



REVISED TAB X
TREASURY BOARD / MANAGEMENT BOARD OF CABINET
REQUEST ASSESSMENT NOTE

Ministry:	Energy
Meeting Date:	January 23, 2018
Agenda Class:	Discussion
Last reviewed by: Cabinet (December 2015)	Tracking to: Fast Track Cabinet (January 24, 2018)

SUBMISSION TITLE: Darlington Refurbishment Project – Report on Status

I. DECISION BEFORE THE BOARD

Receive an update on the Darlington Refurbishment Project

II. RECOMMENDATIONS (UNDER DEVELOPMENT)

Receive an update on the Darlington Refurbishment Project.	<i>Receive</i>
Approve the Ministry of Energy ensuring that Ontario Power Generation (OPG) proceed with refurbishment of Darlington Unit 3 beginning in Fall 2019 consistent with OPG's Release Quality Estimate and the 2013 Long-term Energy Plan principles for nuclear refurbishment.	<i>Under development (see last three bullets on page</i>
Direct the Ministry to include in future report backs to TB/MBC on the Darlington Refurbishment Project: - Projected changes in OPG's contribution to the Province, as well as ratepayer impact from original projections for the Project, and from what's included in the 2017 Long Term Energy Plan. - Provide its recommendation and rationale on whether an off-ramp is required in future report backs to TB/MBC regarding a decision to proceed with refurbishing the next Unit at Darlington.	<i>Direct</i>

III. FINANCIAL SUMMARY

\$ Millions	2017-18	2018-19	2019-20
Initiative cost requested	0.0	0.0	0.0
Initiative cost recommended	0.0	0.0	0.0
Offset recommended	0.0	0.0	0.0
Total Fiscal Impact	0.0	0.0	0.0

IV. KEY COMMENTS AND CONSIDERATIONS

The Ministry is providing an update on the four-unit Darlington refurbishment project now under way.

In December 2015, Cabinet approved OPG's total budget of \$12.8 billion and schedule of 112 months to refurbish the four nuclear units at Darlington. Appendix C provides the 2015 Cabinet minute.

In October 2016, OPG began the execution of refurbishment of Unit 2 at Darlington (Followed by Units 3,1,and 4).

This following table provides an overview of the Ministry's update:

Report Requirement	Update – Highlights (See Appendix D for more details)
Progress of Darlington Unit 2 refurbishment	• Unit 2 refurbishment is on track to be complete within approved project budget and schedule • Unit 2 field work 50% complete and 18 days ahead of schedule • Unit 2 spend to-date is \$1.78 billion – currently \$11 million over plan, but forecast to be on budget at completion. It is 18 days ahead of schedule • The Heavy Water Storage Facility experienced cost and schedule challenges – but is expected to be in service before its needed in 2020-21 • Project not on critical path for U2 refurb • Overall cost will be 20-30% higher than \$381M estimate • OEB will review costs and if any are disallowed will need to be written off by OPG/have a fiscal impact on the province
Planning and preparation for Unit 3 refurbishment	• To ensure that lessons learned from the Unit 2 refurbishment are incorporated into subsequent refurbishments, OPG will not commence execution of refurbishment work on Unit 3 until Unit 2 refurbishment is complete. • Unit 3 refurbishment planning is under way, in line with OPG's phased approach to refurbishment • OPG is planning to be ready to execute Unit 3 refurbishment as early as October 2019, one month after the earliest potential completion of Unit 2 • November 9, 2017, OPG Board confirmed that the project schedule and budget for Unit 3 refurbishment remains within the 2015 approved Darlington refurbishment project schedule and budget
Update on oversight of Darlington refurbishment project	• FAO – Nov 2017 Report - Re-affirms the long-term benefits of Ontario's nuclear refurbishment plan and notes the robust oversight and protections have been put in place to mitigate against risks during refurbishment • OEB – Dec 2017 – the OEB issued its decision and determined that OPG's approved budget for Unit 2 refurbishment and supporting infrastructure is prudent, including OPG's proposed contingency amounts • Government's oversight advisor prepared a due diligence report with a summary assessment of the Darlington refurbishment project performance to-date as well as planning and preparation for Unit 3 refurbishment • To date, the Unit 2 refurbishment remains on track to meet the committed high confidence schedule and budget • OPG has developed and implemented robust project management processes to manage a project of this size and complexity – citing specifically the lessons learned component informing the next refurb • OPG's contracting strategy has been implemented to assign risk to the main contractors, incentivise the appropriate behaviours and allow for the necessary transparency and visibility by OPG project management

