CABINET BRIEFING NOTE AND LRC RECOMMENDATION

Energy
Implementation of Ontario's Fair Hydro Plan

Cabinet (info)	TB/MBC	Cabinet	Announcement	TB/MBC	Cabinet	Introduction
Feb 15, 2017	March 1, 2017	March 1, 2017	March 2, 2017	May 9, 2017	May 10, 2017	May 11, 2017

Summary of Proposal

The proposed legislation contains a variance from Cabinet direction, which is detailed in the ministry's variance memo and within this note.

Context for Decision:

On March 2, 2017, the government announced Ontario's Fair Hydro Plan (OFHP), which would lower bills by 25% for a typical residential consumer, starting in the summer of 2017. Up to 500,000 small businesses and farms would also benefit. These measures include the 8% rebate introduced in January 2017 and builds on previously announced initiatives to deliver broad-based rate relief on electricity bills. OFHP includes some benefits for all consumer classes as well as targeted benefits to those with the greatest need, and includes the following major components:

- Refinancing the Global Adjustment (GA);
- Helping vulnerable electricity consumers;
- Extending the Industrial Conservation Initiative (ICI);
- Improving sector efficiency; and
- Modernizing Ontario's electricity market.

Since March 2, 2017, the Affordability Fund and ICI expansion have been implemented.

This proposal follows Cabinet direction to the Ministry of Energy to take the necessary steps to implement electricity price mitigation initiatives that support OFHP to provide additional rate relief to Ontario electricity ratepayers.

The proposed legislation, the *Fair Hydro Act, 2017*, if enacted, enables approaches to fairly allocate a portion of GA amongst specified current and future electricity rate payers ("Schedule 1- *Ontario Fair Hydro Plan Act, 2017*"), and help the most vulnerable Ontarians through enhancements to electricity support programs through government funding ("Schedule 2- Amendments to the *Ontario Energy Board Act, 1998*"). To fully implement the initiative, the ministry will be seeking future approvals for regulations identified in the proposed bill.

The proposed legislation:

1. Establishes a framework to refinance a portion of the GA costs in order to reduce costs for eligible electricity ratepayers (“specified consumers”) in the near term while recovering these costs over the mid- to long-term:
   - July 1, 2017, to April 30, 2018, reduces, on average, after-tax electricity costs for prescribed typical consumers by 25% (inclusive of the 8% rebate and shifting of support program to be government funded).
   - May 1, 2018, to June 30, 2021, electricity rates will be prescribed by regulation. This regulation making authority would enable the government keep increases in line with the Consumer Price Index (CPI) (see page 17- Fiscal Pressure)
   - July 1, 2021, to April 30, 2047, electricity rates will increase at a pace that ensures recovery of the accumulated debt, interest costs and administrative costs (see page 14- Future Impacts to Electricity Rates). Time period may be extended by regulation.
   - Provides for amendments to the *Electricity Act, 1998* and the *Ontario Energy Board Act, 1998*, to enable Ontario Power Generation (OPG), the Ontario Energy Board (OEB), and the Independent Electricity System Operator (IESO) to address payment, settlement and cost-recovery obligations and to manage the refinanced GA costs. (see page 19- OPG Mechanism).
2. Expands electricity support programs for the most vulnerable consumers and moves program costs from the rate base to the tax base. The bill amends the *Ontario Energy Board Act, 1998* to:
   - Move the recently expanded Ontario Electricity Support Program (OESP) to government funding, allow for the potential transition of the program administration to the Crown or other entity, and to enable information exchange between the Ontario Disability Support Program (ODSP) and Ontario Works (OW) to potentially allow for automatic enrolment procedures to be established;
   - Enable the funding of existing Rural or Remote Rate Protection (RRRP) for prescribed customers to be provided for through provincial revenues, rather than from electricity customers.
   - Enable a broader government funded Distribution Rate Protection (DRP) program (broadened RRRP) which provides additional distribution rate protection to residential customers of prescribed higher cost LDCs by enabling the regulations to prescribe a maximum distribution charge.
   - Enable the provision of a government funded on-reserve First Nations Delivery Credit (FNDC), which would cover 100% of the delivery charge for on-reserve First Nation residential customers.

Terms you need to know

- **Global Adjustment (GA) –** The GA accounts for the difference between generation costs (contracted and rate-regulated) and the wholesale market price in order to recover fixed costs, including capital costs, of putting in place and operating Ontario's generation fleet, as well as the cost of conservation and demand management programs. The GA is instrumental in maintaining a reliable electricity system by ensuring that sufficient generating capacity is available.

