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BY EMAIL

May 17, 2011

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge Street, Suite 2700
Toronto ON M4P 1E4

Dear Ms. Walli:

Re: Ontario Power Generation Inc. and School Energy Coalition Motions to Review and Vary Board Decision EB-2010-0008 Board File Number EB-2011-0090 and EB-2011-0091

Please find enclosed Board Staff's submission. Please forward the submission to Ontario Power Generation Inc., the School Energy Coalition and all other registered parties to these proceedings.

Yours truly,

Original signed by

Violet Binette
Project Advisor, Applications & Regulatory Audit

ONTARIO POWER GENERATION INC.
MOTION TO REVIEW AND VARY
DECISION WITH REASONS (EB-2010-0008)
EB-2011-0090

SCHOOL ENERGY COALITION
MOTION TO REVIEW AND VARY
DECISION WITH REASONS (EB-2010-0008)
EB-2011-0091

Board Staff Submission

May 17, 2011

Introduction

Ontario Power Generation Inc. ("OPG") filed an application, dated May 26, 2010, with the Ontario Energy Board under section 78.1 of the *Ontario Energy Board Act,1998,* S.O. 1998, c.15, Schedule B (the "Act") seeking approval for increases in payment amounts for the output of certain of its generating facilities, to be effective March 1, 2011. On March 10, 2011, the Board issued its Decision with Reasons ("Decision") on OPG's application for 2011-2012 payment amounts.

On March 30, 2011, OPG filed a Notice of Motion to review and vary the Decision in relation to the pension and other post employment benefits ("OPEB") costs, and in relation to OPG's request for a variance account for pension and OPEB costs. The Board assigned the OPG motion file number EB-2011-0090.

On March 30, 2011, the School Energy Coalition ("SEC") filed a Notice of Motion to review and vary the Decision in relation to tax matters, specifically the treatment of tax deductions taken by OPG prior to April 1, 2008 and disposition of the tax loss variance account. The Board assigned the SEC motion file number EB-2011-0091. This motion was subsequently withdrawn by SEC.

The Notice of Hearing and Procedural Order No. 1 issued on April 15, 2011, made provision for submissions on the threshold question and the merits of the motions, and established dates for the oral hearing. Procedural Order No. 2 issued on April 22, 2011, made provision for the filing of facta and revised the submission dates.

As SEC withdrew its motion on May 6, 2011, this submission only addresses OPG's motion.

The OPG Motion

OPG seeks a review of the Decision in which the Board did not accept OPG's update of the pension and OPEB costs, and did not accept OPG's request for a variance account. OPG seeks an order:

- Varying the finding that the pre-filed evidence was the best evidence of such costs on the record; and

- Establishing a variance account to record the difference between pension and OPEB costs reflected in approved payment amounts and actual pension and OPEB costs and associated tax impacts.

In the alternative, OPG seeks an order:

- Finding that the update was the best evidence of OPG's pension and OPEB costs and was therefore the appropriate amount to be used for the purposes of determining the pension and OPEB costs in OPG's test year revenue requirement; and
- Establishing a deferral account to record the difference between the pension and OPEB costs in the pre-filed evidence and the update, and associated tax impacts.

The Threshold

Rule 45.01 of the Board's Rules of Practice and Procedure states:

> In respect of a motion brought under Rule 42.01, the Board may determine, with or without a hearing, a threshold question of whether the matter should be reviewed before conducting any review on the merits.

Rule 44.01(a) provides the grounds upon which a motion may be raised with the Board:

> Every notice of a motion made under Rule 42.01, in addition to the requirements under Rule 8.02, shall:
>
> (a) set out the grounds for the motion that raise a question as to the correctness of the order or decision, which grounds may include:
>
> (i) error in fact;
> (ii) change in circumstances;
> (iii) new facts that have arisen;
> (iv) facts that were not previously placed in evidence in the proceeding and could not have been discovered by reasonable diligence at the time.

The Board's most thorough analysis of Rule 45.01 came from a decision on several motions filed in the *Natural Gas Electricity Interface Review Decision* ("NGEIR Review Decision")[1].

