Ontario Energy Board
P.O. Box 2319
2300 Yonge Street
26th. Floor
Toronto ON M4P 1E4
Telephone: 416- 481-1967
Facsimile: 416- 440-7656
Toll free: 1-888-632-6273

Commission de l'Énergie de l'Ontario
C.P. 2319
2300, rue Yonge
26e étage
Toronto ON M4P 1E4
Téléphone; 416- 481-1967
Télécopieur: 416- 440-7656
Numéro sans frais: 1-888-632-6273

December 5, 2001

To: All Local Electricity Distribution Companies

Re: PILs Proxy for Inclusion in Rates March 1, 2002

The Board's correspondence of August 24, 2001 indicated that: local electricity distribution companies ("LDCs") should add the amount of their 2001 section 93 payments in lieu of taxes ("PILs") on the wires-only portion of LDC income to their application for annual rate adjustments ("ARA") to be effective March 1, 2002; an estimate of the utility's annualized tax expense for 2002 would have to be developed for inclusion in rates; a deferral account would be established to accommodate the inclusion of 2001 PILs into the March 1, 2002 ARA and the pass-through treatment of PILs referred to in the Board's Electricity Distribution Rate Handbook; and a consultation process would be conducted to provide further details on this approach.

Preliminary consultations were conducted with a working group comprised of members of the EDA to develop a methodology designed to calculate a provision for PILs to be included in rates, a deferral account mechanism, and monitoring details. In general, the methodology uses the wires-only earnings before interest and income tax (EBIT) adjusted for certain mandatory additions and deductions to determine income-related PILs, while capital-related PILs uses wires-only rate base adjusted for exempt amounts.

A utility's initial rate unbundling was accomplished using 1999 utility financial statements and adjusting the income for various amounts, such as interest. The Market Adjusted Revenue Requirement ("MARR"), derived using the Electricity Distribution Rate Handbook formulae, relied on 1999 financial information to calculate rate base, equity and debt. It follows that in providing for taxes on the MARR amounts, and on the capital amounts, that the 1999 financial statements should be the source of the calculations.

During the consultation it was noted that the revenue requirement associated with some payments-in-lieu of tax were subject to income tax. Gross-up is required since the Federal Large Corporation Tax (LCT) and income taxes are not deductible in computing income tax. Income taxes and LCT will be grossed up to permit the pass-through referred to in the Electricity Distribution Rate Handbook. By contrast, Ontario capital tax is a deductible expense for both Federal and Ontario income tax purposes; therefore, the actual amount (without gross-up) is the pass-through.

On December 6, 2001 the Board will have posted on its website (www.oeb.gov.on.ca) under "What's New?" a worksheet which indicates how to calculate income taxes, LCT and Ontario capital tax. The worksheet represents a full year filing requirement for PILs, from the inclusion of PILs in rates, to deferral account entry calculation, to monitoring requirements which will, in some circumstances, result in further deferral account entries. Also on the website are document files which contain footnotes/ instructions to the worksheet and an example of a utility's filing sequence for 2001 and 2002 (in six parts) to assist utilities in their examination of the material.

We request that you review the proposed methodology and submit six copies of any comments in writing to Paul Pudge, Board Secretary, Ontario Energy Board. In order to finalize the worksheets and instructions the Board must receive your comments no later than December 17, 2001. This will allow for the submission of the PILs data in conjunction with the annual rate adjustment process.

The Board is developing a Rate Adjustment Model (RAM) that will support the annual rate adjustment process. The revenue requirement associated with both 2001 and 2002 PILs will be inserted into the RAM. The PILs worksheets will provide part of the required evidentiary material to be submitted for consideration of the Board in order to approve just and reasonable rates for the rate year starting March 1, 2002.

Should you have questions please contact OEB Board staff:

Duncan Skinner	416-440-8127	skinnedu@oeb.gov.on.ca
John Vrantsidis	416-440-7613	vrantsjo@oeb.gov.on.ca

Yours truly,

Paul Pudge
Board Secretary
Ontario Energy Board