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October 3, 2016 **VIA E-MAIL**

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge St.
Toronto, ON
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Dear Ms. Walli:

Re: Ontario Power Generation Inc. 2017-2012 Payment Amounts
EB-2016-0152, Re: Expert Evidence VECC response

We are in receipt of the letter decision of the Board of September 28, 2016, (the "letter decision") regarding the cost award funding of intervenor evidence in the above-noted proceeding, and in particular, denial of the request for funding of the evidence of Dr. Laurence Booth to be put forward by the ratepayer groups, VECC, CCC, and CME ('the intervenors"). We note that the Board has allowed for further submissions, and we are accordingly responding to that opportunity.

VECC would first indicate that we do not object to the new procedure of requesting proposals associated with expert evidence to be submitted by Board Staff and interested parties. We do have considerable concern and uncertainty about the process and criteria for approving an expert proposal by the Board, and its application in this particular instance. We will address our concerns by starting with the premise the evidentiary record for the letter decision of September 28, 2016 consists of the evidence and submission filed to date by all parties as of September 28, 2016. We will return to this premise in our specific issues below.

Reasonableness of the Process

The singular impression that is left by the language of the letter decision is that once the Board staff wishes to retain an expert witness, funding for that expert chosen pre-empts the ability of an intervenor to retain an expert. The letter decision notes on page 2:

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"The role of OEB staff in this proceeding is to represent the public interest. In seeking to fulfill this mandate, the OEB staff plans to file evidence, Based on the information provided, the OEB believes that it would be not appropriate to require ratepayers to bear the costs of any additional expert reports on the subjects for which OEB staff has already retained experts to file evidence."

This conclusion is informed by the fact that the "information provided" referenced in the letter decision consisted of the name of the consulting firm chosen, a two sentence paragraph describing the proposed work and its cost which happened to be more than double that of the proposed intervenor evidence. This information was provided in the Board Staff letter of September 14, 2016 proposing the filing of the Brattle Group evidence.

The letter decision also appears to suggest a chronological order of retention of experts which does not match the reality. Dr. Booth's proposed retention was communicated to Board Staff in response to inquiries early in the process, and during the stakeholder consultation process in May of this year. We were first verbally informed by Board staff of their intention to introduce evidence in August of this year, While we do not wish to suggest that the approval of the submission of evidence is predicated on when it is sought to be retained, we do want to avoid the impression that in this instance that the sponsoring intervenors were somehow "latecomers" to the importance of this issue.

However, if there now is to be a hierarchy or controlling queue that governs the ability to submit evidence funded through the cost award system, this raises some potential conflicts with the accepted goals of that system. With its establishment the OEB sought to adopt a participation based model for funding – not simply one based on the need for funding. As VECC noted in its 2013 submissions in the EB-2013-0301 proceedings:

"The OEB generally made public participation its principal objective. In the 1985 Decision, EBO 116, the OEB established the cost award regime, giving the following rationale:

"The Board believes it should have available to it a broad range of opinions and information for its decision making. Hearings before the Board are becoming increasingly complex. In such circumstances, the Board considers that in fulfilling its duty towards the public interest, which is implicit in the OEB Act, there is increasing need to ensure that a broad range of interests is represented at the Board's hearings and that the essential points are canvassed in sufficient depth to have developed a record that will provide maximum assistance to the Board."

This meant that the priorities of the intervention framework would be on diversity of views and completion of a record of evidence. This was a significant policy decision that shaped the approach of the Board to its responsibilities towards the public interest. In brief, the OEB decision meant that its overarching responsibility would be to allow the full range of interests to

be represented. With these interests heard, the Board would exercise its responsibilities under the relevant legislation."