	• There is adequate contingency in the project to accommodate the risks as currently assessed. OPG uses a risk management tool to continuously identify new risks and put in place mitigation plans • The project schedule and budget for Unit 3 refurbishment is expected to remain within the estimate approved for the overall Darlington refurbishment project
Next steps as OPG prepares to execute Unit 3 refurbishment (Includes analysis and considerations with respect to the government's "off-ramps" for Darlington refurbishment)	• The government has established off-ramps for the Darlington refurbishment project that may be used in the event that OPG fails to adhere to the approved budget and schedule for the project • Currently, Unit 2 refurbishment on track to be complete within budget and schedule • Rationale for taking an "off-ramp" before the start of Unit 3 would be based on the on the following considerations: • Poor refurbishment performance on Unit 2 (i.e., loss of confidence in OPG's ability to execute refurbishments); • Refurbished nuclear being uneconomic when compared to alternatives (i.e., no longer provides value for ratepayers); and • Better supply options to address future generation capacity needs emerging (i.e., triggering a Darlington off-ramp would require new capacity). • If an off-ramp is exercised before start of Unit 3, OPG is likely to shut down all of the remaining 3 Darlington units at the end of their safe operating lives and operates the refurbished Unit 2 for an additional 30 years. • Unit 3 in June 2020 • Unit 1 in October 2022 • Unit 4 in March 2024 • Unit 2 in February 2050 – OPG may incur up to \$6 billion in write-offs as a result of cost disallowances by the OEB following the off-ramp. OPG projects that disallowances and foregone capital investment would result in a reduction of OPG's contribution to government's income of \$1.1 to \$1.4 billion per year on average (\$43 to \$55 billion over Darlington's lifetime). • OPG and the advisor conclude that an "off –ramp" is not required based on the performance of Unit 2 and the application of lessons learned to Unit 3.

Financial Implications:

Darlington is owned and operated by OPG, a regulated utility wholly owned by the Province of Ontario. OPG will initially finance Darlington refurbishment with long-term corporate debt and cash generated from operations (equity). OPG will recover the cost of refurbishing Darlington by selling electricity to ratepayers at prices set by the OEB, once each reactor is back online following refurbishment (and over the life of the reactors).

OPG is rate-regulated by the Ontario Energy Board (OEB) which sets the price that OPG receives for all of its nuclear output (i.e., Darlington and Pickering stations) every 5 years. OPG's net income (as adjusted for IFRS)), payments in lieu of taxes (PILs) and net assets are consolidated into the Province's financial statements, and any OPG income or loss from its nuclear business will be reflected in the Province's fiscal

position.

- The refurbished reactors will be added to OPG's 'rate-base' once they are in-service again
- Once Unit 2 refurbishment is complete, the OEB will compare actual costs against OPG's approved budget (i.e., any savings will be returned to ratepayers; any excess will be reviewed and only allowed for recovery if prudently incurred).
- OEB will set a nuclear price that will incorporate the depreciation of the refurbished reactors over their useful lives to recover the approved capital expenditures plus a return on OPG's refurbishment investment to cover the cost of capital (i.e., debt and equity).

OEB Decision (EB-2016-0152) (December 28, 2017) – Approved OPG's application relating to the Darlington Refurbishment Program (DRP), including the addition of \$4,800 million to rate base in 2020 when the first of the four units to be refurbished is expected to come back online (Appendix F).

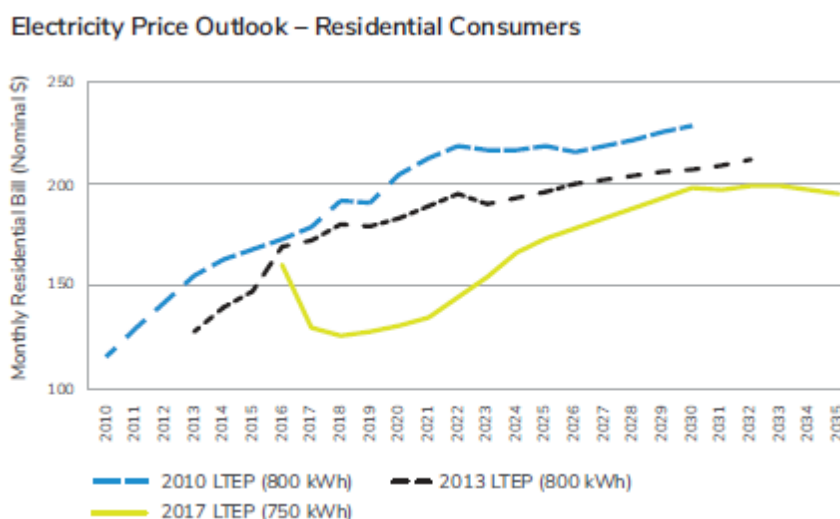
OPG expects to provide \$1.4 billion per year, on average, in revenue to the Province from the Darlington refurbishment and long-term operation through consolidation of OPG's net income and PILs.

- The projected revenues for the Province is based on achieving the refurbishment and operation of Darlington as per approved plan (i.e., refurbishment project completed on budget and schedule and the station operating as planned post-refurbishment).

The Ministry indicates the estimated average price of power from Darlington post-refurbishment continues to be about 8 cents per kWh (in 2015\$) and includes capacity availability greater than 90%. (For comparison, wind prices under the Feed-In Tariff (FIT) program were about 13.5 cents per kWh with only intermittent generation at about 10% capacity availability).