> Therefore, the grounds must "raise a question as to the correctness of the order or decision". In the panel's view, the purpose of the threshold test is to determine whether the grounds raise such a question. This panel must also decide whether there is enough substance to the issues raised such that a review based on those issues could result in the Board deciding that the decision should be varied, cancelled or suspended.
>
> With respect to the question of the correctness of the decision, the Board agrees with the parties who argued that there must be an identifiable error in the decision and that a review is not an opportunity for a party to reargue the case.
>
> In demonstrating that there is an error, the applicant must be able to show that the findings are contrary to the evidence that was before the panel, that the panel failed to address a material issue, that the panel made inconsistent findings, or something of a similar nature. It is not enough to argue that conflicting evidence should have been interpreted differently.
>
> The applicant must also be able to demonstrate that the alleged error is material and relevant to the outcome of the decision, and that if the error is corrected, the reviewing panel would change the outcome of the decision.
>
> In the Board's view, a motion to review cannot succeed in varying the outcome of the decision if the moving party cannot satisfy these tests, and in that case, there would be no useful purpose in proceeding with the motion to review.

Board staff submits that the threshold has been met in this proceeding, and that the Board should hear the motion on its merits. The essence of OPG's argument is that the Board's findings are contrary to the evidence, in that the Board (in OPG's view) improperly determined that the pre-filed evidence was better evidence than the update. There is little question that the decision to rely on the pre-filed evidence was both relevant to the decision and had a material impact. Although Board staff is ultimately of the view that the motion should be dismissed, it is not a spurious motion. Board staff submits that it passes the threshold test as established in the Board's *Rules of Practice and Procedure* and the NGEIR Review Decision, and should be heard on its merits.

[1] Motions to Review the *Natural Gas Electricity Interface Review Decision*, EB-2006-0322/0338/0340, May 22, 2007, p. 18.

The test on a motion to review is whether the moving party is able to demonstrate that there is good reason to doubt the correctness of the original decision. In the current motion, Board staff submits that the onus lies with OPG to demonstrate that the Board was incorrect to rely on the evidence as originally filed – in other words that relying on the original evidence was not within the range of options reasonably open to the Decision panel. A motion to review is not a hearing *de novo*, and the task before the review panel is not necessarily to substitute its own judgment for that of the Decision panel. Only if the review panel determines that the finding reached by the Decision panel was not within the range of reasonable alternatives should its decision be overturned.

Alleged Errors in Fact – the Board's reliance on the pre-filed evidence as the "best evidence"

By way of an impact statement filed on September 30, 2010 (the "Update")[2], OPG forecast that test period pension and OPEB costs increased by $264.2 million over the $633 million forecast in the application filed on May 26, 2010. The Board did not allow for recovery of the additional $264.2 million in the Decision, as it held that the pre-filed evidence was better evidence than the Update.

In the motion, OPG states that the Board erred in concluding that:

- The Update was less rigorous and not internally consistent and that it reflected the change of only one variable, such that it was not the best evidence of OPG's forecast pension and OPEB costs for the test period; and
- The Update was a selective update.

Board staff submits that there are no identifiable errors or inconsistent findings in the Decision on pension and OPEB costs, and that the OPG motion should be dismissed.

The Update

The test period pension and OPEB costs provided in the Update were projected by external actuaries at the end of August 2010 (the "Mercer Projection").[3] The evidence

[2] EB-2010-0008, Exh. N-1-1.
[3] EB-2010-0008, Exh. H1-3-1, Attachment 1.

provided in the Mercer Projection was subject to a variety of qualifications and caveats, for example:

- Page 2 of the cover letter: Actual discount rates and market conditions as at January 1, 2011 and January 1, 2012 may result in the 2011 and 2012 benefit expense being different than projected.
- Page 2 of Appendix B: The employer contributions for 2011 are based on a projected financial position at January 1, 2011 under both a going concern and a solvency basis (i.e. the bases on which OPG's minimum contribution requirements are determined). Actual experience to January 1, 2011 and market conditions as at January 1, 2011 may result in the 2011 minimum contribution requirements being more or less than the $480 million assumed.
- Page 2 of Appendix B: Based on the estimated financial position of the RPP [Registered Pension Plan] at January 1, 2011, it is likely that OPG will be required to file valuation reports for the RPP on an annual basis. Thus it is assumed that another valuation would be required as at January 1, 2012. Actual experience to, and market conditions at, that date may result in the 2012 minimum contribution requirements being more or less than the $530 million assumed.
- Page 3 of Appendix B: As noted, due to the nature of the terminal accounting approach and the sensitivity of results to changes in demographic data it is difficult to project the post employment benefits expense and actual results will likely vary from those presented.

Board staff submits that the qualifications and caveats listed above reflect the variability of financial market conditions and are consistent with the Decision panel's observations.

In addition to the above qualifications and caveats, Board staff also questions the following assumption at page 2 of Appendix B of the Mercer Projection:

> In the calculation of the market-related value of assets at the end of 2010, we have taken into account the market conditions up to August 31, 2010 and assumed the market return on equities would be 0.0% during the last four months of 2010.

