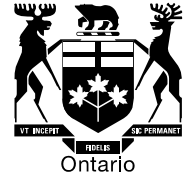


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BY EMAIL

April 2, 2012

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.
Niagara Tunnel Project Prudence Review
2013-2014 Payment Amounts
Board File No. EB-2012-0002**

Please find attached the comments of Board staff.

Yours truly,

Original signed by

Violet Binette
Project Advisor, Applications & Regulatory Audit

ONTARIO POWER GENERATION INC.
Niagara Tunnel Project Prudence Review
2013-2014 Payment Amounts

EB-2012-0002

Board Staff Comments

April 2, 2012

Introduction

Section 78.1 of the *Ontario Energy Board Act, 1998* (the “Act”) authorizes the Ontario Energy Board (the “Board”) to set payments to be made to Ontario Power Generation (“OPG”) with respect to the output of the prescribed generation facilities. Ontario Regulation 53/05, *Payments Under Section 78.1 of the Act Regulation*, states that the “Board may establish the form, methodology, assumptions and calculations used in making an order that determines payment amounts for the purpose of section 78.1 of the Act.” The Board has issued filing guidelines for each of OPG’s cost of service applications.

The Board released the most recent *Filing Guidelines for Ontario Power Generation Inc. in Setting Payment Amounts for Prescribed Generation Facilities* (the “Filing Guidelines”) on November 11, 2011. The Filing Guidelines set out the information that the Board expects OPG to file for purposes of the setting of payment amounts for 2013-2014 for certain of OPG’s generation assets under section 78.1 of the Act.

On March 12, 2012, OPG filed correspondence with the Board seeking the Board’s concurrence with OPG’s proposal to file a separate application in 2013 to review the reasonableness of the costs associated with the Niagara Tunnel Project (“NTP”). OPG states that the rate base impact of the NTP is standalone and severable from the balance of the payment amounts application. OPG anticipates recovery of NTP costs via a rate rider, and states that the overall ratepayer impact as determined in a separate proceeding will be the same as it would be if the NTP is considered as part of the 2013-2014 payment amounts application.

On March 26, 2012, the Board invited comments on OPG’s NTP proposal from parties to the 2013-2014 Filing Guidelines consultation, EB-2011-0286. In particular, the Board sought an understanding of whether any party is materially affected in an adverse way, or whether the 2013-2014 payment amounts proceeding is adversely affected by deferring the review of the NTP by one year.

Board staff supports OPG’s proposal, subject to resolution of certain matters. The following are Board staff’s comments on the proposal.

Board Staff Comments

Proposal Benefits

While the in-service date for the NTP is expected to be within the test period, OPG states that a separate, dedicated proceeding in 2013 is appropriate for reasons which include:

- NTP will be the largest capital project ever to come before the Board for prudence review;
- Construction began in 2005 and will be completed in 2013. The Board, intervenors and OPG will all benefit from a focused review of the complex project;
- The 2013-2014 payment amounts application will feature a number of significant issues. Including NTP prudence review would extend the proceeding and add to its complexity; and
- OPG proposes to file the NTP application in the spring of 2013. Project cost and schedule will be more certain at that time.

Board staff notes that while the final cost of the project is not yet known with certainty, the OPG approved budget for the project is \$1.6 billion.¹

If OPG proceeds with a separate proceeding for the review of the NTP, the 2013-2014 payment amounts application would not meet the “form, methodology, assumptions and calculations” set out in the Filing Guidelines. For example, the exhibits and continuity statements outlined in the Filing Guidelines related to rate base, capital projects, cost of capital and rate of return would, in the normal course, include the impact of the NTP because it is scheduled to be in service during the test period.

