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Please Reply to the TORONTO OFFICE

BY EMAIL

October 2, 2006
Our File No. 2060552

Ontario Energy Board
2300 Yonge Street
26th Floor
Toronto, Ontario
M4P 1E4

Attn: Kirsten Walli, Board Secretary

Dear Ms. Walli:

Re: Ontario Power Generation - Payments for Prescribed Assets – EB-2006-0064

We are counsel for the School Energy Coalition, and in this letter are providing our further comments on the issues in this matter, having heard the submissions in the Technical Conference on September 15, 2006.

Background

At the commencement of this process, the School Energy Coalition submitted that the only sensible approach to regulation of OPG's Prescribed Assets was cost of service, but we also identified as the main concern the inability to carry out proper cost of service within a reasonable time frame. We rejected a "limited issues" cost of service, because it is never in the Board's interest to do a slapdash job of regulation. A regulatory approach that trades off both thoroughness and transparency for expediency is not in the interest of the Board, the utility, or the ratepayers. In our initial submissions, we instead proposed a type of incremental cost of service, in which parts of the Prescribed Assets costs would be reviewed each year until all had been completed.

The final draft of the Staff Discussion Paper proposed a variation on cost of service that we believed had some advantages. In their variation, there would be no specific cost of service review, but cost of service type information would be filed on a regular basis, so that the Board and stakeholders could identify areas in which rates were not tracking costs, and areas in which costs appeared to be out of line with external or internal benchmarks and other comparisons. Action could then be taken as required, including reasonableness and prudence reviews, further benchmarking, etc. We

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believed then, and still do, that the high level of transparency and inherent flexibility of the staff proposal would ensure that within a reasonable time period OPG's payments for Prescribed Assets would be adjusted to match thoroughly reviewed costs, and true cost of service could then be implemented on a going forward basis.

At the Technical Conference, there was a fairly broad consensus among many parties that cost of service should be the goal for these assets. (We discount the proposals for regulatory contracts, which were not well thought out, had inconsistencies between them, and frankly did not appear to us to be credible.) However, OPG's view of cost of service is somewhat less rigorous than the traditional concept. OPG sought "limited issues" cost of service, effectively amounting to a free pass on most of their costs.

Comments on Cost of Service Proposals

Based on the submissions at the Technical Conference, it would appear clear that only OPG supports the notion of "limited issues" cost of service. In our view, this should be rejected by the Board. What OPG refers to as "limited issues" cost of service is, simply put, a proposal for an express abdication by the Board of its regulatory mandate. In the OPG proposal, the Board would consciously close its eyes to whether large parts of the costs of OPG are reasonable or prudent. This is not a viable option.

In our view, if OPG agrees that cost of service is the best approach, then it should be done right. OPG should file a full cost of service application, with all costs justified in the normal manner. Evidence would not be filed on a summary basis, but fully. No issues that had a material impact on the revenue requirement would be considered "non-hearing" issues. A full hearing process would be carried out, in which there would be identification of an issues list, interrogatories (and technical conference if required), ADR, oral hearing, and argument.

As we have indicated in our past submissions, we do not believe that it is possible for the Board to have rates in place for April 1, 2008 with full cost of service. It would appear from OPG's submissions at the Technical Conference that they would not be able to file a full application until perhaps the summer of 2007. Given the fact that their operations have not previously been regulated, we anticipated that the proceeding would take twelve months at the very least, and the decision a further three months after that. This suggests that new rates could be in place by January 1, 2009.

We do believe that a different form of "limited issues" cost of service might be acceptable. In somewhat the same way as we proposed in the spring, OPG could elect to file cost of service information on any part or parts of their operations, without filing on the rest. For example, they could provide a cost of service filing on their hydroelectric stations, but leave their thermal stations and any general administration costs alone.

Under this scenario, the revenue requirement would be the average normalized revenue for the years 2004 to 2006, with whatever volume-related adjustments as may be necessary. The projected hydroelectric components would then be compared to the hydroelectric costs in the three year average, and the delta, as approved by the Board after a cost of service review, would be added to

the revenue requirement for 2008. In effect, costs that were fully reviewed would be adjusted (upward or downward), and costs that were not reviewed would be frozen. In the next year, OPG would file for another part or parts of their operations, for example nuclear. The base revenue requirement before review would be the previous approved revenue requirement, including the part or parts that were already adjusted. After review, nuclear would be compared to the nuclear component of the base revenue requirement, and the delta added to or subtracted from the overall revenue requirement.

To prevent cherry-picking, we suggest that OPG would be required to select components of its operations that are logical divisions, such as splits by generating types. It should not be able to seek review of, for example, IT costs, employee wages, and fleet expenses, but nothing else (unless, of course, ratepayers could also select components for review on the same basis).

The approach we are describing here would operate in some respects like the incremental cost of service that we originally proposed, and in some respects like the “limited issues” cost of service proposed by OPG. The main difference between this and the OPG proposal is that, in our approach, each component of cost would remain at the historical level until it had been reviewed by the Board on a cost of service basis. OPG would be free to include as much of its operations as it wanted in cost of service, but would be trading off regulatory speed against the number of components reviewed.

Recommendation

After listening to the submissions at the Technical Conference, it would appear to us that the optimum solution is a full cost of service, with new rates in place at the beginning of 2009.

However, in the event that the Board seeks to have new rates in place earlier than that, in our view a “limited issues” cost of service is only appropriate if a) the costs reviewed are selected in a manner that avoids cherry-picking, and b) the revenue requirement for those costs not reviewed is fixed at the historical levels of actual spending.

Conclusion

We appreciate having had the opportunity to participate in this process.

Yours very truly,
SHIBLEY RIGHTON LLP

Jay Shepherd

Cc: Interested parties (by email)