

(BILL 100—MINISTRY OF ENERGY DRAFT CONSULTATION REGULATION)

ONTARIO REGULATION

proposed to be made under the

ONTARIO ENERGY BOARD ACT, 1998

PRESCRIBED GENERATORS AND FACILITIES RE: SECTION 78.1 OF THE ACT

Prescribed generator

1. Ontario Power Generation Inc. is prescribed as a generator for the purposes of section 78.1 of the Act.

2. The following generation facilities and units of Ontario Power Generation Inc. are prescribed for the purposes of section 78.1 of the Act:

1. The following hydroelectric generating stations located in the Niagara Region:
 - i. Sir Adam Beck I,
 - ii. Sir Adam Beck II,
 - iii. Sir Adam Beck Pumped Generating Station, and
 - iv. De Cew Falls I and II.
2. The R. H. Saunders hydroelectric generating station on the St. Lawrence River.
3. Pickering A and Pickering B Nuclear Generating Stations.
4. Darlington Nuclear Generating Station.

Price Regulation Of Opg Nuclear And Baseload Hydroelectric Plants

Consultation Paper

Key Issues

1. Assets to be Covered
2. Methodology for Setting Rates
3. Quantity Covered, Treatment of Additional Output
4. Variance Treatment
5. Rate by Technology or by Plant
6. Price Structure
7. Inclusion of Other Revenues
8. Price setting – Including Rate of Return
9. Duration for the Initial Price Setting
10. Operations of Non-Regulated OPG Assets
11. Conditions Around the Ontario Energy Board Taking over Price Setting.

1) **Assets to be Covered**

The output of the following electricity generation assets of Ontario Power Generation are to be price regulated 1) the Niagara Region Hydroelectric Generating Stations including the DeCew Falls Generating Station; 2) the R.H. Saunders hydroelectric generating station on the St. Lawrence River; 3) the Pickering Nuclear Generating Station consisting of Pickering A Nuclear Generating Station and Pickering B Nuclear Generating Station; and, 4) Darlington Nuclear Generating Station.

Proposed Treatment of the Other Key Issues

2) **Methodology for Setting Rates**

- a) Rates are to be set to recover allowed costs and to earn an appropriate return on assets employed based on a forecast output level. The regulated rate would apply to all of the station's baseload output. To the extent that the actual output or costs varied from the forecast levels on which the rate was based, OPG would earn more or less net income than its approved return.
- b) There is not intended to be a true-up from year – to – year if actual return differs from allowed return.
- c) Regulated rates would over time incorporate recovery of allowed capital and other costs incurred to maintain or expand output from the regulated facilities. For example, the costs of the approved Niagara Tunnel, which will increase output at the Sir Adam Beck Generating stations, would need to be recovered from the regulated hydroelectric prices. Similarly, the refurbishment costs related to the return of Pickering A unit 1 and related to the return of other Pickering A units if approved, would need to be recovered as part of the regulated price attributable to the output of the Pickering Generating Station.

3) Quantity Covered, Treatment of Additional Output

- a) The output of the hydroelectric assets above the established levels used to set the regulated rates would receive the wholesale market price.
- b) For example, rates could be set on the basis of 90% of the expected annual output of the baseload hydroelectric plants. OPG would receive the wholesale market price for the remainder of its output. Whether this is best done on a monthly, seasonal or annual basis would need to be determined.
- c) Similarly, nuclear plants would be incented with respect to scheduling outages and maintenance schedules to maximize availability at the highest demand times. Whether this is best done on a monthly, seasonal or annual basis would need to be determined.
- d) With respect to the nuclear plants, the Canadian Nuclear Safety Commission would have to be assured that any incentive system would not affect the primary commitment to safety.
- e) The expected output covered by the regulated price would increase in the event of investments taken to expand output from the stations (e.g. the Niagara Tunnel) or to refurbish or return capacity at the station (e.g. return to service of Pickering A unit 1).

4) Variance Treatment

- a) Once the Ontario Energy Board takes on responsibility for approving any changes to these rates, they may provide for the establishment of several variance and/ or deferral accounts for a range of reasons (water levels, nuclear performance issues, legal and regulatory changes etc.) over which OPG would have limited control.
- b) It is not intended to explicitly provide for variance and/ or deferral accounts in the regulation setting the initial rate. However, the regulation would provide that while

the regulation is in effect, OPG could, once a year, request a change to the rate under circumstances where there are large, material changes affecting the finances of OPG.

5) Rate by Technology or by Plant

- a) It is expected that the regulation will set separate prices for the output from: 1) the regulated baseload hydro (Niagara plants and Saunders); 2) Darlington GS; and, 3) Pickering GS (i.e. A and B combined).
- b) Alternatively, given the many common costs, the nuclear rate could be a combined one for the output of Darlington and Pickering. Payments to OPG settled through the Ontario Power Authority will be based on these regulated prices.

6) Price Structure

The regulated rate should be a price per kWh set for the output of the price regulated stations.

7) Inclusion of Other Revenues

Non-energy revenues (e.g. ancillary services revenues, Congestion Management payments) related to the baseload hydroelectric plant could be included in the calculation of the regulated rate. Alternatively, this could be viewed as a competitive market activity and the revenue left to the non-regulated assets to ensure full market incentives.

8) Price Setting – Including Rate of Return:

- a) Price will be determined by allowed costs, rate base, capital structure, allowed rate of return and expected output. Appropriate capital structure will need to be established consistent with the regulated status of the assets and their operational and financial

risk. For example, generating assets generally have higher operational risk than the assets of a typical regulated utility.

- b) The decision as to allowed rate of return will have a significant effect on the rate. A typical utility regulated by the Ontario Energy Board is allowed a after tax rate of return in the range of 10%.
- c) The Government could decide to set the price on the basis of this level, accept a lower return for its assets or alternatively could decide to phase in the return in stages over the years that the regulation applies.
- d) At the time OPG was established, the hydroelectric assets were assigned a higher asset value than the nuclear plants. Consequently, the rates for the baseload hydroelectric plants are more sensitive to the choice of capital structure and rate of return than the nuclear plants.

9) Duration for the Initial Price Setting

The expected duration of the regulation is 2 – 3 years, that is the price established would be in place for 2005 and 2006 and possibly 2007.

10) Operation of Non-Regulated OPG assets

The bidding behavior and the shareholder's expectations regarding performance for OPG's non-regulated assets will be set out in a public Shareholder's Declaration for OPG. It would not form part of the regulation dealing with the regulated assets.

11) Conditions Around the Ontario Energy Board Taking over Price Setting

In establishing future regulated prices for the designated facilities, the Ontario Energy Board would need to take into account the asset values assigned to the facilities for the

purposes of this regulation and any approved investment to increase output from the designated station or to refurbish or add operating capacity to the designated station.

Similarly, for a facility that has been designated as a regulated entity additional output from that facility related to investments to increase output or to increase operating capacity at the station would be subject to the appropriate regulated price.

The regulation could specify the rate of return and capital structure for OPG assets, limit review period and timeframe or set other conditions. Except where otherwise specified by regulation, the Ontario Energy Board would have discretion in establishing the ongoing methodology for setting the regulated price for the designated facilities and the treatment of costs.