2010 Year-End Results

Para. 18 of Mr. Reeve's affidavit states that:

> …based on OPG's most recent estimates, as of the end of February 2011, pension and OPEB costs for the regulated facilities for the test period are

> forecast to be $840.7M, an increase of $207.7M from the Pre-filed Evidence.

It is Board staff's understanding that Mr. Reeve's reference to the end of February 2011 refers to the data which OPG presented in its 2010 Year-End Results, issued on March 4, 2011. These materials were not filed in the original proceeding (they were not available), and were also not provided with the review motion. However, as they were discussed in Mr. Reeve's affidavit, Board staff will address this issue.

Board staff has reviewed the pension and OPEB information in these year end results at Note 12.[4] The cost recognized for 2010 is the sum of $125 million for Registered Pension Plans, $20 million for Supplementary Pension Plans, and $180 million for Other Post Employment Benefits. The total cost recognized of $325 million is the pension and OPEB cost for OPG corporate wide. Board staff assumes that the regulated hydroelectric business and nuclear business represent 78% of those costs, or $253 million.

The pre-filed evidence at Exh. F4-3-1, Chart 9 listed a 2010 bridge year expense for pension and OPEB of $258.4 million. As the 2010 pension and OPEB expense forecast in the pre-filed evidence is similar to the actual cost recognized in the 2010 Year-End Results, this indicates that the net effect of the suite of assumptions when the 2011-2012 payment amounts application was filed was similar to that at year end 2010. On this basis, Board staff questions OPG's assertion that pension and OPEB costs for the test period will exceed the pre-filed evidence by $207.7 million. It is not clear from the affidavit how this conclusion was reached. The 2010 year end result is consistent with the Decision panel's observation that, "financial market conditions are variable and have indeed improved since the impact statement was filed."[5]

Board staff has also reviewed the change in plan assets reported in the 2010 Year End results. The fair value of the plan at the beginning of 2010 was $8,216 million and was $9,118 million at the end of 2010. These results indicate healthy plan performance and they are in contrast to the Mercer Projection assumption of 0.0% return for the last four months of 2010 that was provided in the Update.

[4] 2010 Year-End Results, p. 115.
[5] Decision with Reasons, EB-2010-0008, p. 91.

Although this is to some extent an exercise in hindsight review, it was raised in Mr. Reeve's affidavit and demonstrates that the Board's decision was not based on unreliable evidence.

Conclusion with respect to "best evidence"

Accordingly, OPG has not demonstrated that the Update is better or more reliable than the pre-filed evidence.

Board staff submits that during the proceeding, the Board had two estimates of pension and OPEB costs from which the Board, by applying its considerable regulatory expertise, could select an appropriate dollar amount to be recovered from ratepayers. The Board determined on reasonable grounds that the pre-filed evidence was preferable to the Update.

At paragraphs 19-21 of the notice of motion, OPG highlights what it regards as unfairness in that the Board accepted two of the three proposed updates: namely the Canadian Nuclear Safety Commission ("CNSC") fees and changes to management compensation.

Board staff submits that unlike the pension and OPEB cost update, the CNSC fees and management compensation updates have a high degree of certainty. The September 30, 2010 Update stated that CNSC informed OPG of an increase in regulatory fees for the test period. The Update also stated that OPG was removing the management wage escalation for the period to April 1, 2012, as a result of the *Public Sector Compensation Restraint Act*. The CNSC fees and management compensation impact would not change if the Update were re-filed one month later, while the pension and OPEB cost update would be different one month later. The Decision noted that bond yields had changed and the financial market conditions are variable and had improved. Board staff submits that the Decision panel was not unfair or inconsistent in updating the CNSC fees and management compensation impact, but not accepting the update for pension and OPEB costs.

