# COURT OF APPEAL FOR ONTARIO

Régie de l'énergie
DOSSIER: R-3854-2013
DÉPOSÉE EN AUDIENCE
PAR HQD
Date: 17 DEC. 2013
Pièces n°: NON COTÉE

CITATION: Power Workers' Union (Canadian Union of Public Employees, Local 1000) v. Ontario (Energy Board), 2013 ONCA 359

DATE: 20130604

DOCKET: C55602, C55641 and C55633

Rosenberg, Goudge and Blair JJ.A.

BETWEEN

Power Workers' Union, Canadian Union of Public Employees, Local 1000

Appellants

and

The Ontario Energy Board, and Ontario Power Generation Inc.

Respondents

AND BETWEEN

Ontario Power Generation Inc.

Appellant

and

Ontario Energy Board

Respondent

AND BETWEEN

Society of Energy Professionals

Appellant

and

The Ontario Energy Board and Ontario Power Generation Inc.

Respondents

Richard Stephenson and Emily Lawrence, for the appellant Power Workers' Union

John B. Laskin and Crawford Smith, for the appellant Ontario Power Generation

Paul Cavalluzzo, for the appellant Society of Energy Professionals

Mark Rubenstein, for the intervenor Ontario Education Services Corporation

Robert B. Warren, for the intervenor Consumers Council of Canada

Glen Zacher and Patrick Duffy, for the respondent Ontario Energy Board

Heard: January 29, 2013

On appeal from the order of the Divisional Court (Justice Catherine D. Aitken, Justice Katherine E. Swinton and Justice Alexandra Hoy), dated February 14, 2012.

**By the Court:**

**Introduction**

[1] This is an appeal from the order of the Divisional Court dismissing the appeal from a decision of the respondent Ontario Energy Board (the OEB) in which the OEB reduced by $145,000,000 the revenue requirements sought by the appellant Ontario Power Generation Inc. (OPG) to cover its nuclear compensation costs for 2011 and 2012.

[2] The sole issue is whether the OEB's decision was reasonable or not. The majority of the Divisional Court found that it was.

[3] In dissent, Aitken J. found that it was not. For the reasons that follow, we agree with her. We would therefore allow the appeal.

**Background**

[4] OPG is Ontario's largest electricity generator. Its three nuclear generating stations comprise two-thirds of its generation capacity. The remainder comes from six hydro-electric stations.

[5] OPG employs approximately 10,000 people in its regulated business, about 95

percent of whom are associated with its nuclear generation business.

[6] Some 90 percent of OPG's regulated workplace is unionized. The appellant Power Workers' Union (the PWU) represents approximately two-thirds of the unionized staff. The appellant Society of Energy Professionals (the Society) represents the remainder of its unionized workforce.

[7] The *Ontario Labour Relations Act*, S.O. 1995, c. 1, sched. A, s. 17 compels OPG and its unions to bargain in good faith and make every reasonable effort to reach a collective agreement. Once reached, a collective agreement is legally binding on the parties to it for the duration of its term.

[8] OPG entered into a collective agreement with the PWU for the period April 1, 2009 to March 31, 2012. OPG also has a collective agreement with the Society for the period January 1, 2011 to December 31, 2011. These agreements prescribe the compensation rates for each staff position held by its represented employees. They also provide strict terms regulating the staff levels at OPG's stations. Under these agreements OPG is not free to reduce compensation rates unilaterally. Nor can it reduce staffing levels unilaterally, as it wishes. For example, the PWU collective agreement provides that no employee will be involuntarily laid off during the term of the collective agreement.

[9] Independent of the collective agreements, the Canadian Nuclear Safety Commission has also imposed staffing requirements on OPG to ensure safe and reliable operation of its nuclear stations.

[10] On May 26, 2010, OPG filed an application seeking approval of the rates its customers must pay for its electricity. The rates sought provide the revenue required by OPG to cover its projected costs for operating and maintaining its assets, for making

new investments, and for earning a fair rate on invested capital.

[11] The application was for the period from January 1, 2011 to December 31, 2012. The terms of the two collective agreements cover the same period, save for nine months, in the case of the PWU contract. The application was for a future period, in other words a "forward test period" in the language used by the OEB.

[12] In the application, OPG's single largest projected cost related to the operation, maintenance and administration of its nuclear facilities. By far the biggest share of this was the compensation to OPG's unionized staff in its nuclear operations. That compensation is a product of both compensation rates and staffing levels.

