Ontario Energy Board

Commission de l'Énergie de l'Ontario

**EB-2006-0501**

**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 Hydro One Networks Inc. for an Order or Orders approving or fixing just and reasonable rates and other charges for the transmission of electricity commencing January 1, 2007.

# PARTIAL DECISION AND ORDER

Hydro One Networks Inc. ("Hydro One" or the "Company") filed an Application, dated September 12, 2006, with the Ontario Energy Board under section 78 of the *Ontario Energy Board Act 1998, S.O. 1998*, c.15, Schedule B. The Board assigned file number EB-2006-0501 to the Application and issued a Notice of Application dated October 17, 2006.

By letter dated February 14, 2007 and in the February 23, 2007 update to its application, Hydro One requested that a 2007 revenue deficiency deferral account be established beginning January 1, 2007 to record the revenue deficiency between the approved revenue for 2007 and forecast revenues at currently approved transmission rates. Hydro One requested a decision from the Board on this issue by March 31, 2007.

On March 12, 2007 the Board issued Procedural Order #4 requesting that Hydro One make further submissions addressing the following issues:

- The need for the revenue deficiency deferral account;
- Why the issue of the account must be dealt with on an expedited basis;

- What will be booked into the account, and the accounting entries that are proposed to be made;
- The date upon which Hydro One proposes to start booking entries into the account; and
- What, if any, consequences follow if the account is not established at all, or is not established prior to March 31, 2007 as requested.

The procedural order also invited intervenors to respond to Hydro One's submissions and then provided for Hydro One's subsequent reply submissions.

**Hydro One Submissions:**

Hydro One, in its March 13, 2007 submissions, stated that the EB-2005-0501 transmission earnings sharing mechanism (ESM) was intended to end once new transmission rates were implemented. The establishment of the 2007 revenue deficiency deferral account (RDDA) beginning January 1, 2007, would replace and end the ESM.

Hydro One claimed that the proposed RDDA was more transparent than the ESM, and would be easier to justify and implement for a portion of a year (as un-audited financial results would be used.) In contrast, the part-year RDDA calculations would be based upon approved data consistent with Hydro One Transmission 2007 rate filing. A rates decision in late 2007 would lead to regulatory lag and uncertainty regarding Hydro One in financial markets. An RDDA was also consistent with the Great Lakes Power Limited (GLPL) deferral account (EB-2005-0241) granted in 2005. A decision by March 31, 2007 was requested due to first quarter financial reporting requirements to external investors.

Under the proposed plan, Hydro One submitted that no amounts would be recorded for the ESM in 2007; however, on a monthly basis, the deficiency between the proposed revenue 2007 requirement (per the Hydro One Transmission rate filing) and revenue calculated using current approved rates (by applying a weather normal monthly load forecast consistent with the 2007 load forecast) would be reflected in the deferral account. Monthly carrying costs would be applied to this entry using the short-term interest rate included in the 2007 revenue requirement. Disposition of the account would be subject to future OEB review and approval. Entries would be booked immediately upon receiving a favourable decision from the OEB reflecting the commencement date of January 1, 2007.

**Intervenors' Submissions:**

Four intervenors responded to the Hydro One submission. The Vulnerable Energy Consumers Coalition (VECC) and Schools Energy Coalition (SEC) argued against granting the account. The Association of Major Power Consumers (AMPCO) and the Power Workers Union (PWU) were supportive of the request.

VECC argued that approval of this account was retroactive ratemaking and should not be approved by the Board. The GLPL case should not be considered as a precedent in this application as the deferral account granted to GLPL was only one aspect of a comprehensive settlement agreement. In addition, the GLPL account only applied to deficiencies starting on April 1, 2005, not January 1. VECC also argued that if the account was granted, no interest should be collected in the account.

SEC argued that the Board does not have the authority to revisit rates. SEC noted that in the EB-2005-0501 ESM decision, the Board stated that it was reluctant to have existing rates declared interim and if the Board had meant the mechanism to last only until January 1, 2007, it would have said so. SEC indicated that it would be unfair to ratepayers to allow Hydro One to revisit rates during a period where it anticipates a revenue deficiency but not do so during a period of over-earning. SEC also mentioned the fact that the GLPL deferral account was part of a comprehensive settlement agreement. SEC also noted that recent decisions of the Board have refused to implement rates retroactively on basis that the applicant had not demonstrated that the delay in arriving at just and reasonable rates by the beginning of the test year was not due to factors within the applicant’s control, citing the January 2, 2007 Erie Thames Powerlines Corporation rate order.

AMPCO did not object to the establishment of the RDDA as this action would reassure investors that regulatory risk is minimal. AMPCO stressed that this approval should not pre-empt the Board’s hearing process or be misconstrued as prior approval of Hydro One’s revenue requirement. AMPCO submitted that any revenue deficiency calculation should be based on actual, non-weather corrected revenue under current rates and that the RDDA should be based only on continuance of program expenditures at the level Hydro One executed in 2006 and not on the increased levels being requested for 2007.