Ratepayer impact

The 2017 Long Term Energy Plan (2017 LTEP) includes the following graphic showing projected monthly residential bills. It shows the impact of the Ontario Fair Hydro Plan and includes projected impacts of nuclear refurbishment. There are follow-on decisions pending from the OEB, based on OPG submissions, that will transition the December 2017 decision adding \$4.8B to the rate base, to rate smoothed customer bill impacts. The Ministry indicates this will likely be in-line with the 2017 LTEP (See Appendix F). **(Energy to confirm, or flag the impacts).**



TBS staff note that while the Ministry's submission indicates OPG, the advisor conclude that an "off-ramp" is not required based on the performance of Unit 2, and that the Ministry's submission presents "analysis and considerations," the submission does not explicitly layout the Ministry's concurrence or not and supporting rationale with the recommendation from OPG/Advisor that off-ramping at this point is not required.

- In subsequent briefings, the Ministry has indicated it can do higher-level analysis (rather than redoing the 2017LTEP and involving IESO) on the costs of alternative supply options following an off-ramp. The analysis might take a couple of weeks.
- This analysis should be part of the Ministry's rationale for its recommendation to off-ramp or not. The rationale should also include an assessment of any changes in conditions since the Dec 2015 Cabinet decision, such as government priorities (if green house gas reduction is less of a priority, gas as a supply option may be more viable depending on shifts in commodity prices), changes in demand for electricity etc. The rationale could also point out that shifts in conditions would likely have to be of a magnitude before off-ramping becomes practicable given the financial implications involved with the planned nuclear refurbishment now under way, and the need to build new generating capacity for the supply alternative(s) etc.
- The Ministry recommendation and rationale should inform the TB/MBC discussion and recommended minute. If there is a decision not to move from January 23, 2018 TB/MBC to the February 6, 2018 TB/MBC meeting, Cabinet ratification of the TB/MBC minute could be placed on hold pending the Ministry providing that information to Cabinet Office.
- The Ministry should be directed to provide its recommendation and rationale on whether an off-ramp is required in future report backs to TB/MBC regarding a decision to proceed with refurbishing the next Unit.

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Branch / Division:	Education, Resources and Economic Development / OEMD		

APPENDIX A: PROPOSED MINUTE (UNDER DEVELOPMENT)

Receive the report on status of the Darlington Refurbishment Project.

In this regard,

- i) Approve the Ministry of Energy ensuring that Ontario Power Generation (OPG) proceed with refurbishment of Darlington Unit 3 beginning in Fall 2019 consistent with OPG's Release Quality Estimate and the 2013 Long-term Energy Plan principles for nuclear refurbishment:
 - a) Minimize commercial risk on the part of ratepayers and government;
 - b) Mitigate reliability risks by developing contingency plans that include alternative supply options if contract and other objects are at risk of non-fulfillment;
 - c) Entrench appropriate and realistic off-ramps and scoping;
 - d) Require OPG to hold its contractors accountable to the nuclear refurbishment schedule and price (not applicable to the Bruce refurbishments);
 - e) Make site, project management, regulatory requirements and supply chain considerations, and cost and risk containment, the primary factors in developing the implementation plan; and
 - f) Take smaller initial steps to ensure there is opportunity to incorporate lessons learned from refurbishment, including collaboration by operators.
- ii) Direct the Ministry to:
 - a) Include in future report backs to TB/MBC on the Darlington Refurbishment Project:
 - 1) Projected changes in OPG's contribution to the Province, as well as ratepayer impact from original projections (i.e., Showing historical performance to date, including the latest update) and from what's included in the 2017 Long Term Energy Plan.
 - 2) Its recommendation and rationale on whether an off-ramp is required, or not, in future report backs to TB/MBC regarding a decision to proceed with refurbishing the next Unit at Darlington.
 - b) Work with OPG and Cabinet Office on a communications strategy.

APPENDIX B: FINANCIAL TABLES

FINANCIAL IMPACTS: CHANGES TO EXPENSE AND REVENUE				TABLE B1
\$ Millions	Fiscal Plan Basis			Appropriations Basis
	2017-18	2018-19	2020-21	2017-18
Initiative cost recommended	0.0	0.0	0.0	
<i>Expense changes:</i>				
Operating Expense	0.0	0.0	0.0	0.0
Offset	0.0	0.0	0.0	0.0
<i>Revenue changes:</i>				
N/A	0.0	0.0	0.0	0.0
Total Fiscal Impact	0.0	0.0	0.0	0.0

APPENDIX C: 2015 CABINET MINUTE

Cabinet agreed that:

