COMPENSATION AND BENEFITS

1.0 PURPOSE

The purpose of this Exhibit is to:

- Detail the total test period compensation and benefits costs included in the revenue requirement,
- Discuss OPG’s use of overtime,
- Describe the compensation framework for OPG’s regulated facilities,
- Respond to the OEB’s direction to file an independent compensation study, and
- Respond to the OEB’s direction to discuss alternatives to the use of AA bond yields to forecast the discount rates.

2.0 OVERVIEW

The following table summarizes OPG’s historical, bridge year and test period compensation and benefits levels:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Nuclear</td>
<td>1,297.7</td>
<td>1,317.8</td>
<td>1,173.3</td>
<td>1,215.6</td>
<td>1,195.8</td>
<td>1,219.1</td>
</tr>
<tr>
<td>Previously Regulated Hydro</td>
<td>50.4</td>
<td>54.5</td>
<td>51.8</td>
<td>57.1</td>
<td>58.4</td>
<td>59.0</td>
</tr>
<tr>
<td>Allocated Corporate Support</td>
<td>135.1</td>
<td>142.2</td>
<td>284.1</td>
<td>315.5</td>
<td>308.0</td>
<td>297.4</td>
</tr>
<tr>
<td><strong>Sub-total</strong></td>
<td><strong>1,483.2</strong></td>
<td><strong>1,514.5</strong></td>
<td><strong>1,509.2</strong></td>
<td><strong>1,588.2</strong></td>
<td><strong>1,562.2</strong></td>
<td><strong>1,575.5</strong></td>
</tr>
<tr>
<td>Newly Regulated Hydro</td>
<td>79.2</td>
<td>87.9</td>
<td>91.5</td>
<td>102.1</td>
<td>105.8</td>
<td>104.1</td>
</tr>
<tr>
<td>Allocated Corporate Support</td>
<td>18.6</td>
<td>18.7</td>
<td>23.0</td>
<td>23.6</td>
<td>26.4</td>
<td>25.3</td>
</tr>
<tr>
<td><strong>Sub-total</strong></td>
<td><strong>97.7</strong></td>
<td><strong>106.6</strong></td>
<td><strong>114.4</strong></td>
<td><strong>125.6</strong></td>
<td><strong>132.2</strong></td>
<td><strong>129.4</strong></td>
</tr>
</tbody>
</table>
As Table 1 above demonstrates, over the four years between 2011 and 2015, OPG’s total compensation and benefit cost for its regulated operations is projected to grow by a bit more than one per cent per year. This figure includes the effects of staff increases associated with Darlington Refurbishment and New Build.

Table 1 also illustrates the impact of increases in Pension and OPEB costs on overall regulated compensation costs. Pension and OPEB cost increases are driven primarily by changes in discount rates, a factor beyond OPG’s control. Total regulated compensation costs, excluding increases in Pension and OPEB costs, decline approximately 4% between 2010 and 2015.

OPG’s forecast compensation and benefit costs over the test period are reasonable, stable and below bridge year levels. Forecast compensation costs are largely a function of the collective bargaining agreements that cover about 90 per cent of OPG’s employees and to which OPG is legally bound. OPG cannot unilaterally reduce the compensation of its represented employees or reduce staff through the use of contract workers except as permitted by its collective agreements, and is limited in terms of its ability to adjust the overall size of the unionized workforce in order to cut costs.

Within the constraints of the collective agreements, OPG has taken steps to reduce staff levels, and modify its cost structure, consistent with its objective to continue

<table>
<thead>
<tr>
<th>TOTAL REGULATED COSTS</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,581.0</td>
<td>1,621.0</td>
<td>1,623.7</td>
<td>1,713.8</td>
<td>1,694.4</td>
<td>1,704.9</td>
</tr>
</tbody>
</table>

| Increase in Pension/OPEB Costs Since 2010 | 0.0 | 68.0 | 123.2 | 172.3 | 184.3 | 188.7 |

| TOTAL REGULATED COSTS EXCLUDING INCREASE IN PENSION/OPEB | 1,581.0 | 1,553.0 | 1,500.5 | 1,541.6 | 1,510.1 | 1,516.2 |

---

1. Includes base salary and wages, overtime, incentive pay, and total benefits (comprised of statutory benefits, employee health tax, non-statutory benefits, and current pension and other post employment benefits service cost).
2. The increase in pension/OPEB costs during the period is due primarily to decreases in discount rates, as discussed in Section 6.0.
being a low cost provider of electricity in Ontario. As fully discussed in Ex. A4-1-1, by
year-end 2015 OPG expects to reduce its 2011 headcount by 2,000 employees
through attrition. This decreased headcount is expected to reduce OPG’s OM&A by
$700M between 2011 and 2015.³

- Safe and reliable operations remain OPG’s top priority. Key to meeting this priority is
having employees with the appropriate skills and experience. OPG must continue to
be able to attract and retain the highly specialized and skilled staff needed to manage
and operate its complex generating stations, particularly in the Nuclear business.

As discussed below in Section 3, OPG uses contract employees and overtime as tools to
meet peak work periods. In Nuclear these periods are largely, but not exclusively, associated
with outages when base resources are insufficient to meet all of the scheduled work (See
Ex.F2-4-1, Section 3.2). OPG also uses overtime for Nuclear base OM&A work to meet peak
work requirements, maintain coverage for key staff positions in accordance with licensing
requirements; and complete necessary work impacted by short-term absences (See Ex. F2-
2-1, Section 3.2). In hydroelectric these resources are used for peak work requirements (e.g.
outages and responding to weather events), seasonal work, or to complete necessary work
impacted by short-term staff absences or vacancies (See Ex. F1-2-1, Section 3.1.2).

The remainder of this Exhibit is organized as follows:

Section 3.0 – OPG’s Workforce. This section discusses OPG’s workforce, including
staffing levels, use of contract employees and overtime, demographics and the extent
of unionization.

Section 4.0 – OPG’s Collective Agreements and Labour Relations Environment. This
section discusses OPG’s collective bargaining agreements, its approach to collective
bargaining and the labour relations context in which OPG operates.

³ Of these figures, approximately 1,300 staff and $550M are attributable to regulated operations.
Section 5.0 – Management Compensation. This section discusses OPG’s management compensation costs.

Section 6.0 – Pension and Benefits. This section discusses pension and benefit plans reflected in OPG’s compensation levels.

Section 7.0 – Summary of Staffing, Compensation and Benefits. This section summarizes OPG’s staffing, and compensation and benefit levels.

Section 8.0 – Business Transformation. This section discusses the significant impact Business Transformation will have on OPG’s forecast of test period compensation levels.

Section 9.0 – Benchmarking. This section discusses the results of the compensation benchmarking performed by AON Hewitt.

Section 10.0 – Conclusion.

3.0 OPG’s WORKFORCE

At the end of 2012, OPG had approximately 10,844 regular employees. Of this total approximately 9,453 employees work directly in or are allocated to OPG’s regulated activities. This figure includes some 8,313 employees associated with OPG’s nuclear business, 433 employees associated with the previously regulated hydroelectric plants and 707 employees associated with the newly regulated hydroelectric facilities.

OPG’s regulated staff work in a predominantly unionized environment, with approximately 90 per cent of staff belonging to either the Power Workers’ Union (“PWU”) or the Society of Energy Professionals (“Society”). Of this 90 per cent, approximately two thirds belong to the PWU and approximately one third belong to the Society. The extent of unionization and the mix of PWU, Society and non-represented staff have generally remained stable.
OPG has a mature and experienced workforce. As of year-end 2012, approximately 20% of active employees were eligible to retire with an undiscounted pension. By the end of the test period (year-end 2015) more than 28% of the year-end 2012 employees will be eligible to retire.

In 2011, OPG began a Business Transformation initiative to better align cost with revenue and improve efficiency so as to be able to operate with fewer employees (see Ex. A4-1-1). Through attrition, OPG has a company-wide staff reduction target of 2,000 by the end of 2015 and has already realized half this target (i.e., a headcount reduction through attrition of approximately 1,000 employees since 2011). Business Transformation focuses on building the framework for long-term sustainable operation at these lower staffing levels by re-engineering programs and restructuring to streamline and simplify. Becoming a leaner, more efficient organization will help ensure OPG’s financial sustainability, allow the pursuit of opportunities to strengthen and grow the company and deliver on OPG’s mission to be Ontario’s low-cost electricity generator of choice.

OPG uses a variety of resource types to meet ongoing, planned and unplanned work requirements. These are outlined below:

1. Regular Staff: Employees hired directly by OPG with the expectation of on-going, long-term employment. This category includes probationary, as well as part-time regular employees and regular-seasonal staff (employees who are permanently employed, but subject to seasonal, layoffs).

2. Non-Regular Staff: Temporary Employees hired directly by OPG where there is little or no expectation of on-going employment. This category includes:
   • Students and other temporary employees hired into PWU, Society or non-represented positions.

\(^4\) Approximately 1,300 staff out of the target staff reductions of 2,000 are attributable to regulated operations.

\(^5\) A number of strategies and programs are in place to mitigate the risk of knowledge loss associated with ongoing retirements, including succession planning, training & development programs, knowledge management risk assessments and the development of retention plans where necessary.
• Temporary tradespersons and members of various craft unions hired by OPG from the trade union halls where there is little or no expectation of on-going employment. These are often referred to as casual construction staff.

3. Overtime: Incremental pay, as set out in collective agreements, to regular employees represented by the PWU or Society or to non-regular staff for work outside of their core hours.

4. Purchased Services: External services used to augment OPG’s resources. These resources are not hired directly by OPG as employees. They can be:
   • Individuals engaged “independently”, through a pre-qualified staffing agency or provided by another, external firm. These are often referred to as augmented staff. These individuals typically work in the same environments as employees and under the direct supervision of an OPG staff person.
   • Work provided by third parties where OPG defines the outcome but the resources are not under the direct supervision of OPG staff. This category includes consultants, construction contractors, maintenance services and specialised technical services.