Internally Consistent

At para. 13 of the notice of motion, OPG states that the Board incorrectly concluded that the Update was not performed on an internally consistent basis. Para. 14 – 16, and the affidavit of Mr. Nathan Reeve, explain the methodology that OPG applied to calculate the updated pension and OPEB forecast of test period costs. OPG stated that it confirmed that the methodology is consistent with the methodology applied to calculate the pension and OPEB costs provided in the pre-filed evidence. Mr. Reeve's affidavit provides a summary of the assumptions that were reviewed to prepare the Update. They are: discount rates, inflation rate, salary schedule escalation rate, expected long-term rate of return on pension fund assets, actual return on pension fund assets in the prior year(s) and pension and OPEB cost distribution. Board staff submits that the finding does not question that this review was completed. However, Board staff notes that the 2011-2012 payment amounts application was based on the 2010-2014 business plan, as summarized in OPG's Argument in Chief:

> This Application is based on the forecasts contained in OPG's 2010 - 2014 **Business Plan** (emphasis added). This plan was developed following a robust planning and budgeting process, designed to contain costs while ensuring the safe and reliable production of electricity. The result is an application that gives rise to a modest increase over the payment amounts approved for 2008. OPG submits that its request is reasonable and should be approved.[6]

At Exh. F4-3-1 page 21 of the pre-filed evidence, the assumptions and budget setting for pension and OPEB costs is provided:

> To project OPG's total pension and OPEB costs **for business planning purposes** (emphasis added), it is necessary to estimate the value of the obligations and the pension fund assets at the end of each year preceding each of the years in the forecast period. This requires making projections of the actual pension fund performance and of the assumptions that will be used to determine the costs

Para. 5 of Mr. Reeve's affidavit states:

> In the Update, OPG stated that the $633M pension and OPEB cost forecast included in the Pre-filed Evidence was based on discount rates (presented in Chart 8 of Ex. F4-T3-S1) forecast during the 2010-2014 **business planning process** (emphasis added) which was finalized during the fall of 2009.

[6] EB-2010-0008, Argument in Chief, p. 2.

Board staff submits that OPG's evidence was that it conducted a multi step business planning process upon which the 2011-2012 payment amounts application was based. There were economic and business planning assumptions upon which the business plan is based. The process was reviewed with OPG witnesses during the EB-2010-0008 oral hearing and is the subject of chapter 2 of the Decision.

The evidence before the Decision panel was that the business plan underpinning the application was developed in a coordinated internal process, and approved by OPG's Board of Directors and shareholder. Board staff submits that pension and OPEB costs are one of the elements considered in and affected by the development of the 2010-2014 business plan. The application was further reviewed by OPG in May 2010 to identify ways to further lessen the impact on rate payers. Accordingly, the pre-filed pension and OPEB costs are more internally consistent than the Update.

Variance Account

At para. 18 of the motion, OPG states that the Board incorrectly concluded that pension and OPEB costs can be forecast in the same way as other OM&A costs and that any variance can be managed within OPG's overall operations. OPG also states that changes to the discount rate and the performance of the pension fund are factors not subject to the control of OPG management.

Board staff observes that all the regulated utilities with registered pension plans forecast pension and OPEB costs for a test period. With one exception[7], these utilities manage the costs without a variance account. The single exception is a variance account for pension cost variances only. OPG's request for a variance account was denied in the 2008-2009 payment amounts case, and was also denied in the 2011-2012 payment amounts case. The Decision stated that, "Pension and OPEB costs should be included in the forecast of expenses in the same way as other OM&A expenses, and then managed by the company within its overall operations."

Board staff observes that the Board has been consistent in its decisions to deny variance accounts for pension and OPEB costs, and that in circumstances where an account is approved, such as Hydro One transmission and distribution, the Board has

[7] Hydro One Networks Inc. Distribution, RP-2004-0180/EB-2004-0270, Hydro One Networks Inc. Transmission, EB-2006-0501.

limited the scope of the account. The Board made no error in denying OPG's request for this account. OPG may not like the result, but it has not pointed to a reviewable error.

As noted in Exh. F4-3-1 of the pre-filed evidence and transcript Vol. 10, page 183 (provided as Tab 7 of the OPG motion), the discount rate provided by actuaries may be adjusted by 25 basis points and it is OPG's responsibility to set and determine the discount rate. Accordingly, OPG management has some control of the discount rate it uses for forecasting purposes. Also, as noted in the Mercer Projections at page 3 of Appendix B, "For purposes of determining the financial position on a solvency basis, it has been assumed that OPG will elect to smooth assets and liabilities, as currently permitted under Ontario regulations. It is our understanding that OPG will evaluate this option when the January 1, 2011 funding valuation is being prepared and <u>will decide at that time whether to make such an election</u>." (emphasis added) This statement demonstrates that OPG has some influence over the assumptions that the actuary must follow and the degree of uncertainty for the actuary.

If the review panel is inclined to approve a variance account, the use of the account and the appropriate entries would need to be defined by the Board.

Conclusion

It is Board staff's position that the OPG motion does not identify errors or inconsistent findings or introduce material new information not considered by the Decision panel and the motion should be denied.

All of which is respectfully submitted