The PWU also supported the approval of the RDDA citing the need for utilities to have sufficient financial certainty so that they can carry out existing and new transmission work programs. The PWU also agreed with Hydro One that the RDDA was consistent with the GLPL decision and stated that the extended application of ESM for 2007 was inappropriate.

**Hydro One Reply Submissions:**

In its March 21, 2007 reply, Hydro One indicated that it was not requesting prior approval of its proposed 2007 programs or revenue requirements. Hydro One also submitted that SEC’s assertions regarding “retroactive rate increases” are not supported as the OEB is not retroactively setting rates and that it is not revisiting rates for a period during which final rates were in place. Hydro One also noted that the settlement agreement in the GLPL case was the basis for the final order issued November 14, 2005, while the deferral account was granted much earlier on March 22, 2005.

Hydro One also stated that it believes that by requiring the use of audited financial statements for the ESM calculations, the Board intended full year application of the ESM, not part year application.

Hydro One submitted that AMPCO's suggestions that the revenue deficiency be calculated on the basis of non-weather corrected actual 2007 revenue and to use 2006 actual program costs is inconsistent with typical regulatory practice and the GLPL decision. Hydro One also pointed out that the GLPL decision included carrying costs in the approved deferral account.

**Findings**

It often happens that rate proceedings occur within timeframes that do not coincide with the conventional rate period. This can occur for a variety of reasons. In such situations an issue arises as to when the rates approved by the Board will become effective. Determining the effective date for rates is an important aspect of the Board's jurisdiction, and it can have significance for Applicants and ratepayers.

It is clear that such a situation will arise this year with respect to the revenue requirement for Hydro One. It is likely that the final determination of its revenue requirement for 2007 will not be made until the latter half of 2007.

Deferral accounts, such as the one applied for by Hydro One in this proceeding, are 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.

In the case of the deferral account applied for by Hydro One, the unknown future event is the Board's final determination of the 2007 revenue requirement, the effective date governing that revenue requirement, and the terms and conditions imposed by the Board on the disposition, if any, of the amounts recorded in the deferral account.

Parties commenting on Hydro One's request for the Revenue Deficiency Deferral Account have raised issues respecting rate retroactivity, and have attempted to define with great particularity the terms and conditions that should govern the creation of the account, if the Board sees fit to approve its creation.

In the Board's view, the time to make these arguments is in the course of the revenue requirement proceeding per se, and, if necessary, at the time Hydro One seeks to have the amounts recorded in the account disposed of, so as to effect its revenue requirement or the resulting rates derived from it. Parties will be free to make whatever submissions they see fit as to the appropriateness of any disposition option.

At this stage, the Board is simply concerned with ensuring that the account meets the objective of administrative and accounting utility.

Accordingly, the Board approves the creation of a deferral account, effective January 1, 2007, to be referred to as the Revenue Difference Deferral Account. This account will record the sufficiency or deficiency arising from the difference between the 2006 Transmission rates, that is, rates that are currently in force, and the rates that would result from the new revenue requirement as determined by the Board in this proceeding. Parties will note that the Board has made the deferral account symmetrical to account for the possibility that the new revenue requirement as found by the Board may be lower than that which underpinned the 2006 rates.

In its materials, the Applicant referenced the Earnings Sharing Mechanism (ESM), which was instituted by a previous Board panel. In the Board's view, the creation of the deferral account as approved by the Board in this proceeding has the effect of terminating the ESM as of December 31, 2006. That is so because the Revenue Difference Deferral Account now accommodates the tracking of sufficiency as well as deficiency and this fact makes the continuation of the ESM unnecessary. If the new revenue requirement is higher than that underpinning the 2006 rates, the account will represent a credit to the utility to the extent of the difference. On the other hand, if the new revenue requirement is lower than that upon which the 2006 rates are based, the entire amount reflected in the account will be to the credit of ratepayers.

The final balance in the account will reflect a series of decisions made by the Board in its determination of the revenue requirement for 2007.

The Board's approval of the creation of this deferral account should not be construed in any degree as predictive of the quantum of, the terms of or the timing of the disposition, if any, of the contents of this account.

**THE BOARD THEREFORE ORDERS THAT:**

1. Hydro One shall establish a deferral account in which to record the differences in revenue between 2006 Transmission rates currently in force, and the rates that would result from the new revenue requirement as determined by the Board in this proceeding, beginning January 1, 2007. Hydro One is directed to prepare and submit a draft accounting order to the Board reflecting this order.

**DATED** at Toronto, March 30, 2007.

ONTARIO ENERGY BOARD

*Original signed by*

Peter H. O'Dell
Assistant Board Secretary