As outlined in Nuclear and hydroelectric evidence (See Ex. F1-2-1, Section 3; Ex. F2-4-1, Section 3.2; and Ex. F2-2-1 Section 3.2) there are a number of factors that lead to the use of resources incremental to regular staff:
   • Compliance with collective agreements
   • To meet planned and unplanned peak work demand when it is not economic to maintain ongoing regular staff compliments at levels required for periodic peaks
   • Where required skills are not available internal to OPG
   • To meet a short term need to complete necessary work such as projects or to replace employees on maternity leave and other short term absences

OPG’s business units determine the resource option to employ based on factors such as cost, time frame (duration of need and lead time), availability of internal resources (skills and capacity) and the need for specialized skills or equipment.
4.0 OPG’s COLLECTIVE AGREEMENTS AND LABOUR RELATIONS ENVIRONMENT

Pursuant to the Ontario Labour Relations Act, as a successor employer to Ontario Hydro, OPG was required by law to adopt collective agreements covering the employees transferred from Ontario Hydro to OPG when it began operation on April 1, 1999. For the unionized employees within OPG, items such as wages, pensions, and benefits can only be changed through the collective bargaining process; they cannot be changed unilaterally by OPG.

The nature of collective bargaining dictates that outcomes result from agreements reached by both parties. To obtain agreement, parties often must modify their initial positions. Ultimately, “success” in collective bargaining is influenced by the priorities and approaches pursued by both management and the union over the course of negotiations. Since subsequent collective agreements build on past agreements, changes can only occur where bargaining produces new arrangements that both sides can agree to.

4.1 OPG’s Approach to Collective Bargaining

OPG and its unions follow a formal and structured approach to collective bargaining. The following paragraphs outline the process.

Research and Consultation — OPG begins with a review of the external labour relations landscape. The review focuses on the bargaining results of Ontario Hydro successor companies and other broader public sector employers. Included in the review is an assessment of recent agreements and arbitrated decisions relating to wages, benefits, pensions, contracting out, job security, productivity issues, and other compensation issues. Sources used as part of this review include the Ministry of Labour (MOL) and successor companies collective agreements. The economic and political environment is also reviewed to evaluate general economic conditions and to identify any government directives or initiatives that impact collective bargaining. Internal consultation is carried out to identify key strategic, operational, cost, revenue and productivity issues facing the company.
Formation of the Bargaining Team – Representatives from OPG’s business units are
selected by business unit leaders to represent OPG in collective bargaining. The individuals
selected are senior level, experienced leaders with good insight into the strategic and key
operational issues facing the company. The collective bargaining process is directed by an
experienced team of labour relations staff who have extensive negotiating experience and
frequent dealings with OPG’s unions. OPG periodically engages external labour lawyers
directly in collective bargaining or to advise on key issues. OPG’s legal support is comprised
of experienced lawyers who represent major Canadian employers including other
government agencies.

Development of the Bargaining Agenda – The Bargaining Team develops the bargaining
agenda based on the company’s priorities. OPG’s priorities are established by soliciting input
from across the company on key issues that should be addressed through the collective
bargaining process. Each item is critically evaluated on its merits and prioritized based on the
value to the company and anticipated reaction of the relevant union. The team also
anticipates items that will be brought forward by the unions. These items are assessed based
on their value and compared to OPG’s items to determine potential areas of agreement.
OPG and the union exchange bargaining agendas at an agreed date at the start of
negotiations.

Negotiations – A schedule for negotiations is established based on the expiry date of the
collective agreements to allow time for meaningful discussions. For the Society, a typical
round of negotiations takes approximately one month; for the PWU negotiations take
anywhere from two to four months. These estimates do not include the preparation time
involved for each side. OPG’s negotiating team is led by a management chairperson who is
accountable for representing the company and empowered to reach an agreement based on
a mandate approved by the Board and consistent with Government direction. The
chairperson works to ensure that key priorities are achieved and reports on major
developments to the executive leadership team.
Impasse – In the event of an impasse with the PWU, the parties are required to satisfy statutory requirements of the Ontario Labour Relations Act (the Act) before engaging in a strike/lockout. Where the parties become deadlocked on issues they must engage in mandatory conciliation under the Act. Mandatory conciliation involves the appointment of a mediator by the Minister of Labour to confer with the parties in the interest of resolving any impasse prior to a work stoppage. OPG and the PWU have engaged in mandatory conciliation twice in recent history following a deadlock. In the event of an impasse with the Society, the parties are required to enter into an interest mediation/arbitration process due to the no strike/no lock-out clause in the collective agreement. OPG and the Society have used interest mediation/ arbitration to resolve their differences for the two most recent contracts.

Agreement/Award – Where an agreement is reached, the unions must take the agreement out for a ratification vote by their members. Once an agreement/award is finalized, the details of the agreement are communicated through a comprehensive change management plan that is put in place to ensure line managers are informed about contract changes.

Implementation – Once the parties have an agreement (or arbitration award), Labour Relations oversees the implementation of the changes to the collective agreement.

4.2 The PWU and Society Collective Agreements

As discussed above, OPG has collective agreements with the PWU and the Society covering approximately 90 per cent of its regulated staff. The PWU represents the majority of employees who perform the work of technicians, tradespersons, plant operators, security guards and administrative assistants.

4.2.1 PWU

The current collective agreement with the PWU covers the period from April 1, 2012 to March 31, 2015. The wage increases provided under agreement are: April 1, 2012 – 2.75%; April 1, 2013 - 2.75%; and April 1, 2014 - 2.75%.
The PWU agreement was negotiated in early 2012. Prior to that time, the Government had passed the Public Sector Compensation Restraint to Public Services Act, 2010 (Compensation Restraint Act) as part of Bill 16. The Compensation Restraint Act included measures to extend controls over management compensation. While its provisions covered only OPG’s non-unionized employees, the Government requested that OPG, and other Provincially-owned entities, achieve contracts with net zero compensation increases, meaning any increase in compensation had to be offset by corresponding savings elsewhere in the collective agreement. OPG negotiated a number of cost and productivity offsets to the wage increases in the PWU agreement.

OPG tracks the differences between the union wages it pays and those that other employers pay to the extent possible. The primary competitor for nuclear jobs represented by the PWU is Bruce Power LP. A wage comparison, conducted following the last round of negotiations between the PWU and Bruce Power LP is shown in Table 2. Overall OPG wages for PWU represented staff are lower than those at Bruce Power LP.

**Table 2 - 2013 Wage Comparison of PWU Positions between OPG and Bruce Power**

<table>
<thead>
<tr>
<th>PWU Job Category (2013)</th>
<th>OPG</th>
<th>Bruce Power</th>
<th>Difference ($/Hr)</th>
<th>Difference (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Civil Maintainer I</td>
<td>$38.95</td>
<td>$52.36</td>
<td>-$13.41</td>
<td>34.43%</td>
</tr>
<tr>
<td>Emergency Response Maintainer</td>
<td>$38.95</td>
<td>$47.19</td>
<td>-$8.24</td>
<td>21.16%</td>
</tr>
<tr>
<td>Civil Maintainer II</td>
<td>$38.95</td>
<td>$49.04</td>
<td>-$10.09</td>
<td>25.91%</td>
</tr>
<tr>
<td>Nuclear Operator</td>
<td>$50.08</td>
<td>$58.32</td>
<td>-$8.24</td>
<td>16.45%</td>
</tr>
<tr>
<td>Shift Control Technician</td>
<td>$50.08</td>
<td>$57.27</td>
<td>-$7.19</td>
<td>14.36%</td>
</tr>
<tr>
<td>Mechanical Maintainer</td>
<td>$50.08</td>
<td>$57.10</td>
<td>-$7.02</td>
<td>14.02%</td>
</tr>
<tr>
<td>Nuclear Security Officer</td>
<td>$38.95</td>
<td>$40.87</td>
<td>-$1.92</td>
<td>4.93%</td>
</tr>
<tr>
<td>Business Support Representative (OPG - Office Support Representative II)</td>
<td>$38.95</td>
<td>$46.02</td>
<td>-$7.07</td>
<td>18.15%</td>
</tr>
<tr>
<td>Project Tech II – E&amp;C (OPG - Project Technician - E&amp;C)</td>
<td>$50.08</td>
<td>$51.34</td>
<td>-$1.26</td>
<td>2.52%</td>
</tr>
<tr>
<td>Chemical Technician</td>
<td>$50.08</td>
<td>$51.99</td>
<td>-$1.91</td>
<td>3.81%</td>
</tr>
<tr>
<td>Cost &amp; Scheduling Technician (OPG - Planning &amp; Cost Control Technician)</td>
<td>$50.08</td>
<td>$52.63</td>
<td>-$2.55</td>
<td>5.09%</td>
</tr>
<tr>
<td>Finance Clerk (OPG- Finance &amp; Payroll Representative)</td>
<td>$38.95</td>
<td>$48.74</td>
<td>-$9.79</td>
<td>25.13%</td>
</tr>
</tbody>
</table>

* Wage comparisons for PWU positions are based on top step of the OPG salary bands and top step of the Bruce Power competency based scales or multi-trade scales (if applicable).

Bruce Power wage information was obtained from the collective agreement between Bruce Power and the PWU. The above classifications account for the majority of Bruce Power
classifications. Some classifications in OPG do not exist at Bruce Power (e.g., Thermal and Hydroelectric classifications).

The following table compares OPG’s base wage increases for the PWU since 2001 to the increases in other companies that have collective agreements derived from Ontario Hydro. Cumulative compound 2001-2012 increases are shown for all organizations. Compound increases through 2013 and 2014 are provided where available. OPG negotiated increases have been at or below most of the successor companies in most years since 2001 resulting in cumulative increases that are below most of the successor companies. A comparison of recent (2010-2013) negotiated increases where data is available shows OPG has continued to achieve equal or lower increases. During this period OPG negotiated a simple cumulative increase of 11.5%, which is lower than or equal to Bruce Power (12%), Hydro One (11.5%) and Kinetics (12%).