1. ENERGY ensure that Ontario Power Generation (OPG) proceed with refurbishment of Darlington Unit 2 beginning in Fall 2016 consistent with OPG's Release Quality Estimate and the 2013 Long-term Energy Plan principles for nuclear refurbishment:
 - a) Minimize commercial risk on the part of ratepayers and government;
 - b) Mitigate reliability risks by developing contingency plans that include alternative supply options if contract and other objects are at risk of non-fulfillment;
 - c) Entrench appropriate and realistic off-ramps and scoping;
 - d) Require OPG to hold its contractors accountable to the nuclear refurbishment schedule and price (not applicable to the Bruce refurbishments);
 - e) Make site, project management, regulatory requirements and supply chain considerations, and cost and risk containment, the primary factors in developing the implementation plan; and
 - f) Take smaller initial steps to ensure there is opportunity to incorporate lessons learned from refurbishment, including collaboration by operators.
2. ENERGY report back to Treasury Board/Management Board of Cabinet (TB/MBC) and seek Cabinet approval twenty months prior to OPG proceeding with refurbishment of the next Darlington unit and twenty months in advance of all remaining units.
3. In addition to TB/MBC approving OPG's Business Plan annually, ENERGY report back to Cabinet annually to update on progress and implementation of the refurbishment project.
4. ENERGY provide continued independent oversight of Darlington Refurbishment Project including:
 - a) ENERGY formally engaging Infrastructure Ontario (IO) to leverage their expertise; and
 - b) Having third party expertise sit on the Darlington Refurbishment Committee of the OPG Board of Directors as an observer and work with ENERGY and IO to provide independent oversight.
5. ENERGY ensure that OPG proceed with the contracting strategy outlined in ENERGY's November 30, 2015 submission to mitigate project execution risk.
6. ENERGY ensure that OPG work with Bruce Power under the signed Memorandum of Understanding to increase collaboration between the two nuclear operators.

APPENDIX D: MORE DETAILED UPDATE

Unit 2 Refurbishment – Update:

Unit 2 refurbishment is on track to be complete ahead of schedule and within budget. As of December 11, 2017:

- Unit 2 field work is 50% complete and 18 days ahead of schedule; and
- Unit 2 spend to-date is \$1.78 billion – currently \$11 million over plan, but forecast to be on budget at completion.

Infrastructure projects being implemented at Darlington to improve plant safety and to support refurbishment and continued operations of the full site are nearly complete.

- 17 of 18 projects are in service; and
- The one remaining project, Heavy Water Storage Facility (HWSF), has experienced cost and schedule challenges. The contract is being aggressively managed and the facility is expected to be in service well before its need date in 2020-2021.

There is no adverse impact for the HWSF delay on the overall approved refurbishment schedule and budget as appropriate contingency has already been built in.

- The HWSF is not on the critical path for Unit 2 refurbishment.
- OPG has taken steps to hold the vendor accountable for project performance and minimize costs by enforcing contractual penalties, negotiating a lower cost for remaining work and capping the overall cost of the facility
- OPG expects that the overall cost will be 20-30% over the \$381 million estimate
- OEB will review HWSF costs for prudence once the project is complete. Any disallowed costs will need to be written off by OPG with a corresponding fiscal impact on the Province.

DARLINGTON RECURBISHMENT PROGRAM PERFORMANCE – UNIT 2			
SAFETY 		QUALITY 	
• No Lost Time Injuries since the launch of the project in early 2010. • All Injury Rate is at 0.49 incidents per 200k hours worked, which continues to be substantially better than general construction industry performance in Ontario. • Due to a recent increase in near miss safety events, SNC/Aecon stood down their skilled trades workforce to re-inforce the priority placed on safety.		• No regulatory non-compliance events on Unit 2. • No quality related system failures resulting in loss of generation or impacts to the High Confidence Schedule.	
SCHEDULE 		COST 	
• The project is 18 days ahead of the high confidence shedule and currently forecast to be complete ahead of the 40-month schedule duration.		• Unit 2 is currently \$11 Million over budget. • The forecast to complete Unit 2 remains within the approved budget of \$3.417 Billion. • The forecast to refurbish all 4-units and complete all Facility & Infrastructure and Safety Improvement projects remains within the approved \$12.8 Billion budget.	
 Ahead of Plan  On Plan  Marginally Behind Plan  Behind Plan			

The Ministry continues to closely monitor OPG's performance on Unit 2 refurbishment through regular briefings with OPG management, OPG Board and the government oversight advisor.

Unit 3 Refurbishment – Planning and Preparation – Update

OPG is planning to be ready to execute Unit 3 refurbishment as early as October 2019, one month after the earliest potential completion of Unit 2.

- With concurrence of the Minister of Energy, OPG's Board has now released \$242 million to commence design replication, long-lead material procurement and incorporation of lessons learned from Unit 2 refurbishment into the development of the project schedule and budget for Unit 3.

OPG's planning and preparation activities for refurbishment of Unit 3 include:

- Establishment of an independent planning organization;
- Replication of Unit 2 engineering designs for Unit 3;
- Engineering for scope specific to Unit 3;
- Procurement of long-lead materials;
- On-going incorporation of lessons learned from Unit 2; and
- Development of the detailed budget and schedule estimates for Unit 3.

OPG is currently in the process of assembling detailed project schedules and updated budget estimates to support the next funding request of \$164 million for Unit 3 from OPG's Board in March 2018, for a cumulative total of ~\$436 million authorized spend.

- The near-term focus is on pre-requisite projects starting in Q3 2018 as well as long-lead procurement leading up to potential Unit 3 "breaker open" in October 2019.

OPG spent approximately \$2 billion in project planning and preparation prior to receiving final Cabinet approval in 2015 to proceed with execution of the refurbishment project.

November 9, 2017, OPG Board confirmed that the project schedule and budget for Unit 3 refurbishment remains within the 2015 approved Darlington refurbishment project schedule and budget.