The ability to introduce evidence funded by the cost award system that informs the Board as the views of "the broad range of interests" is an essential component of this system. While such evidence must be responsible and of assistance to the Board, in VECC's submission, it should not be pre-empted by the simple fact that the Board's own staff decides to submit evidence. In fact, on multiple occasions both Board Staff and interveners have filed expert testimony on the same issues precisely to generate the diversity of views sought by the OEB. The implicit approach in the letter decision limits full participation of intervenors and confines their ability to assert the interest of their constituents without the support of expert evidence. Without in any way disparaging the mandate of Board Staff, intervenors have no say in the choice of experts, the instructions to the experts, or access to their assistance. This may not always be relevant, particularly when Board staff is carrying out their historic function of completing the evidentiary record, but certainly presents difficulties of representation in particular circumstances.

What is worrisome is the concept of the automatic trumping and subsequent exclusion of potential intervenor evidence in the manner described in the letter decision. This approach cannot assist in fostering the necessary public perception of open access by their representatives to the necessary resources to challenge and test utility evidence in OEB proceedings. This is particularly the case where the decision-maker, the witness sponsor, and the applicant are all subject to the aegis of the government. In that instance, VECC would assert that there is an affirmative a need for the OEB to "*have available to it a broad range of opinions and information for its decision making"* as contemplated by EBO 116.

In VECC's view, the Board's seemingly pre-emptive exclusionary approach is a considerable migration from the prudent superintendence of intervenor costs and regulatory efficiency by the potential withdrawal of the important tools that ratepayers and other stakeholders have to have to fully participate effectively. This may not have been the intention of the Board in its letter decision, but the implications of that decision are far-reaching.

The Brattle Group

VECC does not wish to suggest that the selection of the Brattle Group to present cost of capital evidence would result in the presentation of the same by unqualified expert or experts. However, the Brattle Group's evidence in Canadian regulatory jurisdictions, has primarily involved stout arguments for thicker equity levels and higher rates of return for regulated utilities. We admit that our understanding of that Canadian history of the presentation of cost of capital by this American–based consulting firm is based on our research that may not capture all instances of the same, but it does raise questions whether any redundancy with the proposed intervenor evidence can be assumed to arise.

The Brattle Group presented cost of capital evidence in the Ontario Energy Board in the Union Gas 2007 Rates Application EB-2005-0520. The evidence set out the Brattle Group's opinion that given the Board's ROE formula in effect at the time of that hearing,

> *"the corresponding economically consistent deemed equity ratio at the formula rate was in the upper half of a range from 46 to 56 percent"*[1].

This remarkable conclusion represented a very significant increase over Union's then allowed 35% common equity ratio and was buttressed by the use of a technique that estimates the utility's weighted average cost of capital (ATWACC) and compares it across other firms and industries. The ATWACC theory proposes that, as explained by the Brattle witness,

> *"the economically appropriate regulatory equity ratio for a regulated firm is the quantity that, when applied to the formula rate of return on equity, produces the same, market-determined ATWACC"*[2].

The Union 2007 Rates case resulted in the Board approval of a settlement that provided for an equity ratio of 36% (an increase of 1%) which was itself part of a package settlement. The settlement agreement also included a commitment by Union not to use the ATWACC methodology again to support any changes to the Formula ROE, or the capital structure unless to respond to a Board or utility proposal to do so.[3]

The Brattle Group's recommended ATWACC technique, involving estimating an ATWACC and then adjusting either the allowed ROE or common equity ratio to target that rate for a regulated utility, is extremely controversial and has been rejected in Canada for normal utilities. The clearest rejection of this technique on theoretical grounds occurred in the Brattle group's evidence on behalf of Trans Alta where the Alberta Energy and Utilities Board Decision U99099 stated:

> *"The Board would be **derelict** (bold added) in its statutory responsibilities to recognize market capitalization ratios that are derived from a market value capitalization that deviates from the intrinsic long-run value of the regulated firm. For example, if the Board has traditionally set an allowed equity return based on book equity and this has resulted in an equity market capitalization which is considerably above a ratio of one, an ATWACC based on market capitalization ratios would call for a higher composite return… Accordingly, the Board finds it necessary to reject TransAlta's version of the ATWACC model."*[4]

