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March 31, 2008

BY EMAIL & BY COURIER

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

Ms. Walli:

### **Board File No. EB-2007-0905**

### **Payment Amounts for Ontario Power Generation Inc.'s Prescribed Facilities Energy Probe Interrogatories Set # 2**

Attached please find two hard copies of Set # 2 of the Interrogatories of Energy Probe Research Foundation (Energy Probe) in response to Procedural Order No. 2, issued March 20, 2008. An electronic version of this communication will be forwarded in PDF and Word formats.

Should you require additional information, please do not hesitate to contact me.

Yours truly,

David S. MacIntosh  
Case Manager

cc. Barbara Reuber, Ontario Power Generation Inc. (By email)  
Michael A. Penny, Torsys LLP (By email)  
Josephina D. Erzetic, Ontario Power Generation Inc. (By email)  
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**Ontario Energy Board**

**IN THE MATTER OF** the *Ontario Energy Board Act, 1998*;  
S.O. 1998, c. 15, (Schedule B);

**AND IN THE MATTER OF** an Application by Ontario  
Power Generation Inc. pursuant to section 78.1 of the *Ontario  
Energy Board Act, 1998* for an Order or Orders determining  
payment amounts for the output of certain of its generating  
facilities.

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**INTERROGATORIES OF  
ENERGY PROBE RESEARCH FOUNDATION  
("ENERGY PROBE")**

**SET NUMBER 2**

**March 31, 2008**

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**ONTARIO POWER GENERATION INC.  
DETERMINING PAYMENT AMOUNTS  
EB-2007-0905**

**ENERGY PROBE RESEARCH FOUNDATION  
INTERROGATORIES – SET NUMBER 2**

**Interrogatory # 16**

**Ref:** Exh. B1/T 1/S 1, p. 1 of 8

**Issue 1.1:** Is the rate base appropriately determined in accordance with regulatory and accounting requirements?

The Prefiled Evidence indicates that the Prescribed Facilities be held, and the associated business activities will be conducted, within OPG. This appears to create complications of separating those facilities and their financial activities from the other parts of OPG.

Does the commingling give rise to allocations and reconciliations of financial information that affect the determination of the rate base and revenue requirements of the Prescribed Facilities?

**Interrogatory # 17**

**Ref:** Exh. D3/T 1/S 1, Table 1

**Issue 1.1:** Is the rate base appropriately determined in accordance with regulatory and accounting requirements?

According to the Prefiled Evidence, capital expenditures by certain of OPG's Corporate Groups are to be made on assets related to (or that impact on) the Prescribed Facilities.

Are any of these assets included in the rate base? If so, please identify the total relevant capital expenditure, as shown in Table 1, on those assets for the test period.

### **Interrogatory # 18**

**Ref:** Exh. B3/T 1/S 1, Table 2

**Issue 1.1:** Is the rate base appropriately determined in accordance with regulatory and accounting requirements?

The Prefiled Evidence presents information on the working capital component of the rate base in 2008 on a calendar-year basis rather than on a test-period basis.

What is the level of working capital (cash, fuel, materials and supplies) in the rate base for nuclear as of the beginning of the Test Period March 1, 2008?

### **Interrogatory # 19**

**Ref:** Exh. B1/T 1/S 1, p. 1 of 8

**Issue 1.1:** Is the rate base appropriately determined in accordance with regulatory and accounting requirements?

The Prefiled Evidence indicates that the Prescribed Facilities be held, and the associated business activities will be conducted, within OPG. This appears to create complications of separating those facilities and their financial activities from the other parts of OPG.

- a) Does OPG currently operate or invest in businesses through subsidiaries? If so, please identify those businesses and investments.
- b) Suppose, in order to maintain the approved debt/equity ratio for the Prescribed Facilities, OPG paid a dividend. Apart from the reporting on OPG's financial statement, how would this dividend affect the activities and financial condition of the Prescribed Facilities?

## **Interrogatory # 20**

**Ref:** Exh. C2/T 1/S 1, p. 122 of 261

**Issue 2.1:** What is the appropriate capital structure for OPG's regulated business for the 2008 and 2009 test years? Should the same capital structure be used for both OPG's regulated hydroelectric and nuclear businesses? If not, what capital structure is appropriate for each business?

The expert opinion on capital structure and fair return on equity states that it is important that the proposed deemed capital structure avoids potential cross-subsidization and proposes a formula at footnote 118.