- The estimated average price of power from Darlington post-refurbishment continues to be about 8 cents per kWh (in 2015\$) and includes capacity availability greater than 90%. Note: For comparison, wind prices under the Feed-In Tariff (FIT) program were about 13.5 cents per kWh with only about 10% capacity availability.

OPG's scope of work for the Unit 3 refurbishment is similar to Unit 2, with the following differences:

- Exclusion of one-time facility and safety projects and in-station support service projects, which are already in place as part of work to enable Unit 2 refurbishment; and
- Inclusion of digital upgrade work for the Turbine Generator Control Systems (Note: This work will be performed for Unit 2 at a later date).

OPG Board Approved Refurbishment Project Schedule and Budget Estimate		
Unit 3	2015	2017
Schedule	40 months	40 months
Budget	\$2.4 billion	\$2.4 billion

OPG has put in place a formal lessons learned process to benefit Unit 3 refurbishment planning and preparation.

OPG has also created a dedicated Darlington Unit 3 Innovation Project Team to identify, review and implement "high impact" innovative ideas with significant opportunity to reduce cost and duration on future units.

Ministry of Energy is being regularly updated on the status of Unit 3 planning as part of the reporting on the status of Darlington refurbishment project.

Oversight of OPG's Refurbishment Project – Update

The government is committed to strict oversight of OPG during the Darlington refurbishment project in order to ensure that ratepayers are protected and the refurbishments adhere to the approved project schedule and budget.

- As directed by Cabinet in June 2015, Ministry of Energy developed an oversight structure for the execution phase of Darlington refurbishment project with support from Infrastructure Ontario (IO).
- An independent oversight advisor (MZConsulting – Milt Caplan) is actively monitoring the Darlington refurbishment project and regularly reporting to the Minister of Energy.

OPG also has significant project oversight in place to monitor the Darlington refurbishment project and to ensure challenges are identified early and addressed promptly.

- The Darlington Refurbishment Committee (DRC) of the OPG Board is responsible for overseeing the project's execution including monitoring progress and performance against the approved project schedule and budget and making recommendations to the OPG Board with respect to refurbishment of subsequent units at Darlington.
- The DRC has also retained external oversight advisors to support the oversight of the project by the OPG Board (i.e., Burns & McDonnell).
- The Refurbishment Construction Review Board (RCRB) is a panel of industry experts that provides external oversight and advice to OPG's CEO, Chief Nuclear Officer and SVP of Nuclear Projects.

The Darlington refurbishment project is also subject to regulatory oversight by Canadian Nuclear Safety Commission (CNSC) and Ontario Energy Board (OEB).

- OEB ensures that ratepayers are only responsible for refurbishment costs that have been prudently incurred.
- CNSC ensures that OPG is in compliance with all regulatory safety requirements when undertaking the refurbishments.
- Evaluation of OPG's risk management strategy with respect to emerging project risks; and
- Review of processes and ongoing progress on collaboration activities between the Darlington and Bruce refurbishment projects.

The advisor has provided 3 semi-annual reports covering the following reporting periods (i.e., since the start of Execution Phase of Darlington refurbishment)

- Jan 2016 – Jun 2016
- Jul 2016 – Dec 2016
- Jan 2017 – Jun 2017

Government Oversight Advisor – Due Diligence Report

- To support a Cabinet report back on the Darlington refurbishment project, the Ministry of Energy asked the government oversight advisor to prepare a due diligence report with a summary assessment of the Darlington refurbishment project performance to-date as well as planning and preparation for Unit 3 refurbishment.

Key Elements	Summary Finding
Unit 2 Performance	• To date, the Unit 2 refurbishment remains on track to meet the committed high confidence schedule and budget. • The use of reactor mock-up at the Darlington Energy Centre has been particularly beneficial for project performance (e.g., testing tools, procedures and lessons learned). • OPG is taking action to improve upon previous challenges experienced with transitions as one element of refurbishment work concludes and the next one begins.

Key Elements	Summary Finding
OPG Project Management Performance & Lessons Learned	• OPG has developed and implemented robust project management processes to manage a project of this size and complexity. • A key element of the project is the lessons learned program which includes a “lessons learned review” following completion of each refurbishment task. OPG is successfully transitioning into a strong learning organization and contractor capability is improving. • OPG should be diligent in developing a robust Human Resources program to ensure existing staff resources are sustained and new resources are available over the entire refurbishment period (i.e., to 2026).
Implementation of OPG's Contracting Strategy & Project Risk Management	• OPG's contracting strategy has been implemented to assign risk to the main contractors, incentivise the appropriate behaviours and allow for the necessary transparency and visibility by OPG project management. – The Heavy Water Storage Facility is an example where OPG actively intervened to improve contractor performance including demanding organizational changes and enforcing contractual disincentives. • OPG has a robust risk management process. There is adequate contingency in the project to accommodate the risks as currently assessed. OPG uses a risk management tool to continuously identify new risks and put in place mitigation plans.
OPG & Bruce Power Collaboration	• OPG and Bruce Power collaboration is going well as both parties see the benefit of collaboration and are enthusiastic supporters of working together. – There are strong intercompany relationships at all levels, with both companies initiating contacts whenever there is an issue to be discussed or help is required. • Issues being addressed include safety and development of staff to ensure that there are sufficient qualified people at all levels to implement both utilities' refurbishment projects taking into account the overlap of Darlington and Bruce units post-2020.
Unit 3 Planning & Preparation	• A planning organization is in place and project schedule is being prepared taking into account the actual experience of Unit 2 to-date. – Following the completion of each major refurbishment task for Unit 2, a lessons learned meeting is held to review the outcome and requirements for future units. This is then built into the Unit 3 and subsequent units' schedules. – There is also an updated risk assessment underway that looks at where risks have been reduced and acknowledges where risks may also increase due to any unique aspects of Unit 3. • The project schedule and budget for Unit 3 refurbishment is expected to remain within the estimate approved for the overall Darlington refurbishment project. • As an integral part of the planning process for Unit 3, OPG must continue to focus its efforts on the development of people at all levels of the organization taking into account Unit 2 experience and the collaboration efforts with Bruce Power.