[13] OPG's application was filed under s. 78.1 of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, sched. B ("the Act"). It empowers the OEB to fix the rates that OPG is entitled to charge its customers. Section 78.1(5) requires that those rates be "just and reasonable". In such an application, s. 78.1(6) places the burden of proof on the applicant. As long ago as 1929, the Supreme Court of Canada established that just and unreasonable rates are "rates which, under the circumstances, would be fair to the consumer on the one hand, and which, on the other hand, would secure to the company a fair return for the capital invested". See *Northwestern Utilities Ltd. v. Edmonton (City)*, [1929] S.C.R. 186 at pp. 192-3.

[14] The OEB heard OPG's application over 16 days in the fall of 2010. It issued its decision on March 10, 2011.

[15] At pp. 18 and 19 of that decision, the OEB described two approaches it uses to determining rates that are just and reasonable. In the case of forecast costs that can be managed by the applicant going forward, the OEB can and does have regard to a wide

variety of considerations including current economic conditions, analyses of economic trends and benchmarking data comparing other entities.

[16] On the other hand, when committed costs are at issue, that is costs that cannot be reduced by the applicant in the test period, the OEB undertakes a prudence review. In *Enbridge Gas Distribution Inc. v. Ontario (Energy Board)* (2006), 210 O.A.C. 4 (C.A.), leave to appeal to S.C.C. refused, [2006] S.C.C.A. No. 208, this court accepted that approach and outlined what it entails at p. 5:

> The Board agrees that a review of prudence involves the following:
>
> - Decisions made by the utility's management should generally be presumed to be prudent unless challenged on reasonable grounds.
>
> - To be prudent, a decision must have been reasonable under the circumstances that were known or ought to have been known to the utility at the time the decision was made.
>
> - Hindsight should not be used in determining prudence, although consideration of the outcome of the decision may legitimately be used to overcome the presumption of prudence.
>
> - Prudence must be determined in a retrospective factual inquiry, in that the evidence must be concerned with the time the decision was made and must be based on facts about the elements that could or did enter into the decision at the time.

[17] The OEB summarized these two approaches at p. 19 of its decision in this case:

> The benefit of a forward test period is that the company has the benefit of the Board's decision in advance regarding the recovery of forecast costs. To the extent costs are disallowed, for example, a forward test period provides the company with the opportunity to adjust its plans accordingly. In other words, there is not necessarily any cost borne by shareholders (unless the company decided to continue to spend at the higher level in any event). Somewhat different considerations will come into play when undertaking an after-the-fact prudence review. In the case of an after-the-fact prudence review, if the Board disallows a cost, it is necessarily borne by the shareholder. There is no opportunity for the company to take action to reduce the cost at that point. For this reason, the Board concludes there is a difference between the two types of examination, with the after-the-fact review being a prudence review conducted

in the manner which includes a presumption of prudence.

[18] In the end, the OEB reduced by $145,000,000 the nuclear compensation costs applied for by OPG: $55,000,000 for the 2011 year, and a further $90,000,000 for the 2012 year. The OEB did so because it concluded that OPG's compensation rates and its staffing levels were both too high.

[19] In reaching this conclusion, the OEB relied on information, including staffing and compensation comparison reports, that was not in existence at the time OPG entered into the collective agreements with the PWU and the Society.

[20] The OEB decided that OPG should manage its projected nuclear compensation costs downward over the two years by this total of $145,000,000. OPG should achieve this reduction by reducing the compensation rates it pays to its unionized staff positions sufficiently to move these costs from the 75th to the 50th percentile in the benchmarking study of comparator employees, and by reducing the number of its staff positions.

[21] The OEB treated both compensation rates and staffing levels as forecast costs that OPG could manage downward. Neither was treated as committed costs. Nowhere did the OEB engage in a prudence review. It did not inquire into whether OPG's decision to enter the collective agreements was prudent based on the information that was known or ought to have been known at the time.

[22] The majority of the Divisional Court found that both the OEB's use of hindsight in determining the reasonableness of OPG's nuclear compensation costs as well as its ultimate decision to require a reduction of $145,000,000 were reasonable, and should therefore not be disturbed on appeal. The majority agreed with the OEB that OPG could manage these costs downward within the framework of the collective agreements. The majority of the Divisional Court concluded that a prudence review was not required,

would not permit the OEB to fulfill its statutory objective of promoting cost effectiveness in the generation of electricity, and would not allow the OEB to act as a market proxy.

[23] The dissent, on the other hand, concluded that the collective agreements imposed compensation costs on OPG that are committed costs. Rates proposed to recover these costs should therefore be subject to a prudence review to determine whether they are just and reasonable. The OEB did not undertake such an analysis, but assessed the reasonableness of those costs using information that came into existence after the collective agreements were made. The dissent found the OEB's approach to contravene both the principles of the prudence review and the decision of this court in *Enbridge*.

**Analysis**

[24] As in the Divisional Court, the parties all take the position that the appropriate standard of review is one of reasonableness. We agree.

[25] The issue, therefore, is simply whether the OEB's decision of March 20, 2011, including its reasoning and analysis, was reasonable.

