earliest practical implementation date.

This then leaves the question of recovery of foregone revenue pertaining to the September 21, 2007 to January 31, 2008 period. Given the implementation date of this Decision and the relatively short time period until PUC Distribution's rates should next be adjusted, and considering the additional bill impacts that would result if the foregone revenue was collected through a rate rider upon implementation of the new base rates, the Board is of the view that it is more appropriate that the notional revenues that would have flowed to the utility for the period September 21, 2007 to January 31, 2008 be recorded in a deferral account (Account 1574 – Deferred Rate Impact Amounts) for disposition at a later date.

THE BOARD ORDERS THAT:

1. PUC Distribution Inc. shall file with the Board, and serve the Vulnerable Energy Consumers Coalition a Draft Rate Order attaching proposed Tariff of Rates and Charges reflecting the Board's findings in this Decision, within 14 days of the date of this Decision.
2. The Vulnerable Energy Consumers Coalition shall file any comments on the Draft Rate Order with the Ontario Energy Board and serve PUC Distribution Inc. within 21 days of the date of this Decision.

3. The Vulnerable Energy Consumers Coalition shall file with the Ontario Energy Board and forward to PUC Distribution Inc. its cost claim within 21 days from the date of this Decision.
4. PUC Distribution Inc. may file with the Ontario Energy Board and serve the Vulnerable Energy Consumers Coalition any objection to the claimed costs within 35 days from the date of this Decision.
5. The Vulnerable Energy Consumers Coalition may file with the Ontario Energy Board and forward to PUC Distribution Inc. any response to any objection for cost claims within 42 days of the date of this Decision.

DATED at Toronto, January 8, 2008

ONTARIO ENERGY BOARD

Original signed by

Kirsten Walli
Board Secretary