### Table 3 – PWU Increases Compared Among Successor Companies

<table>
<thead>
<tr>
<th>Year</th>
<th>OPG</th>
<th>Bruce Power</th>
<th>Hydro One</th>
<th>Kinetics</th>
<th>New Horizons</th>
<th>Inergi</th>
<th>IESO</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>0.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.00%</td>
</tr>
<tr>
<td>2002</td>
<td>2.00%</td>
<td>3.10%</td>
<td>3.00%</td>
<td>5.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.00%</td>
</tr>
<tr>
<td>2003</td>
<td>3.00%</td>
<td>4.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.50%</td>
<td>2.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2004</td>
<td>2.50%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.50%</td>
<td>3.25%</td>
<td>4.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2005</td>
<td>2.50%</td>
<td>3.00%</td>
<td>3.50%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.50%</td>
</tr>
<tr>
<td>2006</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.50%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.75%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2007</td>
<td>3.00%</td>
<td>3.25%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2008</td>
<td>3.00%</td>
<td>3.20%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2009</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2010</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.70%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2011</td>
<td>3.00%</td>
<td>2.75%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.70%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2012</td>
<td>2.75%</td>
<td>2.75%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.70%</td>
<td>2.60%</td>
<td>2.50%</td>
</tr>
<tr>
<td>Cumulative</td>
<td>39.5%</td>
<td>44.0%</td>
<td>44.0%</td>
<td>40.4%</td>
<td>43.8%</td>
<td>41.7%</td>
<td>38.5%</td>
</tr>
<tr>
<td>2013</td>
<td>2.75%</td>
<td>3.50%</td>
<td>2.50%</td>
<td>3.00%</td>
<td>2.60%</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>Cumulative</td>
<td>43.3%</td>
<td>49.1%</td>
<td>47.6%</td>
<td>44.6%</td>
<td>47.5%</td>
<td>n/a</td>
<td>n/a</td>
</tr>
</tbody>
</table>
The Society of Energy Professionals represents the majority of employees who perform the work of professional engineers, front line managers, and accountants. The current collective agreement with the Society covers the period from January 1, 2013 to December 31, 2015. Pursuant to the Government’s direction, OPG attempted to negotiate zero compensation increase in the current collective agreement. When a negotiated agreement was not achieved, the matter was submitted to interest arbitration as the collective agreement requires. The terms of the agreement, including compensation were fixed by binding arbitration conducted within the criteria established by the collective agreement, and the generally established protocol for interest arbitrators (See Attachment 1, “An Assessment of the Industrial Relations Context and Outcomes at OPG” by Professor Richard Chaykowski, which is discussed in Section 4.4).

The collective agreement requires the arbitrator to consider:

1. A balanced assessment of internal relativities, general economic conditions, external relativities
2. OPG’s need to retain, motivate and recruit qualified staff
3. The cost of changes and their impact on total compensation
4. The financial soundness of OPG and its ability to pay

Section 4.4 below and Attachment 1 provide additional discussion of the considerations that inform interest arbitration decisions.

The Interest Arbitrator awarded annual increases over 2013, 2014 and 2015 of 0.75, 1.75 and 1.75 per cent, respectively, based on his assessment of the criteria and evidence presented by each side. He also ordered a temporary freeze on pay progression through the established pay grid for employees during the 2nd and 3rd years of the collective agreement (2014 and 2015).
Table 4 below compares OPG’s 2013 pay ranges for the various classifications (bands) of Society represented employees to those of Bruce Power. For each band, both the minimum and the maximum weekly salary offered by Bruce Power exceed the corresponding salary offered by OPG. For the highest salary bands (MP5 and MP6), Bruce Power’s minimum weekly salary is more than five percent above OPG.

Table 4 - 2013 Wage Comparison between Society Bands for Bruce Power and OPG ($ per week)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>MP6 Max</td>
<td>2509.67</td>
<td>2528</td>
</tr>
<tr>
<td>Min</td>
<td>2162.66</td>
<td>2274</td>
</tr>
<tr>
<td>MP5 Max</td>
<td>2353.50</td>
<td>2372</td>
</tr>
<tr>
<td>Min</td>
<td>2006.49</td>
<td>2133</td>
</tr>
<tr>
<td>MP4 Max</td>
<td>2207.26</td>
<td>2224</td>
</tr>
<tr>
<td>Min</td>
<td>1286.42</td>
<td>1331</td>
</tr>
<tr>
<td>MP3 Max</td>
<td>2070.93</td>
<td>2086</td>
</tr>
<tr>
<td>Min</td>
<td>1286.42</td>
<td>1331</td>
</tr>
<tr>
<td>MP2 Max</td>
<td>1942.05</td>
<td>1957</td>
</tr>
<tr>
<td>Min</td>
<td>1286.42</td>
<td>1331</td>
</tr>
</tbody>
</table>

Table 5 below compares base wage increases for Society represented employees since 2001 to the increases in companies that have collective agreements derived from Ontario Hydro. Cumulative compound 2001-2013 increases are shown for all organizations. Compound increases through 2014 and 2015 are provided where available. As with PWU, OPG’s increases have been at or below most of the successor companies in most years since 2001 resulting in compound increases that are below most of the successor companies. A comparison of recent (2010-2013) cumulative increases shows OPG has continued to achieve lower increases. During this period OPG achieved a simple cumulative increase of 9.75%, which is lower than Bruce Power (12%), and all other successor organizations.
Table 5 – Society Wage Increases Compared Among Successor Companies

<table>
<thead>
<tr>
<th></th>
<th>OPG</th>
<th>Bruce Power</th>
<th>Hydro One</th>
<th>Kinetics</th>
<th>New Horizons</th>
<th>Inergi</th>
<th>IESO</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>1.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>4.50%</td>
</tr>
<tr>
<td>2002</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.00%</td>
<td>1.00%</td>
<td>2.50%</td>
<td>2.00%</td>
<td>4.00%</td>
</tr>
<tr>
<td>2003</td>
<td>2.00%</td>
<td>2.00%</td>
<td>3.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2004</td>
<td>3.00%</td>
<td>4.00%</td>
<td>3.00%</td>
<td>2.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2005</td>
<td>3.00%</td>
<td>3.25%</td>
<td>4.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2006</td>
<td>3.00%</td>
<td>3.25%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2007</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2008</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2009</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>2010</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>2.50%</td>
<td>3.00%</td>
<td>2.60%</td>
</tr>
<tr>
<td>2011</td>
<td>3.00%</td>
<td>2.75%</td>
<td>2.50%</td>
<td>3.00%</td>
<td>2.75%</td>
<td>3.00%</td>
<td>2.70%</td>
</tr>
<tr>
<td>2012</td>
<td>3.00%</td>
<td>2.75%</td>
<td>2.50%</td>
<td>3.00%</td>
<td>2.75%</td>
<td>2.75%</td>
<td>2.85%</td>
</tr>
<tr>
<td>2013</td>
<td>0.75%</td>
<td>3.50%</td>
<td>2%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>1.50%</td>
<td>2.00%</td>
</tr>
<tr>
<td>Cumulative</td>
<td>41.6%</td>
<td>46.8%</td>
<td>44.0%</td>
<td>38.5%</td>
<td>43.3%</td>
<td>41.6%</td>
<td>47.8%</td>
</tr>
<tr>
<td>2014</td>
<td>1.75%</td>
<td>2.75%</td>
<td>2.25%</td>
<td>n/a</td>
<td>n/a</td>
<td>1.50%</td>
<td>2.00%</td>
</tr>
<tr>
<td>Cumulative</td>
<td>44.0%</td>
<td>50.9%</td>
<td>47.2%</td>
<td>n/a</td>
<td>n/a</td>
<td>43.7%</td>
<td>50.7%</td>
</tr>
<tr>
<td>2015</td>
<td>1.75%</td>
<td>n/a</td>
<td>2.25%</td>
<td>n/a</td>
<td>n/a</td>
<td>1.50%</td>
<td>n/a</td>
</tr>
<tr>
<td>Cumulative</td>
<td>46.6%</td>
<td>n/a</td>
<td>50.6%</td>
<td>n/a</td>
<td>n/a</td>
<td>45.9%</td>
<td>n/a</td>
</tr>
</tbody>
</table>

4.3 Other Relevant Terms of the Collective Agreements.

As in most unionized environments, OPG’s collective agreements with both the PWU and Society restrict the company’s ability to reduce compensation costs through contracting out work or reorganizing the workforce. The paragraphs below explain how these limitations are structured in both the PWU and Society agreements.

4.3.1 Contracting Out

With respect to contracting out, both the PWU and Society collective agreements contain clauses that restrict the degree to which OPG can contract out the work of employees who are members of the union. Given the degree of unionization, these clauses capture
substantially all of the work at OPG. As discussed below, in general terms, the contracting
out clauses are principle-based and rely on management and union cooperation to assess
the merits of contracting out against the impact on employment continuity. With some
exceptions, the agreement of the union is required before work can be contracted out. In the
event of a disagreement an arbitrator is required to determine whether or not the contracting
is permissible.

4.3.1.1 PWU

Contracting out has been a long standing issue between OPG and PWU. Since the late
1970’s, the PWU agreement has contained a provision for job security in the event that the
contracting out of work normally performed by PWU members results in job loss. The
genesis of the current restrictions on contracting out in the PWU collective agreement is
found in the resolution of a province-wide strike in 1985. To avoid another strike over this
issue, the parties have agreed on a provision that requires a significant assessment of the
merits of contracting compared to the impact on employment continuity.

The existing clause in the PWU collective agreement provides for a jointly managed process
for determining what work can be contracted out. The process for contracting work is
stringent and requires OPG to justify its proposals to contract work and assess the impact on
employment continuity. For work to be contracted out there must be joint agreement between
OPG and the PWU. Failing agreement, any work to be contracted out requires the
development of a business case that compares the benefits of contracting out versus
performing the work internally and assesses the impact on employees. Where agreement
cannot be reached the dispute moves to arbitration for resolution.