[26] The appellants say that it was not. They all argue that the OEB impermissibly used hindsight in relying on current information that was not available when the collective agreements were made, and in not conducting a prudence review of the nuclear compensation costs proposed by OPG,. The appellants argue that the compensation costs applied for are committed costs because of the collective agreements and that the OEB unreasonably evaluated these costs without a prudence review.

[27] The OEB's position, supported by the two intervenors, is that a prudence review

was not needed because such a review does not apply to forecast compensation costs, and in any event is simply a regulatory tool developed for past capital expenditures. The OEB says that these compensation costs can be managed by OPG regardless of the collective agreements. It argues that it was entitled to rely on current information in finding these compensation costs excessive and that its decision that these costs must be reduced by $145,000,000 over the two years was reasonable.

[28] In resolving the issue in appeal, it is important to reiterate the difference between committed costs and forecast costs, a difference well-known in the regulation of utilities such as OPG and well-described in the decision of the OEB in this very case in the passage quoted above.

[29] When an application is made by a utility for the approval of rates for a timeframe to cover the costs in that time frame, its committed costs are those that it is committed to pay in that time frame. Those costs cannot be managed or reduced by the utility in that time frame, usually because of contractual obligations. When, as in this case, the timeframe of the application stretches into the future, costs that have been contractually incurred to be paid over the timeframe are nonetheless committed even though they have not yet been paid.

[30] The OEB's assessment of the reasonableness of committed costs is by way of a prudence review. The OEB's jurisprudence says as much. Moreover, this approach was sanctioned by this court in *Enbridge*, at para. 8.

[31] A prudence review of committed costs is not confined to capital costs or to costs that have been paid at the date of the application. In *Enbridge*, no one contested that a prudence review was warranted even though the case involved operating costs rather than capital costs, as well as costs that had not yet been paid as of the date of the

application.

[32] Moreover, the rationale behind the prudence review is inconsistent with confining the approach to a certain subset of committed costs. All committed costs must be paid during the time frame under review. The regulator is required to maintain a balance of fairness between the utility and the consumer. It would upset that balance to evaluate the reasonableness of these costs with the benefit of hindsight using current information that had not been available to the utility when it made the commitment to pay them,

[33] Forecast costs, on the other hand, are costs that the utility can alter by managing them during the timeframe under consideration. The regulator is free to assess the reasonableness of these costs using current information. This approach is sensible because the utility may act on that same information if it chooses to alter these costs during the timeframe under consideration.

[34] In this case, the OEB found that OPG's nuclear compensation costs for 2011 and 2012 were forecast costs and, because of current information, must be reduced by $145,000,000 through a reduction in the compensation rates for unionized positions and a reduction in the number of staff positions over these two years. The OEB did so without conducting a prudence review of these costs.

[35] In our view, the compensation costs at issue before the OEB were committed costs. Compensation rates for unionized staff positions are, save for several months for the PWU, fixed for 2011 and 2012 by OPG's collective agreements. OPG is legally bound to pay them. It could not reduce the rates, or compel a re-opening of the agreements. OPG is also constrained by safety requirements. Equally, the number of staff positions is strictly regulated by the collective agreements. OPG could not unilaterally reduce that number, nor could it compel unionized staff to retire.

[36] We would conclude, therefore, that the OEB acted unreasonably in two respects. First, the OEB unreasonably assessed the reasonableness of these committed costs using the hindsight of current information unavailable when the collective agreements were made. Second, the OEB unreasonably failed to conduct a prudence review of these costs. Its resulting decision is therefore also unreasonable.

[37] We say this for two reasons. First, the Board's approach to these committed costs is contrary to the approach required by its own jurisprudence and accepted by this court. Second, it is unreasonable to require that OPG manage costs that, by law, it cannot manage.

[38] Our conclusion does not mean that the OEB is powerless to review the compensation rates for OPG's unionized staff positions or the number of those positions. In a prudence review, the evidence may show that the presumption of prudently incurred costs should be set aside, and that the committed compensation rates and staffing levels were not reasonable; however, the OEB cannot resort to hindsight, and must consider what was known or ought to have been known at the time. A prudence review allows for such an outcome, and permits the OEB both to fulfill its statutory mandate and to serve as a market proxy, while maintaining a fair balance between OPG and its customers.

**Disposition**

[39] As a result, we conclude that the OEB acted unreasonably. The appeal must be allowed and the OEB's decision set aside. OPG's application is remitted to the OEB to be heard in accordance with the principles in these reasons.

[40] The parties have not sought costs. None are ordered.

Released: June 4, 2013 ("S.T.G.")

"M. Rosenberg J.A."

"S.T. Goudge J.A."

"R.A. Blair J.A."