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[1] Written evidence of A. Lawrence Kolbe, the Brattle Group, for Union Gas Limited EB-2005-0520, January 2006 , p.7
[2] Ibid at p.19
[3] Union Gas Limited Settlement Agreement, May15 , 2006, EB- 2005-0520 para 4.3, p.22
[4] AEUB Decision U99099, p.303

Our survey of Brattle's Canadian involvement includes testimony presented on behalf of the regulated utility in the following proceedings:

Utility	Regulator	Proceeding	Date of Decision
TransCanada (Mainline)	National Energy Board	RH-4-2001 Fair Return Application	August 2001
NGTL (Nova)	AUC	Decision 2004-052 Generic Cost of Capital	July 2004
TransCanada(Mainline)	National Energy Board	RH-2-2004	April 2005
Trans Québec & Maritimes Pipeline Inc.	National Energy Board	RH-1-2008	March 2009
Gaz Metro Inc.	Regie de l'energie	R-3690-2009	December 2009
TransCanada Toll	National Energy Board	RH-3-2011	March 2013

In each of the above-noted proceedings, Brattle Group witnesses gave evidence on behalf of the regulated utility that recommended a disposition that would result in a substantially more robust return than the regulator was prepared to give.
It is to be noted that the duty of an expert witness in OEB proceedings is to provide objective opinion evidence for assistance to the Board in an independent and impartial manner. This duty prevails over any obligation associated with the witness engagement. This duty is recognized by the filing of Form A that accompanies any evidence. We assume that the Brattle Group would adhere to that duty. However, the application of these principles at the practical level is more complex and nuanced.

As the Board is aware, the issue of cost of capital is one of major importance in terms of the viability of a regulated utility, the ability to raise capital and the determination of rates. Expert witnesses, whose techniques of assessment and opinions based upon the exercise of their judgment are sought out by applicant utilities when they are confirmative of the expectations of the shareholder. Not surprisingly, that is why utility-sponsored cost of capital witnesses in regulatory proceedings across North America uniformly give opinion evidence that is supportive of policies that produce greater returns for that utility, The small group of witnesses that are engaged in providing evidence are usually careful not to be inconsistent in their approach from proceeding to proceeding, as such inconsistencies will be likely be raised at subsequent regulatory proceedings with practical consequences for the acceptance of the expert opinion as well as future retainers. In the result, utility cost of capital witnesses tend not to be engaged by stakeholder interests seeking lower returns than that sought by the regulated utility.

The maintenance of consistency of approach is, of course, a great concern for commercial consulting firms providing expert assistance with cost of capital issues. As is reflected in the Brattle Group's significant cost estimates in this case, and the Concentric Energy Advisers invoice to Enbridge for capital structure testimony in 2012 (an eye-popping $394,600)[5], the stakes are somewhat higher given the risk for future retainers.

VECC does not seek to speculate on the assistance to the proceeding that will be rendered by the Brattle Group, nor criticize its selection as the choice to provide evidence on behalf of Board Staff. VECC does submit, however, the Board's letter decision to pre-empt the submission of intervenor ratepayer evidence on this issue, in light of the Board Staff choice is perplexing. The intervenors suggested the funding evidentiary assistance of an experienced independent academic, with a substantial record of expert testimony in regulatory tribunals across Canada, and a record of research achievement and publications in refereed journals across North American.[6] The information on the record concerning the Brattle Group, apart from the record in Canada of its appearances in the OEB and in other tribunals previously described, is confined to the paragraph in the Staff submission of September 14, 2016 describing its intended work and its price tag.

Importance of the Issue

The applicant, Ontario Power Generation (OPG), has proposed an increase in its equity thickness from 45% to 49% with supporting evidence offered by Concentric Energy Advisers. The application proposes approval of a regulated rate base that increases to $15.6B by 2021.[7] Even a back of the envelope computation illustrates the substantial impact of every one per cent change in the common equity ratio of OPG.