The issues identified by the government oversight advisor are consistent with those raised by OPG's external oversight advisors (i.e., RCRB and Burns & McDonnell) and there continues to be broad agreement in each group's reporting.

- OPG is very responsive and open in addressing findings and recommendations from internal and external oversight.

Both OPG and the advisor conclude that an “off-ramp” is not required based on the performance of Unit 2 and the application of lessons learned to Unit 3.

APPENDIX E: DARLINGTON REFURBISHMENT “OFF-RAMPS” – ANALYSIS AND CONSIDERATIONS

Currently, Unit 2 refurbishment on track to be complete within budget and schedule. Nuclear refurbishment remains the most cost-effective option for meeting Ontario’s round-the-clock electricity needs, as confirmed by 2017 LTEP and 2017 FAO report.

- OPG requires government approval before proceeding with each remaining unit refurbishment. These decision points act as “off-ramps” for the project

Rationale for taking an “off-ramp” before the start of Unit 3 would be based on the on the following considerations:

- Poor refurbishment performance on Unit 2 (i.e., loss of confidence in OPG’s ability to execute refurbishments)
- Refurbished nuclear being uneconomic when compared to alternatives (i.e., no longer provides value for ratepayers)
- Better supply options to address future generation capacity needs (i.e., triggering a Darlington off-ramp would require new capacity)

If an off-ramp is exercised before start of Unit 3, OPG is likely to shut down all of the remaining 3 Darlington units at the end of their safe operating lives and operates the refurbished Unit 2 for an additional 30 years.

- Unit 3 in June 2020, Unit 1 in October 2022, Unit 4 in March 2024, Unit 2 in February 2050

If the Darlington off-ramps were triggered for Units 1, 3 and 4, new capacity would be required.

- This new capacity would also be required to produce a large amount of energy to replace the baseload production from Darlington.
- The IESO is undertaking a Market Renewal initiative that is expected to result in lower-cost procurements for any new capacity needs.
- As part of the Market Renewal initiative, the IESO has launched a Non-Emitting Resources Subcommittee (NER-SC) to study how non-emitting resources will participate in the new market designs. The IESO will issue a Request for Information in 2018 to understand the technical, operational and commercial considerations of non-emitting resources.

Two scenarios are being considered to address the future capacity needs:

- Replacement Scenario – Gas-fired Generation
 - 3,400 MW of simple cycle or combined cycle gas plants are built to replace the capacity lost from the Darlington off-ramp and meet total system needs.
- Replacement Scenario – Non-Hydro Renewable Generation
 - Renewable capacity (i.e., wind) is built to replace the capacity lost from the Darlington off-ramp on a MW-per-MW basis; and
 - 3,000 MW of natural gas-fired capacity is also required in order to provide firm capacity, ensure system reliability and meet total system needs.
 - A greater portion of the replacement energy could be provided by wind, however this would increase the cost and require some form of large-scale energy storage to provide firm capacity/

Replacing off-ramped Darlington units with gas-fired generation results in an increase in greenhouse gas (GHG) emissions (i.e., about 5 - 6 Mt annually starting in 2026).

Replacing off-ramped units on a MW-per-MW basis with wind reduces GHG emissions relative to the natural gas option, but they are still higher than the base case with all Darlington units in service due to increased use of natural gas. Replacing off-ramped units with other generating sources makes it difficult to meet the electricity sector GHG emissions outlooks in the 2017 LTEP.

Cost Impacts:

Replacing off-ramped Darlington units with gas-fired generation results in similar cost outcomes, however the risk profiles of the two scenarios are very different.

- The primary risk for natural gas is operating cost, as the plants are exposed to natural gas and carbon price volatility. This is very difficult to forecast over a 20-year plant life and will increase end-user electricity price volatility.
- Conversely, the primary risk for nuclear refurbishment is capital cost, with very little variability in operating costs. The Darlington refurbishment is currently within its approved capital budget.

Replacing Darlington with renewables would substantially increase electricity costs as a large renewable build-out would be required. Replacing all of the electricity produced by off-ramped Darlington units would require a near doubling of the installed wind capacity in the province.