One unique aspect of the contracting out provision with the PWU is the use of thresholds to
establish amounts or types of work that can be contracted. Thresholds represent agreed,
pre-defined characteristics that if met, enable OPG to contract out without additional union
approval. A new threshold was negotiated in 2012 to provide that distinct work programs or
packages of 250 hours or less are within the threshold.
4.3.1.2 Society

The Society collective agreement includes a detailed process for contracting out work normally performed by Society members. The process is managed jointly between the Company and the Society and is designed to make effective business decisions through the full involvement of employees and their representatives in the decision-making process. For work to be contracted out there must be joint agreement between OPG and the Society. Failing agreement, any work to be contracted out requires the development of a business case that supports contracting out versus performing the work internally and assesses the impact on employees. Where no agreement is reached, the dispute moves to arbitration for resolution.

In 2010, OPG and the Society agreed to suspend the collective agreement provision on contracting out work in favour of an alternative agreement. Under this agreement, OPG obtained flexibility to contract out work in exchange for agreeing that it would not lay off employees as a direct result of contracting. OPG can contract work up to an annual value of $165M. For any contracting in excess of $165M per year, a payment equal to 1% of the amount in excess of $165M is paid to the Society. The company is required to advise the Society on the amount of contracting through regularly scheduled meetings and reports detailing the annual amounts spent. This agreement also provides a similar payment for contracted out work in the context of major, multi-year projects such as the Niagara Tunnel and the Darlington Refurbishment Projects that would be otherwise performed by Society represented employees. These payments are made on an annual basis over the life of the project. This agreement will expire on December 31, 2015 unless it is renewed.

4.3.2 Re-organizing the Workforce.

Re-organization of the workforce entails reducing and redistributing staff, and restructuring jobs. Each of these aspects of reorganization is limited by the collective agreement. Where OPG determines a staff excess, three options can be employed: redistribute excess staff to fill vacant positions; encourage employees to resign by offering a voluntary severance package; or invoke a layoff process.
4.3.2.1 PWU

In general, the PWU collective agreement uses seniority to govern re-organization of the workforce. Seniority dictates that employees with the most service have a right to continued employment over employees with less service. Under a layoff, the collective agreement provides that an employee who is qualified and senior can displace another employee with less service anywhere in the province. The displacement of employees disrupts business operations, involves re-training and can involve relocation costs where employees are required to relocate more than specified distances. Employees who are laid off are entitled to severance, or can elect to be recalled to a vacant position within 3 years from their date of layoff.

Voluntary severance is an alternative to lay-offs. Under a voluntary severance arrangement OPG is required to make severance packages available to broad classes of employees and must select employees in order of seniority from those who volunteer for severance. Thus, OPG can control how many employees leave, but has limited control over which employees leave. Given the lack of ability to control which employees leave, workforce rebalancing often is required to match the remaining employees to the positions created by senior employees volunteering to leave. This process also disrupts business operations and requires re-training and relocating employees.

In lieu of layoff or severance, OPG can redistribute staff to balance staffing levels in circumstances where a demand for labour exists in one area and excess labour exists in another. Like layoffs and voluntary severance, staff redistribution is based on seniority. Thus, the actual employee whose position is in excess of OPG’s needs may not be the employee who ends up transferring. Retraining may be required when an employee is displaced and if an employee is required to relocate over a specified distance, OPG incurs relocation cost.

Based on collective bargaining with the PWU, a no lay-off clause was included in the PWU contract. As a result, excess staff can only be addressed through staff redistribution or voluntary severance.
4.3.2.2 Society

The Society collective agreement contains an employment continuity clause which addresses layoff, voluntary severance and redistribution of employees. Many aspects of the Society agreement are the same as the PWU agreement discussed in the preceding section. The primary difference is how excess employees are identified for lay-off or redistribution. While seniority is a feature of the process, the dominant factor is the employee’s skill set.

Under the agreement with the Society, the parties must jointly match employees’ skills to positions in the organization and then identify which employees are excess. Determining which employees are excess involves examining the qualifications of each employee against the qualifications for each job identified in the organization. Where multiple employees are qualified for the same job, seniority applies. As a result, the person currently doing a job may not retain it if another qualified employee has seniority. Once this matching is completed, employees are either laid off or redistributed to other organizations.

Where an employee is displaced, re-training is offered. An employee who is laid off is entitled to a job search period of up to 60 weeks to secure employment in OPG. During the search period the employee remains on the payroll. An employee who has not found a new position during the search period is severed.

The entire exercise of lay-offs and redistribution is disruptive to business operations due to employee turnover, and the time required for retraining and relocating employees. Redistribution of excess employees may result in re-training and relocation costs.

4.4 The Labour Relations Context

OPG’s compensation levels and the terms of the PWU and Society collective agreements exist within a labour relations context defined by legal requirements and a long history of collective agreements. This context bears directly on the amount of compensation paid by OPG and on the prospects of achieving significantly different labour costs.
To assist in understanding this context, Attachment 1 is a report by Professor Richard Chaykowski, entitled “An Assessment of the Industrial Relations Context and Outcomes at OPG.” Dr. Chaykowski, a faculty member in the School of Policy Studies and in the Faculty of Law (cross-appointed) at Queen’s University. He has been a visiting scholar at MIT, the University of Toronto and McGill University. Dr. Chaykowski is a recognized expert in the area of labour relations. As set out in his report, it is Dr. Chaykowski’s opinion that:

- The compensation levels and increases of unionized employees at OPG are determined solely through the collective bargaining process, and not through the unfettered interaction of supply and demand in the labour market.
- The set of main factors that determine the relative bargaining power of the major unions and OPG all function to increase the bargaining power of the unions relative to the bargaining power of OPG.
- Consistent with the empirical research evidence that unions deliver a sizable wage premium, both the PWU and Society should be successful in raising compensation levels considerably above the wage levels that would be expected to prevail in broader competitive labour markets characterized by little or no unionization.
- In terms of pay and other employment related outcomes, the relevant and appropriate comparators for OPG are those firms that are subject to similar regulatory and legislative regimes, especially labour relations policy, similar legal regimes, and that have similarly high levels of unionization.
- OPG wage settlements tend to track the negotiated increases in the Ontario broader public sector over time. This outcome is to be expected given the very high level of unionization across the Ontario public sector, and in the electricity industry.
- The most recent OPG contract settlement with the PWU and interest arbitration award for the Society include lower pay increases than the previous contracts. This outcome is consistent with the long term trend whereby negotiated wage settlements at OPG tend to track the average wage negotiated in large Ontario broader public service bargaining units.

5.0 MANAGEMENT COMPENSATION
As a result of the Agency Review Panel findings, OPG has adopted a Management Group (MG) compensation policy of generally paying at the 50th percentile while balancing the need to attract and retain qualified staff. In some instances OPG has paid above the 50th percentile for key positions where it has been difficult to attract and retain the necessary talent. OPG’s MG compensation complies with government requirements.

Each fall, OPG’s MG compensation band structure and base pay merit budget are reviewed against external benchmarks to ensure that MG compensation is in line with the 50th percentile. Since 2008, changes to OPG MG compensation have been driven by self-imposed salary restraints and Government legislation in the form of Bill 16 and Bill 55. The MG band structure has been frozen since 2008 and base pay and merit increases have been restricted as follows:

- In January 2009, OPG voluntarily imposed the same constraints the Ontario Government had implemented for elected officials and government employees. These were: no base pay increases for senior management, and base pay budgets were established providing 1.5 per cent for employees earning greater than $150,000 and 2 per cent for remaining employees. These increases were below the average general market increases of 3.5% as reported by major salary surveys. In 2009, OPG also voluntarily rolled back all incentive payments by 5%.

- In January 2010, OPG voluntarily imposed a base pay budget limit of 1.5 per cent. This budget was distributed according to competency and performance levels. There were no across-the-board increases. The increases were below general market increases which ranged between 2.3% and 3.0% as reported by major salary surveys. Also in 2010, OPG voluntarily rolled back all incentive payments by 10%.

- Effective March 2010, the Ontario Government introduced the Public Sector Compensation Restraint to Protect Public Services Act (part of Bill 16) for employees that do not collectively bargain compensation. The Act prohibited increases in pay ranges for non-bargaining employees before April 2012, but did allow increases based on individual merit.

- In January 2011 there were no MG base pay increases and the salary structure remained frozen.
In March 2012, the Government introduced Bill 55, the Strong Action for Ontario Act (Budget Measures), which included measures to extend controls over executive compensation. The Act covers OPG’s MG employees at the Vice President level and above and is to remain in effect until the Province of Ontario ceases to have a budget deficit. Additionally, in response to OPG’s financial situation and Government preference for net-zero wage increase, OPG extended the Bill 55 restrictions to all MG staff including those below the Vice President level. No adjustments have been made to base salaries for any MG employee except as permitted under the Act.

These salary restraint measures have contributed to a reduction in OPG’s total cost of MG base salaries since 2010 and, as noted in Section 9 (Benchmarking), have reduced management salaries such that they are now generally at or below the 50th percentile relative to the comparator groups.

5.1 Goals and Operation of the Management Group Compensation Program

OPG’s MG compensation program is designed to ensure that OPG is able to attract, retain, and motivate key talent in a highly specialized and technical industry that is facing increasing competition for resources due to entry by new firms and a shrinking supply of experienced personnel due to demographics. Specifically, the objectives of OPG’s MG compensation program include:

- Attract, motivate and retain talent to enable the company to meet its operational and financial performance objectives.
- Motivate employees by creating a pay-for-performance environment that rewards strong performance and drives desired behaviours while ensuring that business-related risks are managed.
- Provide an appropriate level of compensation relative to its talent market by ensuring alignment with strategic business objectives, and a balance of fixed and variable compensation.
- Meet Government direction related to compensation.
While the salary restraint measures mentioned in section 5.0 have helped to reduce MG wage costs, they have created challenges to the fundamental objectives of the MG compensation program listed above:

- Significant salary compression exists across OPG with 161 managers currently earning less than one or more of the staff they supervise.
- Salary levels for MG staff in administrative and clerical positions are moving below comparable positions held by OPG's represented staff.
- The prospect of a long term salary freeze is a concern for represented staff when recruiting qualified internal personnel into MG positions.

