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April 30, 2007

BY COURIER

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St, Suite 2701
Toronto ON M4P 1E4

Dear Ms. Walli:

**Board File No. EB-2006-0064 – Setting OPG Payment Amounts
Energy Probe Comments on March 30, 2007 Staff Discussion Paper**

Please find attached three hard copies of the submissions of Energy Probe Research Foundation (Energy Probe) in response to the Board's letter dated March 30, 2007 inviting comments on the Staff Discussion Paper *Filing Requirements for Ontario Power Generation*. An electronic version in PDF format will be forwarded to the Board.

Should you have any questions or require additional information, please do not hesitate to contact me.

Yours truly,

David S. MacIntosh
Case Manager

cc. Interested parties (By email)

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Ontario Energy Board

Setting Payment Amounts for Ontario Power Generation Inc.'s Prescribed Generation Assets

Energy Probe Research Foundation

◆ Comments on Staff Discussion Paper ◆

Filing Requirements for Ontario Power Generation

Submitted April 30, 2007

**Board Staff Discussion Paper:
Filing Requirements for
Ontario Power Generation**

Comments of Energy Probe Research Foundation

Background

The following comments are provided on behalf of Energy Probe Research Foundation (Energy Probe) in response to the Board's invitation, by letter dated March 30, 2007, to provide comments on the staff's draft filing requirements in their discussion paper of March 30, 2007.

To assist in preparing comments, Energy Probe reviewed much of the material previously filed in this process, read the staff's Discussion Paper and reviewed material filed before the Ontario Legislature Standing Committee on Government Agencies in its Review of Ontario Power Generation (OPG) on February 26, 2007. Energy Probe appeared before the Committee in that Review, as did The Society of Energy Professionals and the Association of Power Consumers in Ontario (AMPCO).

In addition to reviews by the Ontario Legislature Standing Committee on Government Agencies, there have been two formal reviews of OPG within the last several years.

The Pickering "A" Review Panel was established in May of 2003 to investigate the causes for cost overruns and delays in returning Pickering A, Unit 4 to service in September 2003. Soon after the release of the Panel's report in December 2003, the Chair, CEO and Chief Operating Officer of OPG resigned.

Almost immediately the government created the OPG Review Committee to assess the appropriate future role and structure of OPG. In March of 2004, the report of the OPG Review Committee was released with a number of recommendations, some of which were not acted upon:

OPG focus on its major operating assets – nuclear, hydroelectric and fossil fuel – exiting non-core business such as wind power, solar, biomass and small hydro projects.

OPG be divided internally into two principle operating divisions, the nuclear division and the hydro/fossil division.¹

Some of the recommendations of the OPG Review Committee appear to have been acted upon, including the following:

OPG Board Members should be remunerated in line with the remuneration paid to members of boards of comparable private sector entities.

Instructions or similar directives given by the shareholder to OPG be in writing and be given as a matter of public record.²

The recommendation in March 2004 that the Ontario Energy Board independently approve the rates at which the output of each OPG operating division is sold³, was not fully implemented by the Ontario government, but this process is a partial response to that recommendation. It has been hard for the government to relinquish its total control over the crown operating units that were created in the wake of Ontario Hydro's financial demise.

Energy Probe has previously submitted comments at a number of junctures during EB-2006-0064. Without recapping the details, the overall theme of Energy Probe's comments has been to suggest that the public, the government, and OPG will be looking to the Board to develop a fair and transparent regulatory methodology that validates the process.

¹ OPG Review Committee, Transforming Ontario's Power Generation Company: Recommendations, March 2004.

² Ibid.

³ Ibid.

Discussion Paper Proposed Filing Requirements Framework

In the report issued by the Board on November 30, 2006, entitled *A Regulatory Methodology for Setting Payment Amounts for the Prescribed Generation Assets of Ontario Power Generation Inc.* (OPG Report), the Board outlined the regulatory steps it considered appropriate to implement. In response staff has developed draft filing requirements to support the Board's direction:

The Board has therefore concluded that the regulatory methodology to be used to set initial payment amounts for the prescribed generation assets will be a cost of service review, limited to OM&A and rate of return, with each of the nuclear and hydroelectric businesses being reviewed separately.⁴

Following the paragraph quoted immediately above, the Board laid out the components of the initial cost of service review separately for nuclear and hydroelectric prescribed generation. Further on in the OPG Report, the Board recognized that the initial proceeding would not be a typical cost of service review.⁵

In reviewing the Discussion Paper, Energy Probe observes that staff has interpreted the Board's direction for the initial cost of service review as follows:

As contemplated in the OPG Report, the Board will review the prescribed hydroelectric and nuclear generation assets in separate sequential proceedings. As a result, the filing requirements set out in Part 2 call upon OPG to make two separate filings, one for each class of assets. The Board may find it expedient to issue orders for each of these classes of assets also in sequence. If that is the case, each of those orders will be treated as the Board's first order for purposes of the application of Regulation 53/05.⁶

Energy Probe further notes that in the OPG Report, the Board's direction did not make even one reference to "separate sequential proceedings". That being so, it is the submission of Energy Probe that another framework would more effectively further Board's objectives in the initial cost of service review.