- **Local Distribution Companies (LDCs) –** Local electricity utilities, responsible for distributing power from transmission lines to people's homes (e.g., Hydro Ottawa, Toronto Hydro, etc.) LDCs recover their costs through distribution rates. LDCs are licensed to serve a specific geographic area by the Ontario Energy Board (OEB). An LDC must receive Ontario Energy Board approval to charge a distribution rate.
- **Delivery charge –** The costs of getting electricity from generating stations to homes and businesses. Appears as one line on electricity bills, includes three components:
  - Transmission: The costs of moving electricity across high voltage lines from generating stations to the distribution system. This cost is recovered through a variable per unit charge that is approved by the OEB.
  - Distribution: The costs of moving electricity from the transmission system to homes and businesses. Depending on the LDC, distribution costs makes up about 60% to 80% of the Delivery line. This cost is currently recovered through both a variable charge and fixed charge, approved by the OEB. Distribution rates for residential customers are moving to a fully-fixed charge by 2019 for most LDCs. Some LDCs, such as Hydro One and Algoma Power are transitioning over a longer period.
  - Line Loss: The costs to recover electricity that is lost when it is delivered over a power line.
- **Regulated Price Plan (RPP) –** Since April 2005, the Ontario Energy Board (OEB) has administered an electricity price plan that provides stable and predictable electricity pricing, encourages conservation and ensures the price consumers pay for electricity better reflects the price paid to generators. This pricing plan is known as the Regulated Price Plan (RPP). About 5 million residential consumers, small businesses and farms are eligible for the RPP.
- **Customer classification for Hydro One –** Customer service classes are determined by the kind of electricity service as well as by density – how many customers there are in the area and the number of customers per kilometre of line. Lower customer density increases the cost to serve. Residential class R1 customers are considered ‘medium density’ customers and residential class R2 are considered ‘low density customers.’ Hydro One also served urban residential customers, considered “high density” through its UR class. Hydro One also has urban and non-urban general service classes.
- **Ontario Power Generation (OPG) –** A business corporation owned by the Province that owns and operates generation assets, including nuclear and hydro, and generates almost half of Ontario’s electricity.
- **Ontario Energy Board (OEB) –** A Crown Agency that independently regulates Ontario’s electricity and natural gas sectors in the public interest. Implements an open and transparent process to allow for stakeholders to participate in quasi-judicial

proceedings and formal stakeholder consultations.

- **Independent Electricity System Operator (IESO) –** An independent corporation established under the *Electricity Act, 1998* that operates the electricity market in Ontario. Balances the supply of and demand for electricity in Ontario and then directs its flow across the province's transmission lines, including interties with other jurisdictions.
- **Special Purpose Vehicle (SPV)** – **Special Purpose Vehicle (SPV) –** A Special Purpose Vehicle (SPV) sometimes referred to as a Special Purpose Entity (SPE) is an off-balance sheet legal entity created by the sponsor or originator. SPVs can be viewed as a method of isolating the risks of an underlying pool of exposures held by the sponsor and reallocating them to the SPV and often investors. This allows investors access to investment opportunities which would not otherwise exist, and provides a new source of revenue generation for the sponsor.
- **Security Interest –** A security interest is a type of property interest created by agreement or by operation of law over assets to secure the performance of an obligation, usually the payment of a debt. It gives the beneficiary of the security interest certain preferential rights in the disposition of secured assets.

Why does Ontario need these changes? Why now?

Addressing rising electricity prices is among the highest priorities for Ontarians. On March 2, 2017, the Ontario government announced OFHP, and since then, there has been increased media attention and public pressure for the government to bring forward the legislation which would enact the commitments made in the Plan. The government has committed to implement further rate relief measures by the summer 2017. On April 20, 2017, the OEB announced that, starting in May, electricity rates would be 17% lower than would have otherwise been without the 8% rebate (OREC), the anticipated move of OESP costs to government funding, and a portion of the reductions estimated under OFHP based on a comfort letter sent from the Minister of Energy.

What is the expected cost to government?

While the GA refinancing structure is intended to result in no fiscal impact to the province, the total projected cost to the electricity rate base is $24.7B amortized until 2047, or longer as may be prescribed. In 2017-18, the GA refinancing cost is forecast to be $2.5B which would eventually be recovered through the rate base. Enhancing electricity support programs and moving to government funding will cost government $499M in 2017-18.

TABLE 1: Cost Impact ($M)	2017-18	2018-19	2019-20	2020-21
Moving Social Programs to Government-Funded (details provided in the chart below)	499	753	829	892
GA Financing (Assumes funded from the electricity rate base)*	2,500	2,600	3,000	3,500
Cumulative Total	2,933	3,353	3,829	4,392

***Note:** GA Financing includes equity injection from the province to OPG. $1.1B investment operating asset in 2017-18 (Ministry has received appropriations)

The GA refinancing portion of the bill establishes a structure in which the IESO records the GA cost recovery deferral as a regulatory asset (regulated by the OEB). The IESO may then sell the regulatory asset, at which time it becomes an investment asset. The investment asset owner (OPG Trust/Special Purpose Vehicle (SPV) or “financing entities”) may then further sell or securitize all or part of the investment asset to other parties in exchange for a funding obligation. Under this structure, OPG, acting as the “Financial Services Manager,” would therefore take on the risk and responsibility of financing the deferral by purchasing monthly regulatory assets from IESO. OPG would finance these purchases through a combination of an equity investment by the Province flowed through the OFA ($1.1 B in 2017-18; see Table 1) and external private sector financing. The structure would increase gross debt of the Province (to finance the equity injection in OPG), increase net investment in OPG (so no net debt impact), increase interest on debt related to that external debt, and increase earnings of OPG to offset the increase in interest costs. The Province’s net debt will remain unchanged as the equity investment in OPG will offset the additional Provincial borrowing. This is expected to be fiscally neutral to the Province.