The OPG Board of Directors approves changes to the MG compensation program and monitors MG compensation on an ongoing basis through its Compensation and Human Resources Committee (“CHRC”). The CHRC consists of four independent Board members plus the Board Chair and OPG’s CEO. The current CHRC members are seasoned former CEOs and senior executives of large, complex, multi-national corporations including international nuclear and other energy companies, each of whom possesses considerable financial and human resources experience. The CHRC is responsible for overseeing all significant compensation matters including:

- Reviewing compensation structures, decisions and payouts (base salary, short-term incentive, etc.), and ensuring the link between pay and performance.
- Annually reviewing and approving changes, as appropriate, to OPG compensation, including compensation principles and objectives for total compensation, desired competitive positioning and comparator groups.
- Ensuring that performance measures in the Corporate Balanced Scorecard appropriately reflect the corporation’s approach to risk management.
- Ensuring that executive compensation levels and performance targets are consistent with the Board’s compensation philosophy and are aligned with and designed to achieve OPG’s strategic and operating objectives.
• Overseeing senior executive pay, including total compensation, and individual contract provisions in senior executive employment offers and severance agreements.

The CHRC establishes salary band ranges for all MG staff including executives. The President and CEO does not participate in CHRC decisions that could impact his compensation. When reviewing executive salaries (and incentives and benefits), the CHRC uses external compensation advisors to provide information on market-based executive compensation.

5.2 Management Group Annual Incentive Plan (“AIP”)  
OPG has an Annual Incentive Plan (AIP) for MG employees. The intent of the AIP is to deliver a portion of compensation on a pay at-risk basis, if key financial and operational objectives of the corporation, business unit and individual are met. The AIP program design provides line of sight to corporate objectives and provides control over program costs. Corporate objectives must be met in order for the AIP to payout because in the event that corporate objectives are not met, the AIP is not funded. The AIP envelope for a given year is capped based on corporate performance. In accordance with Bill 55, the AIP envelop is further constrained to ensure the total performance pay envelope is capped at the envelope awarded for 2011 performance (paid in 2012). Corporate, business unit and individual scorecards are established at the beginning of the year, outlining the expectations for performance. The Corporate Scorecard is reviewed by the CHRC and approved by the OPG Board of Directors. There have been no changes to the current AIP Plan design since January 2010. Performance incentives costs are presented in Ex. F4-4-1.

6.0 PENSION AND BENEFITS  
OPG’s pension and benefit programs consist of a registered pension plan (“RPP”), a supplementary pension plan, health, dental, life insurance and other benefits for current employees and their dependants, and other post employment benefits (“OPEB”). OPEB include post retirement benefits, such as group life insurance and health and dental care for
pensioners and their dependants, as well as long-term disability plan ("LTD") benefits for current employees.\(^6\)

The collective agreements with the PWU and Society contain pension and benefits clauses. Pension and benefits levels for Management Group employees are determined by OPG’s Board of Directors.

6.1 Pension
The RPP is funded by member and OPG contributions. Independent actuarial valuations are required to be performed periodically to determine the funded status of the RPP and contributions that are required to fund any deficit. As required by the Pension Benefits Act (Ontario), the valuations are filed with the Financial Services Commission of Ontario ("FSCO"), and deficits are funded over a period of time (5 - 15 years depending on the nature of the deficit). The most recently filed actuarial valuation was as at January 1, 2011 and showed that the pension fund was in a deficit position. This valuation was previously filed with the OEB in EB-2012-0002.\(^7\) The next actuarial valuation for funding purposes will be completed in 2014 and must be filed with the FSCO by September 30, 2014.\(^8\) There have been no significant changes to the pension plans since EB-2010-0008.

6.2 Benefits
All regular employees and pensioners at OPG can receive health, dental and life insurance benefits. OPG has been taking steps to both monitor and control benefits and has implemented a number of changes to stabilize costs and to better align benefit provisions with those of the external market. Changes for the employees represented by the Society and the PWU are achieved only through the collective bargaining process and are, therefore, tied to the timelines of the agreements.

\(^6\) The term “other post retirement benefits” refers to post employment benefit plans other than the RPP and LTD benefits.
\(^7\) EB-2002-0002, Ex. H2-1-3, Attachment 3
\(^8\) The supplementary pension plan is not funded but is secured by letters of credit.
OPG outsources claims administration to Great-West Life and has a number of plan management and adjudication mechanisms in place to control benefit costs. These include the mandatory substitution of generic drugs, maximizing coordination of benefit opportunities, and a requirement for prior approval for certain drug and treatment therapies.

Other cost containment initiatives include:

- Implementation of the 55 and 10 rule for Society represented and Management Group employees:
  - Removes the ability to retire with less than 10 years of service and receive post retirement benefits for life. Provides for lifetime benefits only if, at age 55, the employee has a minimum of 10 years of service with OPG.

- Outsourcing Benefits/Pension Administration
  - OPG was successful at arbitration in obtaining a Purchased Services Agreement (PSA) to outsource some incremental Benefits/Pension administrative duties to existing carriers. This eliminates duplication of effort and allows for reassignment of OPG staff currently performing this work.

- 24 month Health and Dental benefit claim window
  - Requires employees to submit all Health & Dental Benefits claims within a 24 month window of obtaining the service. This lowers administration costs on the adjudication of old claims and is now in place for all employees.

- Millenium Health & Dental Benefits Plan
  - New externally hired MG employees receive Health & Dental Benefits based on the Management Group Millenium Plan. This plan provides lower coverage levels, both in terms of dollar amounts of coverage and in terms of diversity of coverage, compared to the Management Group Heritage Plan for legacy staff.

6.3 Pension and Benefits Costs
OPG is seeking recovery of test period pension and benefits costs associated with the regulated operations determined in accordance with USGAAP. With the exception of the difference in accounting for LTD benefit costs between USGAAP and Canadian GAAP, the nature of the costs and the methodologies used to derive them are unchanged from those presented in EB-2010-0008 and EB-2012-0002. The difference in the accounting treatment for LTD costs is discussed in Ex. A2-1-1, Section 4.0 and was previously discussed in EB-2012-0002, Ex. A3-1-1, Section 4.1.

6.3.1 Accounting Treatment for Pension and Benefit Plans

In accordance with USGAAP, OPG’s pension and other post retirement benefit costs for the current year are based on the measurement of benefit obligations and RPP fund assets at the end of the previous year. The full impact of certain events arising during a year is not charged to pension and OPEB costs for that year, rather certain amounts are accumulated and amortized over future periods.

In accordance with USGAAP, OPG’s LTD costs for the current year are based on the measurement of the benefit obligation at the end of both the current and the previous year. The full impact of events arising during a year related to LTD benefits is charged to OPEB costs for that year.

The obligations for pension and other post retirement benefits continue to be determined using the projected benefit method pro-rated on service. Under this method, an equal portion of the total estimated future benefit is attributed to each year of service until the date the plan participant would be entitled to the full benefit. The obligation at a particular date is the actuarial present value of the benefits attributed to the service rendered up to that date.

The LTD obligation continues to be determined using the projected benefit method on a terminal basis. Under this method, the total estimated future benefit is attributed to the year of service in which a disability actually occurs.
OPG’s pension and OPEB costs and obligations continue to be determined annually by an independent actuary using management’s best estimate assumptions, both economic (e.g., inflation, salary escalation and health care cost trends) and demographic (e.g., mortality rates, termination rates and retirement rates). In accordance with USGAAP, the discount rates used in determining benefit obligations and costs for pension and OPEB continue to be based on AA corporate bond yields in Canada for the appropriate duration of the benefit obligation. Discount rates are discussed further in Sections 6.3.4 below.

For purposes of determining pension costs, RPP fund assets continue to be valued using a market-related value of assets. The market-related value used in determining OPG’s pension costs recognizes gains and losses on equity assets relative to a six per cent assumed real return over a five-year period. This contributes to the smoothing of impacts from equity market volatility over time.

Pension and OPEB costs are made up of a number of components, including current service costs, interest costs on the obligations at the appropriate discount rate, the expected return on RPP fund assets using an estimated long-term rate of return, amounts for past service costs arising from plan amendments, and amounts for actuarial gains or losses. Actuarial gains and losses consist of experience gains and losses, which arise because actual experience differs from that assumed (e.g., investment experience different than expected or higher inflation), and adjustments for changes in assumptions (e.g., discount rates or mortality assumptions).

Actuarial gains and losses for pension and other post retirement benefits are generally amortized over future periods. In accordance with USGAAP, OPG amortizes the net cumulative unamortized gain or loss for each of these plans in excess of 10 per cent of the greater of the benefit obligation and the market-related value of the plan assets over the expected average remaining service life of the employees. This is known as the “corridor approach.” Past service costs for pension and other post retirement benefits continue to be amortized over the expected average remaining service period to full eligibility of the affected employee groups.
As a result of the use of a market-related asset value and the corridor approach, and the amortization of actuarial gains and losses and past service costs, certain components of the actuarial gains and losses and past service costs are not fully charged to pension and other post retirement benefits costs in the year they arise. However, in accordance with USGAAP, all actuarial gains and losses and past service costs related to LTD benefits are recognized in the year they arise.

Costs associated with plans that provide benefits to OPG’s employees during their employment, such as health and dental coverage, continue to be recorded on the basis of actual benefit payments made by OPG to, or on behalf of, the employees as required by USGAAP.

