**GAZIFÈRE INC.**
**NUMERICAL PROOF (EXAMPLE)**
**RENEWAL OF THE INCENTIVE REGULATION MECHANISM**

## STEP 1
**Calculation of Net Income Before 50/50 Earnings Sharing**

**Before 50/50 Over-earnings Sharing**

| Line No. | | Col. 1A | Col. 1 ($000) |
|---|---|---|---|
| 1. | Revenue | | 5,000 |
| 2. | Gas costs | | 2,700 |
| 3. | Margin | | 2,300 |
| 4. | Other costs | | 1,000 |
| 5. | Depreciation | | 615 |
| 6. | Interest | | 200 |
| 7. | Utility accounting income before taxes | | 485 |
| 8. | Income taxes (below) | | 179 |
| 9. | Utility Net Income (Earnings) | | 306 |
| 10. | Net over-earnings for 50/50 sharing (306$ - 146$ allowed earnings) | | 160 |
| | Income tax calculation | | |
| 11. | Utility accounting income before taxes | | 485 |
| 12. | Tax add back depreciation | | 615 |
| 13. | Tax deduct CCA | | 500 |
| 14. | Taxable income | | 600 |
| 15. | Income tax @ nominal rate | 29.9% | 179 |
| 16. | Effective tax rate = calc. | 37.0% | |
| | Allowed Earnings Based on Actual Rate Base | | |
| 17. | Rate Base | | 4,050 |
| 18. | Equity level @ 40% | | 1,620 |
| 19. | Allowed Earnings @ 9% (Net Income) | | 146 |
| | **Resulting ratepayer & shareholder** | | |
| 20. | **50% share of net over-earnings** | | 80 |
| 21. | | | |
| 22. | **Gross overearnings for return to ratepayers** | | |

## SCENARIO A
**Assumes use of Nominal Tax Rate in determining gross earnings sharing**

**Utility Earnings After 50/50 Over-earnings Sharing**

| Line No. | | Col. 2A | Col. 2 ($000) |
|---|---|---|---|
| 1. | Revenue (original 5,000 - 114 ratepayer share) | | 4,886 |
| 2. | Gas costs | | 2,700 |
| 3. | Margin | | 2,186 |
| 4. | Other costs | | 1,000 |
| 5. | Depreciation | | 615 |
| 6. | Interest | | 200 |
| 7. | Utility accounting income before taxes | | 371 |
| 8. | Income taxes (below) | | 145 |
| 9. | Utility Net Income (Earnings) | | 226 |
| 10. | Net over-earnings for shareholder (should equal 80) | | 80 |
| | Income tax calculation | | |
| 11. | Utility accounting income before taxes | | 371 |
| 12. | Tax add back depreciation | | 615 |
| 13. | Tax deduct CCA | | 500 |
| 14. | Taxable income | | 486 |
| 15. | Income tax @ nominal rate | 29.9% | 145 |
| 16. | Effective tax rate = calc. | 39.2% | |
| | Allowed Earnings Based on Actual Rate Base | | |
| 17. | Rate Base | | 4,050 |
| 18. | Equity level @ 40% | | 1,620 |
| 19. | Allowed Earnings @ 9% (Net Income) | | 146 |
| | **Scenario A - Ratepayer share** | | |
| 20. | Ratepayer share of net over-earnings | | 80 |
| 21. | Gross up by reciprocal of **nominal** tax rate | | 70.10% |
| 22. | | | **114** |

## SCENARIO B
**Assumes use of Effective Tax Rate in determining gross earnings sharing**

**Utility Earnings After 50/50 Over-earnings Sharing**

| Line No. | | Col. 3A | Col. 3 ($000) |
|---|---|---|---|
| 1. | Revenue (original 5,000 - 127 ratepayer share) | | 4,873 |
| 2. | Gas costs | | 2,700 |
| 3. | Margin | | 2,173 |
| 4. | Other costs | | 1,000 |
| 5. | Depreciation | | 615 |
| 6. | Interest | | 200 |
| 7. | Utility accounting income before taxes | | 358 |
| 8. | Income taxes (below) | | 141 |
| 9. | Utility Net Income (Earnings) | | 217 |
| 10. | Net over-earnings for shareholder (should equal 80) | | 71 |
| | Income tax calculation | | |
| 11. | Utility accounting income before taxes | | 358 |
| 12. | Tax add back depreciation | | 615 |
| 13. | Tax deduct CCA | | 500 |
| 14. | Taxable income | | 473 |
| 15. | Income tax @ nominal rate | 29.9% | 141 |
| 16. | Effective tax rate = calc. | 39.5% | |
| | Allowed Earnings Based on Actual Rate Base | | |
| 17. | Rate Base | | 4,050 |
| 18. | Equity level @ 40% | | 1,620 |
| 19. | Allowed Earnings @ 9% (Net Income) | | 146 |
| | **Scenario B - Ratepayer share** | | |
| 20. | Ratepayer share of net over-earnings | | 80 |
| 21. | Gross up by reciprocal of **effective** tax rate | | 63.00% |
| 22. | | | **127** |