Ontario Power Generation Inc. (“OPG”)
Interrogatories for GEC

INTERROGATORY #1

Ref: Page 3, lines 10 - 13

Preamble: Mr. Chernick concludes “that the Board should set separate costs of capital-that is, cost of equity and capital structure-for each of OPG’s operational segments, both to facilitate the tracking of costs and to improve OPG’s decision-making with regard to investments.”

Interrogatory

a) Does Mr. Chernick believe that the regulated wires and generation lines of business of an integrated electric utility have different costs of capital? Please explain in detail.

b) Would Mr. Chernick please confirm that state regulators in the U.S. generally allow a single ROE and capital structure for the composite regulated transmission, distribution and generation operations of integrated utilities? If he cannot confirm, please explain in detail why not.

c) Would Mr. Chernick please explain how he envisages separate cost of capital rates for OPG’s nuclear and hydro operating segments being applied. In this explanation, please specifically comment on the determination of revenue requirement, the allocation of corporate capital budget amounts, the determination of service charges and the allowance for funds used during construction.

INTERROGATORY #2

Ref: Page 9, lines 18 – 25

Preamble: “When the risks of an investor-owned utility are shifted to ratepayers, the utility’s return should generally be reduced. But for OPG, as a provincial entity, a return on equity that reflects the underlying risks has two advantages. First, the higher return will increase OPG’s retained earnings when all goes well, allowing OPG to absorb more of the costs of adverse outcomes when they occur. Second, since OPG will use the return set by the OEB in evaluating investments, it is important that the return on nuclear investments include as much of the nuclear risks as feasible.”

Interrogatory

a) Please explain why the two advantages set out at lines 20 - 25 do not apply equally to investor-owned utilities.

b) If the OEB wanted to establish payment amounts that meet the standard of being "economically efficient", should the risks that have been "transferred to ratepayers" be included in the OEB's determinations of OPG's ROE and capital structure?

c) Is there a difference between establishing a nuclear rate of return that is "appropriate" in that it reflects the nuclear operational and financial risks remaining after consideration of relevant approved risk mitigation proposals, and establishing a rate of return that reflects "as much of the nuclear risks as feasible."?

INTERROGATORY #3

Ref: Page 10, lines 4 – 14

Preamble: "Ms. McShane's estimated cost of capital for OPG's hydro operations is about 8 percent, which is similar to the costs of capital embedded in the bids in the current procurement of peaking capacity under cost-of-service contracts conducted by the Connecticut Department of Public Utility Control (Docket No. 08-01-01). Bidders were allowed to offer costs of equity up to 10.75 percent, indexed to allowed utility ROE (but with a 9.75 percent floor), and up to 60 percent equity. Bidders offered ROEs from 9.75 percent to 10.75 percent, and equity of 40 percent to 50 percent. With a 6 percent debt cost, these bids are equivalent to 7.8 percent to 9.1 percent overall return. The bids that have been recommended by experts for the Department and the Office of Consumer Counsel (including me) offered returns equivalent to 8.2 percent to 8.6 percent."

Interrogatory

a) Please provide a copy of the documentation that supports the referenced costs of equity and equity ratios that bidders were allowed to offer.

b) Please explain in detail how the referenced costs of equity tie to the allowed ROEs of the electricity distributors in Connecticut.

c) If not included in the responses to a) or b), please explain in detail what "indexed to allowed ROE" means in the context of the bids.

d) Please explain whether the costs of capital contained in the bids were a determining factor in Mr. Chernick's recommendations to the DPUC.

e) Please explain how the range of 7.8 percent to 9.1 percent was arrived at given the referenced ROEs and capital structures of the bids.

INTERROGATORY #4

Ref: Page 11, lines 16 - 18

Preamble:

"Q. Are you endorsing Ms. McShane's estimate of nuclear risks."
"A. No. I believe that she may be understating the risk of nuclear investment by assuming that consumers would cover parts of the risks."

Interrogatory

You have indicated at page 9, line 15 that some of OPG's proposals transfer risks to ratepayers. If these same risks are also reflected in the cost of capital OPG is allowed to recover in its approved payment amounts, are ratepayers not essentially going to be paying twice for these risks?

INTERROGATORY #5

Ref: Pages 10 - 12

Preamble: Mr. Chernick comments on the reasonableness of Ms. McShane's cost of capital estimates, but makes no independent estimates of his own, stating that experts have be retained by other parties to do so.

Interrogatory

Would Mr. Chernick please provide his assessment of the reasonableness of the recommendations of each of the experts retained by Pollution Probe, Energy Probe and VECC/CCC?

INTERROGATORY #6

Ref: Pages 13, lines 2 - 8

Preamble:
Q. "Why is it useful to distinguish the costs of capital for nuclear and hydro investments?"
A. "[I]f the OEB establishes separate costs of capital and the mix of OPG's investment changes, due to nuclear retrofits or refurbishment or new nuclear or hydro capacity, OPG's average allowed return would automatically shift in the direction of the investment mix."

Interrogatory

a) Is it Mr. Chernick's assumption that the cost of capital would not change for the separate operating segments as the result of new investment?

b) If new investment was expected to reduce risk, should the operating segment cost of capital be changed to reflect that expected risk reduction? If not, why not?

c) Payments are established based on allowed returns. How would changes in the mix of OPG's generation investments impact customers? What is the practical usefulness of automatic shifts in average allowed returns?

INTERROGATORY #7

Ref: Pages 15, lines 4 - 11

Preamble:

Q. "Can "building risk into cash flows" substitute for risk-adjusted cost of capital?

A. "In principle, revenues from a potential investment could be reduced and operating costs increased to reflect the risks. In practice, it is difficult to capture the many risks of a complex business segment in this fashion. Some risks result from small probabilities of large increases in cost components that are expected to be small, while other risks reflect smooth distributions around the best estimate of cost."

Interrogatory

Is there any reason to believe that adjustment to revenues and operating costs for a specific investment determined through techniques such as Monte Carlo simulations, combined with forecast costs of capital for OPG's regulated operations as a whole, will not yield more accurate investment analyses and decisions than using a technology-specific costs of capital?

INTERROGATORY #8

Interrogatory

Would Mr. Chernick please identify all articles, publications and reports he has written on the cost of utility capital? Please provide copies of all documents.

INTERROGATORY #9

Interrogatory

Would Mr. Chernick please provide a table showing:

a) The recommended returns on equity and capital structure in each case in which he has appeared since 2000
b) The date of the testimony
c) The client on whose behalf the testimony was prepared
d) The regulatory jurisdiction
e) The date of the decision
f) The awarded returns on equity and capital structures; if the case resulted in a settlement, please so indicate.

Please indicate in which of these proceeding Mr. Chernick was accepted as an expert in utility cost of capital. Please provide copies of all testimonies and accompanying schedules for each of the proceedings listed in the table.