RE: BN FSM Fees 29 June 2017.docx

From: "Huang, Jackson (MEDG/MRIS)" <jackson.huang@ontario.ca>
To: "Calwell, Carolyn (ENERGY/MEDEI/MRI)" <carolyn.calwell@ontario.ca>
Cc: "Rehob, James (ENERGY)" <james.rehob@ontario.ca>
Date: Tue, 04 Jul 2017 20:59:37 -0400

Hi Carolyn,

Further to my earlier email, please see summary of precedents below for your review and consideration, which outlines the consideration and discussions James and I had last week regarding FSM fees:

1. Ontario Nuclear Funds Agreement (ONFA) : Not directly applicable.

- ONFA focuses more on the ability of the funds to meet future liabilities. The funds under ONFA are <u>assets</u> set aside for future costs (like a pension fund), and the FSM is managing <u>liabilities</u> to be repaid over time to fund short-term costs. Any performance payments based on the return of funds under the ONFA will not be directly applicable to the management of funding obligations under the OFHPA.
- The fees payable to the fund custodians/fund managers under the ONFA are set out in separate Segregated Fund Custodial Agreements, but we did not find a copy of such agreements. OPG makes contribution to the funds established under the ONFA, but does not seem to manage any of them.
- We found the adjustment mechanism for the fund value of the Used Fuel Segregated Fund (UFSF) established under the ONFA potentially helpful in developing a "cost-plus" strategy for FSM fees:
  - Under the ONFA, through the adjustment mechanism, any surplus (where actual fund value > "fixed" fund value) in the UFSF is returned to the Province, and the Province must make further payments to cover any deficits.
  - The "fixed" balance of the UFSF (i) covers all costs relating to the management of used nuclear fuel (including any brokerage and management fees for the fund), and (ii) grows by a rate of return equal to the discount rate (which is a fixed rate above inflation, as defined under the ONFA).
- In a proposed "cost-plus" model for FSM fees, the formula could provide for (i) all direct and indirect costs incurred by the FSM; and (ii) a minimum required rate of return set by the OEB (to give OEB meaningful discretion) to provide the FSM with the profit it must receive in order to be given the appropriate accounting treatment.
  - The FSM's minimum required rate of return could be expressed:
    (i) inversely in relation to the weighted-average interest rate (for example, weighted by dollar amount of each funding obligation) of all new funding obligations incurred during a calendar year; and/or
    (ii) as a percentage [fixed under regulation or determined by OEB] of the "surplus" (where present value of all funding obligations discounted at a fixed rate [to be prescribed or determined by OEB] > actual present value of all funding obligations) or "deficit" during a period [Note: this most closely tracks the adjustment mechanism in ONFA

and creates a direct relationship between the FSM fees and the dollar effect of FSM's management; a period can be more than one calendar year which means the FSM fees payable for a calendar year would not change until a triggering event]

2. **IESO Rate Order**: Not applicable.

- The IESO's business plan for 2016-2018 was first approved by the Minister, and then submitted to the OEB for approval. The same approval process (with business plan first approved by the Minister) does not apply to the FSM.
- The decision, EB-2015-0275, mainly focused on a specific issue in the rate application: whether a single per MWh usage fee should be charged for domestic and export market participants. In its decision, the OEB relied on a cost allocation study to set separate usage fees for export market participants, such that a revenue-to-cost ratio of close to 100% would be achieved for each group of market participants. The OEB accepted IESO's expenses and revenue requirements in the business plan that was approved by the Minister.
- A revenue-to-cost ratio test would not be appropriate for the FSM. A target revenue-to-cost ratio of 100% would not generate any profits/losses for the FSM to meet the accounting requirement.

3. Distribution Rate-Protection Program (DRP). May be useful for setting benchmarks/comparators

- Under this program, OEB has considerable discretion to approve base distribution rates for all distributors serving DRP consumers, and caps the base distribution rate charged to DRP consumers at the lowest among these distributors.
- One way to give OEB meaningful participation in setting FSM fees is to have the regulation prescribe specific comparators (e.g. enumerating specific entities who are seen by Government as appropriate comparators for OPG (e.g. OFA) to benchmark its costs and financial structure against), and allow OEB to determine a "maximum". Beneath that cap, the FSM is able to demonstrate whether or not it has provided the most cost-efficient approach to conduct financing activities (a modified prudence test which provides an outer limit and retains some discretion for the Board to evaluate actual success in meeting economic and other cost-minimization goals).

Please let me know if you have any questions or if you would like to discuss anything.

Thanks,
Jackson

From: Calwell, Carolyn (ENERGY/MEDEI/MRI)
Sent: July-04-17 4:11 PM
To: Huang, Jackson (MEDG/MRIS)
Subject: FW: BN FSM Fees 29 June 2017.docx

Hi Jackson, were you able to find any helpful precedent that might inform how we approach this issue?

Carolyn

From: Rehob, James (ENERGY)
Sent: June-30-17 10:02 AM

To: Nelms, Scott (MOF); Christie, Tim (ENERGY); Cayley, Daniel (ENERGY); O'Riordan, Eamon (ENERGY)
Cc: McKinlay, Tom (ENERGY); Huang, Jackson (MEDG/MRIS); Calwell, Carolyn (ENERGY/MEDEI/MRI); Montgomery, Kaitlin (MOF)
Subject: BN FSM Fees 29 June 2017.docx

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June 30, 2017

Good morning, Scott, Tim, Daniel and Eamon. Please find attached LSB's draft note on FSM Fees and options for OEB review and approval. Scott, in particular, we are hoping for your detailed review and comment, if that is possible, by before Tuesday morning, please. We hope to have this note up to ADM/DM on Tuesday.

With best regards,

James and Jackson

James P. H. Rehob
Senior Counsel
Ministry of the Attorney General
Legal Services Branch
MAG Civil Law Division
Ministry of Energy, Ministry of Economic Development and Growth, Ministry of Research, Innovation and Science, Ministry of Infrastructure, Accessibility Directorate of Ontario
56 Wellesley Street West
Toronto, ON M7A 2E7
Tel: 416-325-6676
Fax: 416-325-1781
james.rehob@ontario.ca