6.3.2 Forecasting and Assumptions for Pension and OPEB Costs
Forecasting pension and OPEB costs requires estimating the values of the benefit obligations and pension fund assets at the end of the year, for which actual results are not known, that precedes the forecast year. Developing these estimates requires making projections of the actual pension fund performance and the assumptions that will be used to determine the obligations. Forecasting LTD costs also requires estimating the value of the obligation at the end of the last year in the forecast period.

The costs for 2013-2015 reflected in this application were determined using the actual December 31, 2012 values of the benefit obligations and pension fund assets and the final assumptions as at December 31, 2012. The determination of 2014 and 2015 costs reflected projections of benefit obligations and pension fund assets at the end of 2013 and 2014 using these assumptions. OPG’s total projected pension and OPEB costs for 2013-2015 were calculated by an independent actuary, Aon Hewitt, as shown in Attachment 2.

As the final assumptions as at December 31, 2012 were used to project the 2013-2015 costs, except LTD costs, the 2013 pension and OPEB costs are expected to be close to the actual costs for the year, absent any significant unexpected changes in legislation or OPG’s
operations. The 2013 LTD cost projections are less definitive because these costs are calculated using information as of year-end 2013.

For the purpose of projecting pension and OPEB costs, OPG may adjust discount rate assumptions from those provided by its independent actuary by a maximum of 25 basis points. This type of adjustment can occur when bond yields are not indicative of historical trends or are volatile. OPG made no adjustment to the December 31, 2012 discount rates provided by the independent actuary in projecting 2014 and 2015 costs. OPG does not adjust discount rates in determining actual costs.

The long-term inflation assumption used for projecting pension and OPEB costs continues to be based on the Ontario consumer price index. OPG uses the final year in the most recent forecast from an economic report, subject to an adjustment if the rate is outside of the Bank of Canada’s target range for inflation. The salary schedule escalation rate assumption used to project the 2013-2015 pension and OPEB costs is equal to the long term inflation assumption plus 0.5 per cent. As in the past, OPG’s independent actuary has reviewed and agreed with these assumptions.

The expected long-term rate of return on the pension fund continues to be calculated by an independent actuary. The rate is based on the current and expected asset mix and the expected return, considering long-term historical risks and returns associated with each asset class within the fund portfolio and the impact of active fund management.

Chart 1 below presents the assumptions used to determine OPG’s 2010-2012 actual and 2013-2015 projected pension and OPEB costs. The assumptions for 2011-2013 (as well as those used for 2011 and 2012 OEB-approved costs) were previously presented in EB-2012-0002, Ex. H1-1-2, Chart 6.¹

¹ As LTD costs are established in accordance with USGAAP using discount rates determined at the end of the year and in accordance with Canadian GAAP using discount rates determined at the beginning of the year, assumptions for the LTD discount rates differ from those presented in EB-2012-0002.
Chart 1

<table>
<thead>
<tr>
<th>Pension and OPEB Cost Assumptions</th>
<th>2010 Actual</th>
<th>2011 Actual</th>
<th>2012 Actual</th>
<th>2013 Projection(^{10})</th>
<th>2014 Plan(^{10})</th>
<th>2015 Plan(^{10})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discount rate for pension</td>
<td>6.80% per annum</td>
<td>5.80% per annum</td>
<td>5.10% per annum</td>
<td>4.30% per annum</td>
<td>4.30% per annum</td>
<td>4.30% per annum</td>
</tr>
<tr>
<td>Discount rate for other post retirement benefits</td>
<td>6.90% per annum</td>
<td>5.80% per annum</td>
<td>5.20% per annum</td>
<td>4.40% per annum</td>
<td>4.40% per annum</td>
<td>4.40% per annum</td>
</tr>
<tr>
<td>Discount rate for long-term disability(^{11})</td>
<td>5.40% per annum</td>
<td>4.00% per annum</td>
<td>3.50% per annum</td>
<td>3.50% per annum</td>
<td>3.50% per annum</td>
<td>3.50% per annum</td>
</tr>
<tr>
<td>Expected long-term rate of return on pension fund assets</td>
<td>7.0% per annum</td>
<td>6.5% per annum</td>
<td>6.5% per annum</td>
<td>6.25% per annum</td>
<td>6.25% per annum</td>
<td>6.25% per annum</td>
</tr>
<tr>
<td>Inflation rate</td>
<td>2.0% per annum</td>
<td>2.0% per annum</td>
<td>2.0% per annum</td>
<td>2.0% per annum</td>
<td>2.0% per annum</td>
<td>2.0% per annum</td>
</tr>
<tr>
<td>Salary schedule escalation rate</td>
<td>3.0% per annum</td>
<td>3.0% per annum</td>
<td>3.0% per annum</td>
<td>2.5% per annum</td>
<td>2.5% per annum</td>
<td>2.5% per annum</td>
</tr>
<tr>
<td>Rate of return used to project year-end pension fund asset values</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>6.25% per annum in 2013</td>
<td>6.25% per annum in 2013 and 2014</td>
</tr>
</tbody>
</table>

Projections of rates of return to determine year-end pension fund asset values are not required for the calculation of the 2010-2013 costs because the actual prior year-end asset values are known. The actual returns on pension fund assets were 12.2 per cent in 2010, 6.9

\(^{10}\) The assumptions for 2013-2015 can also be found at pages 4-5 of Aon Hewitt’s report in Attachment 2.

\(^{11}\) As the costs for 2010 are presented under Canadian GAAP, the discount rate assumption used to determine LTD costs for 2010 represents the rate as at December 31, 2009. In accordance with USGAAP, the discount rates for 2011-2015 are actual (2011-2012) or projected (2013-2015) rates at December 31 of those years.
per cent in 2011, and 9.4 per cent in 2012. Up to end of August 2013, the return on pension fund assets was 1.7 per cent.

6.3.3 Use of AA Corporate Bond Yields in Determining Discount Rates

The discount rates used in determining OPG’s actual and forecast benefit obligations and costs for pension and OPEB are based on AA corporate bond yields for durations similar to those of the obligations. The payment amounts established for OPG in EB-2007-0905 and EB-2010-0008, as well as the December 31, 2012 balances in the Pension and OPEB Cost Variance Account and Impact for USGAAP Deferral Account approved in EB-2012-0002, reflected pension and OPEB costs determined using such discount rates. These discount rates are also used in determining pension and OPEB costs for the purposes of OPG’s audited consolidated financial statements (e.g., Ex. A2-1-1, Attachment 1) as well as the audited financial statements for OPG’s prescribed facilities (e.g., Ex. A2-1-1, Attachment 2, which will be filed when available).

In the EB-2010-0008 Decision with Reasons (p. 96), the OEB directed OPG “to provide a fuller range and discussion of alternatives to the use of AA bond yields to forecast discount rates in its next application.” The discussion that follows responds to this direction and demonstrates that:

- USGAAP requires the use of high quality corporate bonds that are rated AA or higher in calculating the discount rate, and OPG’s auditors concur with this view;
- OPG’s approach for determining the AA corporate bond yields is consistent with the framework put forward by the Canadian Institute of Actuaries (“CIA”); and
- OPG’s auditors and actuaries have accepted OPG’s approach for determining the AA corporate bond yields.

Based on these factors, as discussed below, OPG has concluded that there are no viable alternatives to the use of AA corporate bond yields in determining discount rates.

6.3.3.1 USGAAP Requires the Use of AA Bonds
In accordance with USGAAP, OPG is required to select discount rates by reference to market yields on “high-quality fixed-income investments.”\(^{12}\) USGAAP further specifies that “fixed income debt securities that receive one of the two highest ratings given by a recognized ratings agency be considered high quality (for example, a fixed-income security that receives a rating of Aa or higher from Moody’s Investors Service, Inc.).”\(^{13}\) In Canada, the Employee Future Benefits Implementation Guide issued by the Canadian Institute of Chartered Accountants (“CICA”) cites the use of AA bonds by reference to the above USGAAP guidance.\(^{14}\)

OPG’s auditors, Ernst & Young, are of the view that the use of corporate bond yields rated AA or higher is required to be compliant with USGAAP. They also agree that the use of bonds with ratings lower than AA (e.g., A-rated bonds) in determining pension and OPEB obligations and costs would not comply with USGAAP.

International Financial Reporting Standards (“IFRS”) similarly require that discount rates be determined by reference to yields on “high quality corporate bonds.”\(^{15}\) In November 2012, the IFRS Interpretations Committee (“IFRIC”), the official interpretative body of the International Accounting Standards Board, explicitly noted that “the predominant practice has been to consider corporate bonds to be high quality if they receive one of the two highest ratings given by a recognized rating agency (i.e., ‘AAA’ and ‘AA’).”\(^{16}\)

6.3.3.2 OPG’s Approach for Determining, AA Corporate Bond Yields Is Consistent with the CIA Framework

The CIA issued an educational note in September 2011 entitled “Accounting Discount Rate Assumption for Pension and Post-employment Benefit Plans” (the “CIA Note”) (see

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\(^{12}\) United States Financial Accounting Standards Board Accounting Standards Codification Topic 715-30-35 to 43

\(^{13}\) United States Financial Accounting Standards Board Accounting Standards Codification Topic 715-20-S99-1

\(^{14}\) CICA Employee Future Benefits Implementation Guide, Second Edition, para. 41R. The guide was issued in connection with Section 3461, which is now Part V of the CICA Handbook – Accounting. In para. 065, Section 3461 requires the use of “high-quality debt instruments” in determining discount rates.

\(^{15}\) International Accounting Standard 19, Employee Benefits, para. 83

Consistent with the discussion in Section 6.3.3.1, the CIA Note states that:

"it is understood that “high quality” in Canada has generally been interpreted as referring to market yields on corporate bonds rated Aa or higher, as is the practice in most other countries where Accounting Standards [USGAAP or IFRS] also apply."\(^{18}\)

There is a limited population of AA-rated corporate bonds with longer-term maturities denominated in Canadian dollars. As such, historically, the development of discount rates by major independent actuaries in Canada, such as Mercer and Aon Hewitt, involved an extrapolation of AA corporate bond yields at the long end of the yield curve based on a small number of corporate bond issues available in the marketplace ("Historical Approach"). The discount rates presented in OPG’s past applications were developed by its independent actuaries using this approach.