- a) Does the formula indicate the capital structure that results in no cross-subsidization? If not, how does the formula contribute to avoiding cross-subsidization?
- b) What other measures, if any, in addition to deeming a capital structure for the regulated activity would be required avoid cross-subsidization with non-regulated activities within the same corporate entity? For example, would separate financial accounts be necessary?

## **Interrogatory # 21**

**Ref:** Exh. C2/T 1/S 1, p. 11 of 261

**Issue 2.4** Are OPG's proposed costs for its long-term and short-term debt components of its capital structure appropriate?

- a) Following the stand-alone principle, should the Prescribed Facilities be financed on terms and conditions appropriate to those assets and activities as established by financial markets, or should they be financed on terms and conditions at which OPG can finance if they are more favourable?
- b) Is the debt associated with the Prescribed Facilities supported by any form of implicit guarantee of the Ontario Government? If so, what are the implications for the appropriate capital structure for those assets?

## **Interrogatory # 22**

**Ref: Exh. C2/T 1/S 1, pp. 1-261**

**Issue 2.2: What is the appropriate return on equity (ROE) for OPG's regulated business for the 2008 and 2009 test years? Should the ROE be the same for both OPG's regulated hydroelectric and nuclear businesses? If not, what is the appropriate ROE for each business?**

- a) Does OPG or its expert rely on a forecast of the rate inflation that is reflected in the nominal expected rates of return on debt and equity for which it is seeking approval? If so, please provide details of these inflation expectations and any studies that have been relied upon.**
- b) Please provide copies of all financial analysts' reports and bond rating agency reports that were relied upon in establishing the recommended return on equity.**
- c) Please identify the Bank of Canada series numbers for T-bill rates in Schedule 1: Trends in Interest Rates and Outstanding Bond Yields (Exh.C2/T 1/S 1, p. 214).**
- d) Is the 12.5% fair return on equity for a benchmark Canadian utility based on the comparable earnings test (Exh.C2/T 1/S 1, p. 50) a return on the book value of equity or the market value of equity?**
- e) Are the returns on equity based on the equity risk premium test and on the discounted cash flow test (Exh.C2/T 1/S 1, p. 50) returns on book value of equity or the market value of equity?**
- f) Please indicate how the results of the comparable earnings test were used to adjust the returns obtained by the other methods to produce the recommended 10.5% equity return. (Exh.C2/T 1/S 1, p. 51)**

### **Interrogatory # 23**

**Ref:** Exh. D1/T 1/S 1, Table 1

Exh. D2/T 1/S 1, Table 1

**Issue 3.6:** Will OPG's accounting policies result in capitalization of an appropriate amount of costs incurred in 2008 and 2009 with respect to the construction or acquisition of capital assets?

It appears that capital expenditures for regulated hydro and nuclear include the capital expenditures for the full 2008 rather than only the last 9 months thereof that the test period covers. In addition, it is not clear whether the capital expenditures for hydro and nuclear in the referenced exhibits include capital spending also included in OM&A

- a) What is the capital expenditure for regulated hydroelectric (as shown in Exh. D1/T 1/S1, Table 1) for the 9 months of 2008 in the test period?
- b) What is the capital expenditure for nuclear (as shown in Exh. D2/T 1/S1, Table 1) for the 9 months of 2008 in the test period?
- c) Does the capital expenditure on regulated hydroelectric (as shown in Exh. D1/T 1/S 1, Table 1) include capital spending on hydro that is included in OM&A? If so, how much spending is included in OM&A over the test period?
- d) Does the capital expenditure on nuclear (as shown in Exh. D2/T 1/S 1, Table 1) include capital spending on nuclear that is included in OM&A? If so, how much spending is included in OM&A over the test period?
- e) Are the capital expenditures (as shown in Exh. D1/T 1/S 1, Table 1) for regulated hydro and (as shown in Exh. D2/T 1/S 1, Table 1) for nuclear net of any disposals of Prescribed Facilities in the test period? If not, then please provide the cash flow expected from such asset disposals.

### **Interrogatory # 24**

**Ref:** Exh. K1/T1/S1, Table 1 and Table 2

**Issue 5.2:** Is the rate base appropriately determined in accordance with regulatory and accounting requirements?

Is the "Depreciation & Amortization" expense item shown in the Summary of Revenue Requirement calculated according to generally accepted accounting principles or according to income tax laws?