Renewable projects must balance three primary factors (Siting renewable projects that satisfy these three criteria would likely be difficult):

1. Wind and solar regime – developments are currently saturated at optimal locations;
2. Transmission connections – transmission congestion limits the amount of low-cost connection points; and
3. Municipal, regional and community support – the pool of supportive host communities is limited.

Economic Impact:

Off-ramping three out of the four Darlington refurbishments would greatly diminish the employment and economic benefits of the project.

- According to the Conference Board of Canada, Darlington refurbishment and continued operation of the facility up to 2055 is expected to contribute \$90 billion to Ontario's GDP and increase employment by an average of 14,200 jobs annually, including over 2,600 jobs onsite at Darlington.
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In addition to the loss of jobs and economic activity in the local communities around Darlington, the loss of these three refurbishments would severely impact Ontario's nuclear industry which is comprised of more than 180 supply chain companies across the province and supports 60,000 jobs.

Upcoming negotiations with labour unions could be adversely impacted by triggering the Darlington off-ramps.

- In March 2018, OPG's collective agreement expires with Power Workers Union (PWU) which represents thousands of OPG employees;
- OPG begins negotiations for a new collective agreement in early January 2018; and
- OPG's objective to realize additional efficiencies (i.e., additional ratepayer savings) would benefit significantly from long-term job security offered by the refurbishments.

Fiscal Impact Considerations:

OPG may incur up to **\$6 billion** in total "write-offs" as result of cost disallowances by the OEB following the off-ramp, which would be written down against net income to Government, including:

- A possible write-off of spend to-date on the Unit 3 refurbishment planning, if, through a future prudence review, the OEB determines that the planning cost is not reasonable in light of off-ramp;
- A possible write-off of capital costs of refurbishing Unit 2, if, through a future prudence review, the OEB determines that the higher per unit refurbishment cost is not reasonable to pass onto ratepayers given that it includes significant up-front planning that was intended for a 4-unit refurbishment project; and

- A possible write-off of increased costs of operating a one-unit station vs. a 4-unit station (i.e., due to loss of economies of scale), if, through a future prudence review, the OEB determines that it is not reasonable to pass the higher operating cost onto ratepayers.

In addition, cancellation of the remaining three Darlington units would reduce OPG's contribution to Government's income (ongoing net income and income tax PILs), as a result of foregone net income from capital investment (i.e., return on equity invested in the 3 foregone refurbishments):

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Darlington "Write-offs"	-3,700	-1,360	-780	-160	-	-	-	-	-	-
Ongoing Net Income & PIL's	-	-	-	-280	-350	-450	-560	-680	-820	-870

Note: Ongoing Net Income and PIL's reductions reflect: (i) foregone cost of capital recovery due to a lower asset base, and (ii) the compounding interest effects from lower cash receipts. While the impact of (i) generally declines over time, the effect of (ii) increases and more than offsets (i). Cost of capital is based on a deemed capital structure of 49% equity / 51% debt, return on equity of ~9% and debt rate of ~5%. PIL's are based on a 25% tax rate.

Overall, OPG projects that the foregone capital investment and possible write-offs due to non-recovery of costs from OEB would result in a reduction of OPG's contribution to government's income (net income and income tax PILs) of \$1,100 to \$1,400 million per year, on average, or \$43 to \$55 billion over Darlington's life.

APPENDIX F: OEB RATE-SETTING SEQUENCE (INCLUDING OEB DECISIONS)

- **2017-2021 Rate Application Period:**

- OPG will submit a 5-year rate application with forecast nuclear revenue requirement and forecast nuclear production over the 5-year period, including a forecast of Darlington Unit 2 refurbishment.
- OEB will determine OPG's appropriate revenue requirement and forecast nuclear production for the 5-year period as well as the amount of nuclear revenue requirement to be deferred until after Darlington refurbishments are complete and accordingly set OPG's "smoothed" nuclear rates for the 5-year period.
 - OEB Decision (EB-2016-0152) (December 28, 2017) – Approval of OPG's application relating to the Darlington Refurbishment Program (DRP), including the addition of \$4,800 million to rate base in 2020 when the first of the four units to be refurbished is expected to come back online.
 - TBS staff note OPG's application (approval of in-service additions to rate base) was updated for removal of the Heavy Water Facility project, which has experienced delays and cost overruns. OPG will be returning to the OEB and provide a detailed account of the history of the HWSF and be subject to OEB review and decision (to add to rate base, or written off by OPG if disallowed).
 - OEB decision pending on a follow-up OPG submission outlining proposed smoothed payment amounts in accordance with regulatory requirement to defer the collection of some the revenue from ratepayers. Only then will customer bill impacts be known.

- **2022-2026 Rate Application Period:**

- OPG will submit a 5-year rate application with forecast nuclear revenue requirement and forecast nuclear production over the 5-year period. OPG's revenue requirement would be informed by the actual refurbishment cost for Unit 2 which is expected to be complete by 2019 and a forecast of the remaining unit refurbishments.
- Similar to the 2017-2021 period, OEB will set smoothed rates for the 2022-2026 period while taking into account the actual refurbishment costs incurred to date, including undertaking a prudence review of the unit's refurbishment costs.