⁴ OPG Report, Page 11.

⁵ OPG Report, Page 12, Number 6.

⁶ Staff Discussion Paper, Page 3

Alternative Proposed Framework

In that part of the initial cost of service review dealing with Operation, Maintenance and Administration Costs (OM&A) and Rate of Return it would add to regulatory efficiency, and more importantly to regulatory effectiveness, to combine the review of the those portions of the nuclear and hydroelectric operating divisions that are prescribed within a Phase One procedure.

For the prescribed nuclear assets, this would entail 1. a), described by the OPG Report at the bottom of Page 11 as follows:

will set the payment amount through a limited issues cost of service proceeding that examines OM&A costs and rates of return on equity while accepting the value of other cost inputs for rate base determination as and to the extent required by Regulation 53/05

At the same time, for the prescribed hydroelectric assets it would include 2. a), described by the OPG Report at the top of Page 12:

will set a payment amount through a limited issues cost of service proceeding that examines OM&A costs and rates of return on equity while accepting the value of other cost inputs for rate base determination as and to the extent required by Regulation 53/05

It is anticipated that in the review of OM&A for those regulated portions of the nuclear and hydroelectric operating divisions, particular focus will be placed on the allocation of costs, not only as between the regulated nuclear and hydroelectric units, but to include allocation to the unregulated hydroelectric and fossil fuel operating units.

Two corporate factors lead to this suggested review format:

- a) the OPG corporate business model utilizes many centralized services, including real estate, human resources, finance, treasury, information technology, audit; and,**
- b) regulated and unregulated hydroelectric units are currently operating under the same management structure lead by a single OPG executive vice president, Mr. John Murphy.**

It appears that it would be both more efficient and more effective to examine and allocate nuclear and hydroelectric OM&A costs in a single procedure examining all OM&A costs across the OPG corporate structure.

A similar rationale applies to return on equity.

At an OPG Issues Conference and subsequent Issues Day, the areas of Operation, Maintenance and Administration Costs that are common to the nuclear and regulated hydroelectric business entities could be identified as combined Issues for the proceeding. Likewise, discrete OM&A matters could be identified as separate Issues for the same proceeding. Both sets of issues would be reviewed within Phase I.

The other components of the initial cost of service review could be examined in relative isolation in a Phase Two procedure, or in completely separate proceedings, as the Board sees fit. These items include 1. b) and 2. b), c) and d) as outlined on Pages 11 and 12 of the OPG Report.

An additional benefit of scheduling the initial review in this manner would be that there would not need to be a pause in the hearing schedule, waiting for a decision from the first proceeding before commencing the second proceeding in a sequential arrangement.

By way of example, holding sequential distribution (EB-2005-0501) and transmission (EB-2006-0501) hearings for Hydro One is functioning well due to a year's separation between the two proceedings. However, a number of issues that were examined in the distribution hearing were treated as settled for the transmission hearing, that is, the second hearing. A preamble was added to the transmission hearing issues list.

Preamble:

The panel in the Hydro One Networks Inc. distribution application (the ‘distribution decision’) made certain findings and observations that may be relevant to this application. Attached as Schedule 1 to the proposed issues list are excerpts from the distribution decision containing some such findings and observations. The schedule is for informational purposes only. It is not intended that this proceeding involve a re-examination of decisions made by the Board in the distribution case which are fully applicable to the transmission business.⁷

Once the initial cost of service review is completed, and well defined cost allocation methodology has been approved, it may not be necessary to duplicate this form of hearing for OPG:

After the first order is made, the Board will conduct a series of more typical cost of service proceedings with the objective of implementing an incentive regulation regime for payment orders that will be made post- 2010⁸

Energy Probe appreciates the opportunity to review and comment on the Staff Discussion Paper. Given the large financial impacts for consumers, Energy Probe submits that the Alternative Proposed Framework described above will provide a solid process for the Board to rely on in developing its decisions.

Respectfully submitted at Toronto, Ontario this 30th day of April, 2007.

Thomas Adams

⁷ EB-2006-0501 Hydro One Tx, Procedural Order No. 2, Appendix “A”, Approved Issues List

⁸ OPG Report, Page 12, Number 6.