ONTARIOPOWER GENERATION

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Deputy Minister Sergio Imbrogno
4th Floor, Hearst Block
900 Bay Street
Toronto, Ontario
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Dear Deputy Minister Imbrogno:

I am responding to your request for OPG's analysis of a Hydro Quebec proposal to supply energy and capacity to Ontario. While OPG has not been part of the discussions with Hydro Quebec, you have asked us to estimate the impacts of entering into a contract for 1,000 MW of firm capacity and 10 TWh of energy for 20 years that could justify the replacement of the refurbishment of two Darlington nuclear units.

In summary, there is no justification or benefit for Ontario to enter into the proposed contract described above. Ontario has already largely de-carbonized its electricity sector, making it one of the cleanest in the developed world. Further, Ontario is in a position of having a surplus of both energy and capacity until after Pickering Nuclear Generating Station is scheduled to cease operations in 2024. Ontario has been able to achieve this by making significant investments in long life generating assets. And more recently, Ontario has recognized the inter-generational value of these assets by implementing the Fair Hydro Plan to more equitably allocate costs to electricity customers over time.

The above factors make entering into the long-term purchase of energy and capacity from Hydro Quebec described above detrimental to Ontario unless very carefully crafted with the customer firmly in mind. Specifically, our analysis of the contract described above concludes:

- **Electricity Customers will Pay More** – Customer costs will increase by an average of $980M/year, primarily because it is not possible to: effectively match energy imports from Quebec with need in Ontario; avoid material costs incurred and committed for Darlington Refurbishment; and avoid significant loss of scale efficiencies resulting from operating only 2 Darlington units.

- **Ontario's Fiscal Position will Deteriorate** – There will be a significant near term impact to the Province's current fiscal year ranging from $1B-$4B stemming from extended delays in OPG's current rate case and capital write-offs as well as a recurring negative fiscal hit to Province of $900M/year resulting from OPG's foregone net income and PILS. Customer cost increases noted in the previous bullet will be partially offset by these write-offs and losses since OPG regulated rate base will be lower.

- **Regional GHG emissions will Increase** – Over the 20 year term regional GHG emissions will increase by more than 5Tg. This is equivalent to emissions from OPG's retired Lambton Coal Generating Station during its last three years of operations. It is also likely that Hydro Quebec will rely upon its laid up Beconcoeur gas plant to provide needed winter capacity.

- **Fair Hydro Plan at Risk** – OPG's ability to borrow to support the Fair Hydro Plan will be impaired as a result of OPG's weakening credit profile.

- **Economy and Workers Suffer** – If the refurbishment of 2 Darlington units is cancelled Ontario will forego a GDP boost of $25-30B over the next 40 years and will lose an annual average of over 4,000 high quality operations and construction jobs.

- **Ontarians are Supportive of Nuclear** – A recent survey by Gandalf Group found that 74% of Ontarians were supportive of nuclear power generation. Even more, 79% of those surveyed, supported refurbishing Darlington, founded largely on the benefits to the economy and clean power generation.

- **Larger purchases are worse for Ontario** – The above noted issues are not mitigated by larger purchases or commitments to Hydro Quebec, rather they result in progressively worse outcomes for Ontario.

OPG's objective has always been to offer help and candid advice to our Shareholder. We believe that there are opportunities for an alternative deal with Hydro Quebec that will benefit Ontario. To do so, the deal must be grounded in what Ontario needs, not what Hydro Quebec wants to sell. In short, it must:

- Leverage the significant investments Ontario has made in de-carbonizing its electricity sector;
- Support market renewal activities undertaken by the IESO whose goal is to reduce costs for electricity customers by increasing the level of competition among generators to supply energy, capacity and ancillary services;
- Allow for shaping energy deliveries to Ontario so that energy arrives when it is needed and does not force spill of GHG-free, near zero marginal cost hydroelectric generation;
- Provide firm year-round capacity to Ontario that avoids or delays future capacity additions.
- Include modest transmission investments to firm up the flow of electricity; and
- Not overly constrain Ontario's ability to export energy to Quebec when it is beneficial to do so.

To further ensure that Ontario receives maximum benefit from a contract with Hydro Quebec, *it is in our* view that OPG should be the counterparty that negotiates and holds the contract. This will allow OPG, rather than Hydro Quebec, to capture the benefits of wheeling energy and capacity through Ontario to other markets. These benefits will flow directly to Ontario electricity customers or taxpayers. Having OPG as the counterparty also allows the IESO to maintain its independence and continue to further its market renewal efforts, rather than acting as a direct counterparty in an arrangement that will be viewed as undermining and contradictory to its market renewal strategy.

Attached is a presentation outlining our analysis of the Hydro Quebec offer as requested, including our thoughts on an alternative deal that might better serve the citizens of Ontario. I'd be happy to discuss this matter in more detail at your earliest convenience.

Regards,

Jeff Lyash
President and Chief Executive Officer

enc.: Assessment of Impact on Ontario of Proposed Hydro Quebec Deal

cc: Andrew Teliszewsky, Chief Of Staff, Ministry of Energy