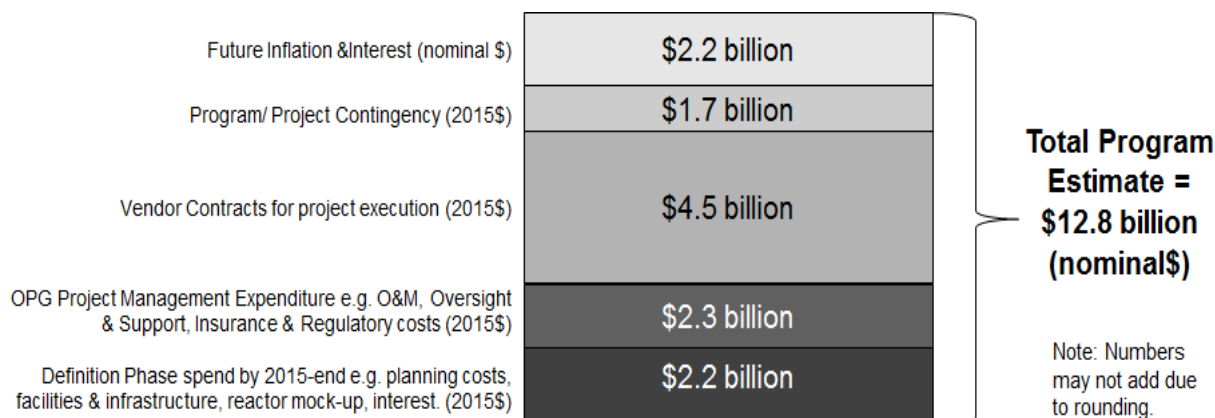
- **Rate Applications beyond 2027:**

- The Darlington Refurbishment Project is expected to be complete and all units in-service.
- OEB to conduct prudence review of Darlington refurbishment costs in setting rates.
- The rate setting period will be determined by OEB.
- OEB will ensure draw-down of prudently incurred costs in the rate-smoothing deferral account in no more than 10 years, on a straight-line basis.

APPENDIX G: DARLINGTON REFURBISHMENT “OFF-RAMPS” – ANALYSIS AND CONSIDERATIONS

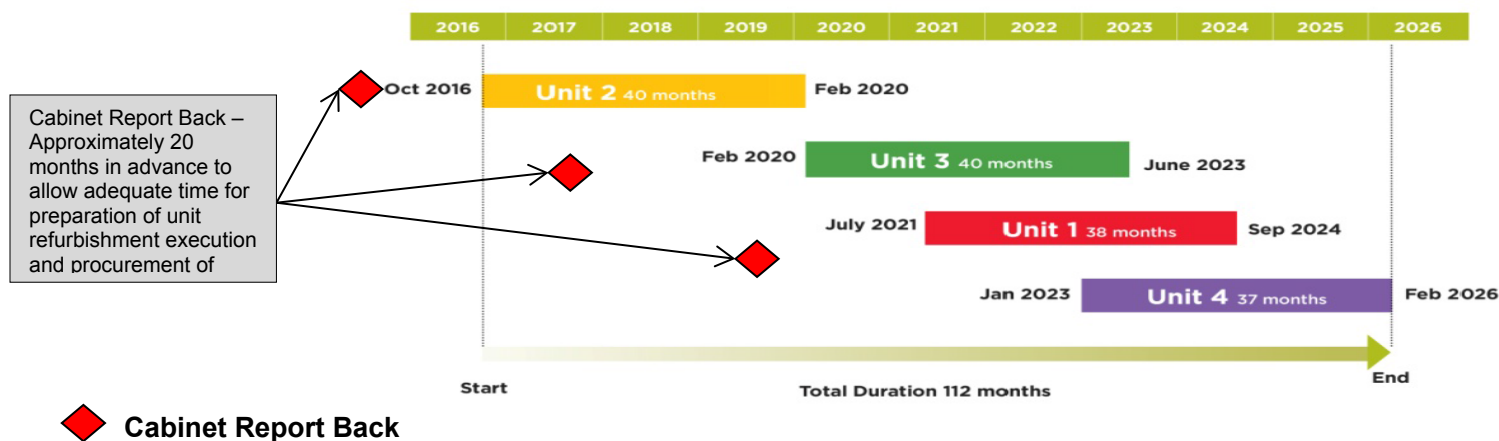
APPENDIX F: PROJECT BACKGROUND

In December 2015, following more than five years of detailed project planning and preparation, Cabinet approved OPG’s total budget of \$12.8 billion to refurbish the four nuclear units at Darlington (see chart below).



Cabinet also approved OPG’s total schedule of 112 months to refurbish the four units at Darlington (see chart below).

- To ensure that lessons learned from the Unit 2 refurbishment are incorporated into subsequent refurbishments, OPG will not commence execution of refurbishment work on Unit 3 until Unit 2 refurbishment is complete.
- Although Unit 2’s planned refurbishment completion date is February 2020, based on performance to date, OPG is expecting to be ready for execution of Unit 3 refurbishment as early as October 2019.
- The government has established off-ramps for the Darlington refurbishment project that may be used in the event that OPG fails to adhere to the approved budget and schedule for the project.



APPENDIX H: TIMELINE AND NEXT STEPS