While it is reasonable to assume that the Board expected the prudence review to be part of the 2013-2014 payment amounts proceeding given the December 2013 in-service date, it is Board staff’s view that OPG’s proposal is a reasonable approach. Board staff agrees with all of OPG’s reasons noted above and in Board staff’s view, OPG’s proposal would allow parties more time and flexibility in deploying their resources for the review of the remaining priority issues; addressing a concern that was identified by the Board in the 2011-2012 payment amounts decision.

¹ Ontario Power Generation Inc. 2011 Financial Results, March 2, 2012, p16.

Efficiency

Board staff notes that the Board has made a specific effort to improve efficiency for the 2013-2014 payment amounts application. The Board plans to implement an issues prioritization process with the objective of identifying the highest priority issues early in the proceeding. The prioritization process is a response to a concern raised in the 2011-2012 decision in which the Board stated that “an inordinate focus on lower priority issues diminishes the time and resources available to pursue the more substantive, higher priority issues.” Separating the review of the NTP into a separate proceeding is consistent with the establishment of priority issues so that the Board can ensure that time and resources are allocated appropriately. Given the magnitude of the costs for the NTP, the Board’s review could be enhanced by the additional focus within a separate proceeding.

Severability of NTP

In the correspondence filed on March 12, 2012, OPG stated that it would exclude forecast NTP rate base, return on rate base and depreciation from the 2013-2014 payment amounts application, and that “OPG also will account for the associated production and tax impacts.” Board staff assumes that the latter means that OPG will also exclude NTP production and tax impacts from the 2013-2014 payment amounts application. Board staff invites OPG to confirm this assumption in its response.

Board staff has some concerns as to whether the NTP project would have an impact on surplus baseload generation (“SBG”), hydroelectric incentive mechanism (“HIM”), SBG variance account and HIM variance account; and that this might cause parties to raise and re-examine hydroelectric production related matters in the NTP proceeding. Board staff encourages OPG to comment on this in its response.

OPG proposes that the 2013-2014 payment amounts be set without consideration of the NTP and that a 2014 rate rider be developed as part of the 2013 prudence review of the NTP. OPG may wish to clarify in its response as to whether the cost of capital parameters OPG will propose to use for the separate NTP application are the same as those OPG will propose for the 2013-2014 payment amounts. In other words, whether OPG will be proposing the cost of capital parameters for the NTP in the main payments proceeding or as part of the separate proceeding should be clarified.

Alternative Processes

In its response, OPG may also wish to comment on whether it considered any alternative processes to two separate and distinct applications.

OPG may wish to comment specifically on a phased approach to the next payment amounts proceeding as an alternative. Phase 1 would deal with the “all but NTP” and phase 2 would address the NTP. A two phase proceeding would be more consistent with the spirit of the Filing Guidelines and would also lessen any payment amount (rate-making) complexities that may arise if concerns are raised about the full severability of the NTP from the 2013-2014 payment amounts. The phased approach however could require OPG’s payment amounts to be set on an interim basis pending the outcome of phase 2. If this approach is adopted by the Board, Board staff would recommend that the Board limit the interim nature of the payment amounts in such a way as to eliminate the possibility of re-hearing in phase 2 any issues not related to the impact of the NTP.

In this context, OPG may also wish to clarify whether it is also seeking the Board’s approval at this time of the mechanism that would be used to recover the revenue requirement impact of the NTP, should the Board decide to hear the matter separately. Board staff asks that OPG in its response clarify whether the rate rider reference is presented as an alternative as to how the additional revenue requirement can be recovered and does not preclude other options. These would include, for example, making the payment amounts ordered in the 2013-2014 proceeding (i.e. all but NTP) interim and finalizing them once the NTP evidence is heard and the impact on the 2013-2014 payment amounts has been determined. This would eliminate the need for additional rate riders and result in final base payment amounts that reflect the true underpinning revenue requirement.

In summary, Board staff agrees that there is merit to OPG’s proposal for a separate prudence review of the NTP, and requests that OPG clarify and respond to the matters identified by staff in these comments to assist the Board in its determination of OPG’s request.