The CIA Note was issued to address the scarcity of AA corporate bonds with longer-term maturities denominated in Canadian dollars. It encourages actuaries to consider long-term AA-rated Canadian provincial bond yields, subject to a spread adjustment, in calculating AA corporate bond yields for terms longer than 10 years.

The CIA Note also suggests a specific approach for calculating the spread between provincial and corporate bonds. Under this approach, the spread adjustment is calculated as: 50 per cent of the difference between the average spread separating AA corporate and AA provincial bonds with terms between 5 to 10 years, and the average spread separating such bonds with terms above 10 years ("CIA Approach"). In presenting this calculation approach, however, the CIA Note acknowledges that deriving the spread adjustment for provincial bonds with longer-term maturities requires judgment and that other approaches could be acceptable with sufficient justification. (Attachment 3, pp. 11 and 13)

\(^{17}\) A supplement to the CIA Note titled “Accounting Discount Rate – Calculating Spread Above Provincial Yields” was subsequently issued in August 2013 and is provided in Attachment 4.

\(^{18}\) The CIA Note observed that while no AAA-rated corporate bonds denominated in Canadian dollars with long maturities currently exist, “an actuary may consider including Aaa-rated corporate bonds as “high quality” bonds in the analysis if they become available.” (p. 4) Thus, while using AAA-rated corporate bond yields is theoretically acceptable; it is not currently a viable alternative. Should such bonds become available, their inclusion in the calculation would be expected to lower discount rates.
In the second half of 2012, Mercer, a leading Canadian actuarial firm, developed the Enhanced Mercer Model to calculate discount rates.\(^{19}\) The Enhanced Mercer Model follows the framework of the CIA Note but uses a different approach for determining the spread between provincial and corporate bonds, and an expanded set of bond issues.\(^{20}\) Attachment 5 is a letter prepared by Mercer that provides a summary description of the Enhanced Mercer Model and a comparison against the CIA Approach.

In 2012, Ernst & Young advised OPG of their position that the Historical Approach for determining discount rates was no longer acceptable under USGAAP. Absent an acceptable alternative approach at that time from OPG’s main independent actuary, Aon Hewitt, OPG reviewed both the CIA Approach and the Enhanced Mercer Model to determine the approach to use for establishing the December 31, 2012 discount rate assumptions.

After reviewing the two approaches, OPG decided to adopt the Enhanced Mercer Model. OPG concluded that the Enhanced Mercer Model produced spreads that were more consistent with market theory. The discount rates produced by the Enhanced Mercer Model as at December 31, 2012 were higher than those under the CIA Approach, resulting in lower pension and OPEB costs.\(^{21}\) The Enhanced Mercer Model is generally expected to produce discount rates that are higher than those under the CIA Approach. Both Aon Hewitt and Ernst & Young accepted the discount rates produced using the Enhanced Mercer Model.\(^{22}\)

6.3.4 Pension and Benefit Cost Distribution

\(^{19}\) This approach is known as the “Enhanced Mercer Model” because it is an enhancement of Mercer’s previous approach, to take into account the guidance of the CIA Note on the use of longer-term provincial bond yields.

\(^{20}\) At p. 2 of Attachment 5, Mercer notes that, as of March 2013, the bond issues used in the CIA Approach and the Enhanced Mercer Model are aligned.

\(^{21}\) The CIA Approach would have produced discount rates of 3.90% for pension, 4.00% for other post retirement benefits and 3.40% for LTD benefits as at December 31, 2012, as compared to the rates of 4.30%, 4.40% and 3.50%, respectively, produced by the Enhanced Mercer Model shown in Chart 8.

\(^{22}\) Other large OEB-regulated companies that report under USGAAP also base their discount rate forecasts on AA corporate bond yields. See EB-2011-0210, Exhibit D1, Tab 3, Page 2, Line 21-22, ADDENDUM (Union Gas); 2012 Annual Consolidated Financial Statements, page 39 (Hydro One); EB-2012-0459, Ex. D1, Tab 16, Schedule 1, Appendix 1, page 5 (Enbridge Gas Distribution). Enbridge, like OPG, proposes calculating the discount rate using the Enhanced Mercer Model.
A portion of OPG’s total pension and OPEB costs continues to be charged directly to the business units as part of standard labour rates. The portion of pension and OPEB costs included in standard labour rates is based on an estimate of the current service cost for pension and OPEB. The remainder of pension and OPEB costs, which includes interest costs on the obligations, the expected return on pension plan assets, amounts for past service costs and actuarial gains and losses, and any current service cost variance from the estimate reflected in the standard labour rates, continues to be recorded as a centrally-held cost (presented in Ex. F4-4-1, Section 3.0).

The centrally-held costs for pension and OPEB are directly assigned and allocated to the regulated business units in proportion to the amount of pension and OPEB costs directly charged to the regulated business units plus the costs assigned and allocated from the support services groups. The same methodology was used in EB-2010-0008 and EB-2012-0002. It has been reviewed by HSG Group, Inc. in the cost allocation study presented in Ex. F5-5-1, as well as by Black & Veatch Corporation Inc. in the cost allocation study filed in EB-2010-0008.

The costs associated with plans that provide benefits to OPG’s employees during their employment continue to be charged to regulated business units largely via standard labour rates with a small portion included in centrally-held costs.

6.3.5 Comparison of Pension and OPEB Costs
Charts 2, 3 and 4 below present pension and OPEB costs attributed to nuclear, previously regulated hydroelectric and newly regulated hydroelectric operations, respectively, for the 2010-2015 period.23 The 2011 and 2012 amounts for the nuclear and previously hydroelectric operations were reflected in the December 31, 2012 balances of the Pension and OPEB Cost Variance Account (on a Canadian GAAP basis) and the Impact for USGAAP Deferral Account approved in EB-2012-0002. Actuarial and audit reports in support of the 2011 and

23 The figures in these Charts differ from those used in Table 1 and Attachment 6 because the amounts here include total pension and OPEB costs (i.e., all components) while Table 1 and Attachment 6 include only the current service cost component of pension and OPEB costs.
2012 costs were filed in EB-2012-0002.\textsuperscript{24} As noted above, OPG is providing in Attachment 2 an independent actuarial report in support of the 2013-2015 costs.

### Chart 2

<table>
<thead>
<tr>
<th>Pension and OPEB Costs – Nuclear\textsuperscript{25} ($M)</th>
<th>2010 Actual</th>
<th>2011 Actual</th>
<th>2012 Actual</th>
<th>2013 Projection</th>
<th>2014 Plan</th>
<th>2015 Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pension – Standard Labour Rate Component</td>
<td>113.8</td>
<td>165.8</td>
<td>163.5</td>
<td>229.7</td>
<td>222.4</td>
<td>220.6</td>
</tr>
<tr>
<td>Pension – Centrally Held Component</td>
<td>(21.2)</td>
<td>29.7</td>
<td>110.9</td>
<td>131.5</td>
<td>120.2</td>
<td>110.7</td>
</tr>
<tr>
<td>Total Pension Cost</td>
<td>92.6</td>
<td>195.5</td>
<td>274.4</td>
<td>361.2</td>
<td>342.6</td>
<td>331.3</td>
</tr>
<tr>
<td>OPEB – Standard Labour Rate Component</td>
<td>45.9</td>
<td>62.9</td>
<td>65.6</td>
<td>79.8</td>
<td>76.9</td>
<td>76.0</td>
</tr>
<tr>
<td>OPEB – Centrally Held Component</td>
<td>103.7</td>
<td>139.6</td>
<td>153.1</td>
<td>165.1</td>
<td>172.4</td>
<td>177.7</td>
</tr>
<tr>
<td>Total OPEB Cost</td>
<td>149.6</td>
<td>202.5</td>
<td>218.7</td>
<td>244.9</td>
<td>249.3</td>
<td>253.7</td>
</tr>
</tbody>
</table>

### Chart 3

<table>
<thead>
<tr>
<th>Pension and OPEB Costs - Previously Regulated Hydroelectric\textsuperscript{25} ($M)</th>
<th>2010 Actual</th>
<th>2011 Actual</th>
<th>2012 Actual</th>
<th>2013 Projection</th>
<th>2014 Plan</th>
<th>2015 Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pension – Standard Labour Rate Component</td>
<td>5.3</td>
<td>7.9</td>
<td>8.2</td>
<td>12.4</td>
<td>12.2</td>
<td>12.0</td>
</tr>
<tr>
<td>Pension – Centrally Held Component</td>
<td>(1.0)</td>
<td>1.5</td>
<td>5.6</td>
<td>7.1</td>
<td>6.6</td>
<td>6.0</td>
</tr>
<tr>
<td>Total Pension Cost</td>
<td>4.3</td>
<td>9.4</td>
<td>13.8</td>
<td>19.5</td>
<td>18.8</td>
<td>18.0</td>
</tr>
</tbody>
</table>

\textsuperscript{24} Refer to EB-2012-0002 Ex. H2-1-3, Attachment 2 for an independent actuary’s report on the 2011 costs and EB-2012-0002 Ex. H1-1-2, Attachment 3 for the equivalent report on the 2012 costs. The 2011 report should be read in conjunction with EB-2012-0002 Ex. A3-1-2, Attachment 3, which is an independent actuarial report on OPG’s transition to USGAAP and provides 2011 LTD costs under USGAAP.