However, the size of the impact of the change sought is not the only reason for ensuring that a full evidentiary record exists. Largely because of the nature of cost of capital evidence and the exercise of judgment and analysis of competing techniques, it is not uncommon for the regulator to countenance more than one expert opinion on that constellation of issues. In the inaugural proceeding in the OEB setting payment amounts for OPG, EB-2007-0905, the OEB was assisted by a number of experts touching upon cost of capital, and in particular, business risk and capital structure. In addition to the OPG witness, these included :

Laurence Booth of the University of Toronto appearing for VECC and CCC
Paul Chernick of Resource Insight Inc. appearing for GEC
A.J. Goulding of London Economics International appearing for Board staff
Lawrence Kryzanowski of Concordia University and Gordon Roberts of York

[5] EB-2011-0354 proceeding
[6] Dr. Booth's resume was filed with the request for funding.
[7] EB-2016-0152, Ex. C, Tab 1, Schedule1, p.1

University appearing for Pollution Probe
Lawrence Murphy of Henley International Inc. and Tom Adams appearing for AMPCO
Lawrence Schwartz of York University appearing for Energy Probe

With the exception of a 10% reduction in Dr. Schwartz' cost award, there does not seem to be any Board expression of unnecessary duplication in the expert work and their views appeared to form part of the evidentiary record upon which the terms of the capital structure, among other things, was decided.

There have been, of course, multiple cost of capital experts involved in generic proceedings or consultations to determine particular issues therein. In the EB 2007-0905 technical consultation, the Report of the Board for Cost of Capital for Ontario's Regulated Utilities, five expert witnesses gave their opinions, *four* of which were utility sponsored experts, funded by rates. In that instance the Board simply averaged the recommendations (which resulted in Ontario utilities having the highest generic allowed ROEs in Canada). Multiple experts were also involved in the consultations leading to the Report of the Board on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors in EB 2006-0088 and EB 2006-0089. The proceeding records of jurisdictions such as Alberta and British Columbia are replete with the use of multiple experts giving opinion evidence as to appropriate ROE and level of risk. The idea that having three experts giving evidence on the capital structure at issue in this proceeding was not unreasonable given the impact of the issue and the history of similar practice in the OEB and in other jurisdictions

Other Issues and Conclusion

Despite his previous role in providing assistance with the determination of the capital structure of OPG, Dr. Booth is unwilling to interpolate himself in what appears to be a new Board methodology for the introduction of ratepayer/public interest evidence through the cost award system. This is particularly the case where the Board has directed our attention in its letter decision to the necessity to provide "incremental value" for the submission of any evidence. Given the state of the record, and the letter decision itself, it is rather difficult to know what evidence that submission would be incremental to, prior to the filing of the expert testimony by the Board staff witnesses. The letter decision creates uncertainty as to what may be required, and, as such, VECC is not requesting approval for funding to submit independent impartial evidence in this proceeding notwithstanding our view as to the need for it.

However, we note the letter decision allowed for the claiming of expert costs associated with the discovery phase of this proceeding. VECC would like to engage Dr. Booth, should he be willing, for his assistance as a consultant to help with the preparation of information requests (already completed), cross examination, and argument, as we did in the 2014 OPG Payment Amounts case EB-2013-0321. We would assume, in that circumstance, that his participation would not be excluded, but governed by the Board's language in the letter decision on page 2:

"All parties who have contracted for expert assistance are encouraged to carefully manage the contracts ensuring that their consultants stay focused on the issues relevant to this proceeding and are efficient in their execution. Expert assistance must be beneficial to the proceeding and be cost effective."

We would request to be advised if our assumption is incorrect.

Yours truly,

Michael Janigan
Counsel for VECC

Cc: Applicant and Intervenors – via e-mail