\textsuperscript{25} Includes allocations of costs related to support services functions. Supplementary pension plan costs are included in OPEB costs. Amounts for 2010 are presented on the basis of Canadian GAAP. Nuclear pension and OPEB costs include approximately $2M each in 2010 and 2011 and approximately $4M in 2012 related to the costs of the Nuclear Waste Management Organization (“NWMO”), which is consolidated into OPG’s financial statements. OPG does not forecast these costs as they are determined by the NWMO.
Pension and OPEB costs increase significantly over the 2010 to 2013 period. The increase is not due to changes in benefit levels or plan provisions. Instead, the primary driver of the increase over the period is a declining trend in discount rates, as shown in Chart 1. In addition, a decline in the expected rate of return on the pension fund assets as shown in Chart 1 and the expected net growth in the cost components during the period also contribute to the increase in the costs. The expected net growth (change) in the cost components includes impacts of changes in current service costs in the normal course, higher interest costs on a higher benefit obligation due to the passage of time, and expected changes in the pension asset values. The increases in 2011 and 2012 were partly offset by the impact of gains on pension fund assets in 2010 and 2011. The increase in 2013 was offset in part by the impact of changes in staffing levels. In the projection for 2014 and 2015, pension costs decrease reflecting negative expected net growth, primarily due to projected
increases in pension asset values. The projection of OPEB costs increases slightly over the
same period, reflecting expected net growth.

Pension and OPEB costs charged to regulated business units directly via payroll burden
increased in 2011-2012, as compared to 2010, chiefly due to lower discount rates. The costs
charged via payroll burden increase further in 2013 mainly due to lower discount rates, partly
offset by the impact of lower staff levels. The projection for payroll burden pension and OPEB
amounts is relatively stable in 2014 and 2015, as compared to 2013.

The declining trend in discount rates over 2010-2013 reflects the impact of financial market
conditions on long-term bond rates. Decreases in expected rates of return over the same
period reflect lower anticipated returns due to global financial market conditions.

Chart 5 below presents the OEB-approved (2011 and 2012) and budgeted (2010) pension
and OPEB costs, which were determined in accordance with Canadian GAAP.

<table>
<thead>
<tr>
<th></th>
<th>Nuclear</th>
<th>Previously Regulated Hydroelectric</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pension – Burden Component</td>
<td>112.9</td>
<td>117.7</td>
</tr>
<tr>
<td>Pension – Centrally Held Component</td>
<td>(18.8)</td>
<td>(3.7)</td>
</tr>
<tr>
<td>Total Pension Cost</td>
<td>94.1</td>
<td>114.0</td>
</tr>
<tr>
<td>OPEB – Burden Component</td>
<td>45.2</td>
<td>47.5</td>
</tr>
<tr>
<td>OPEB – Centrally Held Component</td>
<td>106.8</td>
<td>111.8</td>
</tr>
</tbody>
</table>

26 Includes allocations of costs related to support services functions. Supplementary pension plan costs are included in OPEB costs.
As discussed in EB-2012-0002, Ex. H2-1-3, Section 3.2, pension costs were higher than the OEB-approved amounts in 2011 and 2012 primarily due to lower discount rates and expected long-term rates of return on pension fund assets than those underpinning the OEB-approved amounts. These impacts were partially offset by higher-than-forecast pension fund asset values at the end of 2010 and 2011. OPEB costs were higher than the OEB-approved amounts for 2011 and 2012 mainly due to lower discount rate assumptions. Both pension and OPEB costs were largely on budget in 2010.

As a result of assumptions and projections required in forecasting pension and OPEB costs, significant variances may occur between the forecast and actual costs. Effective March 1, 2011, differences between the forecast pension and OPEB costs reflected in the approved revenue requirement and such actual costs are recorded in the Pension and OPEB Cost Variance Account. As per the approved terms of the account, projected 2013 additions are calculated using cost amounts determined in accordance with Canadian GAAP, as this is the basis upon which the EB-2010-0008 payment amounts were determined. The Pension and OPEB Cost Variance Account, including projected 2013 additions, is discussed in Ex. H1-1-1, Section 4.6.

### 7.0 SUMMARY OF STAFFING, COMPENSATION AND BENEFITS

In EB-2010-0008, OPG committed to providing staff levels on an FTE basis and overall compensation and benefits information in a format equivalent to Appendix 2K for Electricity Distributors. This information is found in Attachment 6, “FTE, Compensation and Benefit Information for OPG’s Regulated Facilities (‘Appendix 2K’).” The sections that follow provide a summary discussion of this information. Additional detail is found in the Nuclear, hydroelectric and corporate exhibits referenced below.

#### 7.1 Staffing
Including the newly regulated facilities, hydroelectric staffing levels are largely stable between 2010 and 2014, except for a one-year jump in 2011 due to additional hiring in both the Hydroelectric Central Support and Plant Groups in order to provide increased support for projects and maintenance activities (See Ex. F1-2-1, Section 3 and Table 4). By the end of 2015, staffing levels are expected to fall by about two per cent relative to 2014 levels.

Nuclear staff levels began to decline in 2009 reflecting completion of safe storage of Pickering Units 2 and 3, the end of the provision of inspection and maintenance services to Bruce Power, and various cost saving initiatives as explained in Ex.F2-1-1. Through various initiatives from 2010 to 2013, Nuclear regular staff levels continued to decline (See Ex. F2-1-1, Table 3). Going forward, OPG’s 2013-2015 Business Plan set outs further regular staff reductions over the plan period.

Allocated corporate staff level increased substantially in 2012 due to the creation of centre-led organizations as part of Business Transformation (BT) (See Section 8 below and Ex. A4-1-1, Section 3.1.1). From 2013 through 2015, FTE levels decline due to attrition supported by BT initiatives.

7.2 Compensation and Benefits

Hydroelectric compensation and benefits costs increased in 2011 primarily due to increases in pension/OPEB costs and the staffing increases described above and shown in Attachment 6. These costs increase again in 2013 due to changes in labour rates before stabilizing between 2013 and 2015.

Nuclear compensation and benefits costs decline substantially between 2011 and 2012 due to a reduction in Nuclear FTEs as employees moved to centre led organizations under BT and net staff levels declined due to attrition combined with aggressively managing hiring. However, labour cost escalation partially offsets the decrease from FTE reductions. From 2012 to 2015 these costs remain fairly constant as shown in Attachment 6.
Corporate support services compensation costs allocated to the regulated operations tend to fluctuate from 2011-2015. Increases from 2011 to 2012 are the result of creating centre-led organizations whose costs are allocated back to the business units. Allocated costs increase across all segments in 2013 compared to 2012 due to higher pension/OPEB costs. Costs for the Newly Regulated hydroelectric facilities increase in 2014 compared to 2013 due to changes in management estimates of support required for these stations by Business & Administrative Services (BAS) and Finance, as well as, an increase in allocated Pension and OPEB costs. Costs allocated to Nuclear in 2014 decrease due to a change in BAS management’s estimate of the cost to support the Nuclear business. Allocated costs decrease in 2015 compared to 2014 due to cost reduction initiatives in the corporate support services groups.

8.0 BUSINESS TRANSFORMATION

OPG’s BT initiative, discussed in Ex.A4-1-1, will have a substantial impact on staff levels and compensation costs during the test period by implementing initiatives to allow OPG to use attrition to reduce its workforce by 2,000 between 2011 and 2015. The test period figures in this exhibit are based on the successful implementation of BT.

9.0 BENCHMARKING

As discussed above, the collective bargaining agreements between OPG and the PWU and the Society that cover the test period compare favourably to the collective agreements negotiated by OPG’s best comparators - Bruce Power and Ontario Hydro successor companies.

In EB-2010-0008, the Board directed OPG to conduct an independent compensation benchmarking study to be filed with this application. In response to this direction, OPG retained AON Hewitt. A copy of AON Hewitt’s report is attached as Ex. F5-4-1. As discussed there, in determining the appropriate comparator group AON Hewitt focused on organizations: from which OPG recruits; to which OPG loses staff; which operate in the same

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27 This figure represents projected total OPG headcount reductions, not including the impact of hiring for Darlington Refurbishment and New Build. Approximately 1,300 of the 2,000 are attributable to regulated operations.
or similar industry sectors; and, which reflect the complexity and size of OPG. AON Hewitt also considered broader general industry information in the form of its Total Compensation Measurement Survey and the Mercer Benchmark Database.

AON Hewitt makes the following observations on the results of their survey:

- OPG’s PWU Group’s total cash compensation is above the market competitive zone at the 50th percentile
- OPG’s Society Group’s total cash compensation is within the market competitive zone at the 50th percentile
- OPG’s Management Group’s total cash compensation is within the market competitive zone at the 50th percentile
- Based on U.S. survey data, there is evidence that jobs in nuclear organizations in the U.S. are paid a premium over similar jobs in non-nuclear organizations

Aon Hewitt found that the existing data are insufficient to quantify a premium for work in Canadian nuclear organizations. However, OPG believes it is reasonable to assume that such a premium also would apply in Canada, which would tend to drive compensation above the 50th percentile.

10.0 CONCLUSION

OPG’s compensation and benefits are largely the product of its collective agreements. These agreements represent significant constraints on the company’s ability to reduce these costs. Nonetheless, by controlling staffing levels, constraining management compensation and bargaining aggressively, OPG has managed to hold the overall increase in these costs since 2011 to slightly more than 1 percent per year while continuing to retain, and where necessary attract, the staff required to operate the regulated facilities safely and reliably.
LIST OF ATTACHMENTS

Attachment 1 – Report by Professor Richard Chaykowski, entitled “An Assessment of the Industrial Relations Context and Outcomes at OPG”

Attachment 2 – AON Hewitt Report calculating Pension and Benefit costs for 2013-15

Attachment 3 – CIA issued educational note entitled “Accounting Discount Rate Assumption for Pension and Post-employment Benefit Plans” issued in September 2011

Attachment 4 – A supplement to the CIA educational note entitled “Accounting Discount Rate – Calculating Spread Above Provincial Yields” issued in August 2013

Attachment 5 – Letter from Mercer regarding Mercer Model for developing accounting discount rates in Canada.

Attachment 6 – FTE, Compensation and Benefit Information for OPG’s Regulated Facilities (“Appendix 2k”)