The estimate for the combined impact of the support programs for the most vulnerable consumers would begin in 2017-18 and is expected to be $499M in 2017-18, growing to $753M in 2018-19 and rising. This investment has been factored into the 2017 Ontario Budget’s fiscal plan. These estimates are based on variable inputs such as program uptake, future energy consumption of various consumer groups and future distribution rates, and are therefore subject to change.

TABLE 2: Fiscal Impact ($M) of Social Programs	2017-18 Budget
Rural or Remote Rate Protection	344
Ontario Electricity Support Program	140
On-Reserve First Nations Delivery Credit	15

Note: As approved in the TB/MBC submission of Mach 1, 2017, and confirmed in Vote-Item 2905-1, the financial impacts of the social programs for the period July 1 2017- March 31, 2018. ENERGY will return updated out-year figures following program implementation

There is inherent risk in the financial estimates given the number of variables that are included in the calculations (e.g. cost of borrowing (projections assume 5%), electricity demand and electricity market conditions and accounting assumptions). Under the mechanism, the government would not have the ability to direct further changes to the rate of repayment for GA refinancing, which would limit the government’s options to address electricity rate concerns in the future (see page 17- Fiscal Pressure).

What are the key steps to deliver this proposal?

- May 11, 2017 - Introduce legislation.
- Spring- Summer 2017- Energy to work with IESO, OEB, OPG, OFA and LDCs on the implementation of OFHP.

- Energy will post a proposal to the regulatory registry in early May outlining proposed new regulations and amendments needed to support implementation.
- Early June 2017 [TBD]- Energy to bring regulations to TB/MBC.
- Early June 2017 [TBD]- Energy to bring regulations to Cabinet/LRC.
- July 1, 2017- the remaining reductions and initiatives associated with the OFHP would take effect. Programs that are not established on this day for technical implementation issues will have benefits that are retroactively applied to customers once program is operational in individual LDCs.

How will the changes be communicated?

On March 2, 2017, the Premier announced OFHP, which would lower electricity bills by 25% for all residential customers including many small businesses and farms. Communications was sustained through minister announcements, local MPP echoes, a radio campaign, and a webpage that features all the programs and initiatives the government is taking to reduce electricity costs.

On May 11, 2017, there will be a news release to announce the introduction of legislation to implement OFHP. Phase two of the marketing campaign will start this summer and will include radio and television.

A robust issues management plan will be developed to mitigate the GA financing risks.

Notes and Recommendation from LRC

LRC item direct to Cabinet.

Cabinet Office Analysis

The proposed legislation allows for the implementation of the key elements of Ontario's Fair Hydro Plan (OFHP) announced on March 2, 2017, to provide further rate relief to Ontario electricity ratepayers. The Global Adjustment (GA) partial refinancing proposal will provide, on average, 25% in electricity rate relief (including the 8% announced in 2016 and shifting of support program costs to the tax base) to "specified consumers" (i.e., residential, farms, small businesses, condominiums, long-term care homes and co-operative housing as prescribed) between July 1, 2017, and April 31, 2018 ("The Fair Adjustment"). Electricity rates would then change by amounts prescribed in the regulations. Regulation making authority would enable the government to keep rate increases in line with Consumer Price Index (CPI) between May 1, 2018, and June 30, 2021 (see page 17- Legal Risks). Additional relief will be provided to Ontarians most in need through enhancements to electricity support programs through government funding.

1. Partial Refinancing of the Global Adjustment:

The proposed legislation establishes the framework to refinance a portion of the current GA costs to future ratepayers by recognizing the longer term benefit many of these generating assets to the electricity system. The methodology is based on the assumption that some assets are expected to continue to provide benefit to future ratepayers beyond the term of current contracts (typically 20 years), and that future ratepayers are expected to continue to be able to utilize and benefit from these assets in the future. Similarly, conservation costs are currently recovered through the GA in the year they occurred while conservation initiatives can provide benefits to the system over many years.

The proposed *Fair Hydro Act, 2017* attempts to balance several key factors including financeability, accounting treatment and legal considerations by:

- Supporting financeability through a number of features, including a provincial undertaking not to interfere with clean energy adjustments once determined, which will be backstopped by a guarantee, and provisions intended to reduce borrowing costs and attract a wide investor base;
- Addressing the necessary accounting requirements through mechanisms to record funding, interest and the transfer of regulatory assets to avoid a fiscal impact to the province; and
- Mitigating legal risk by developing a methodology that attempts to ensure an alignment of costs with benefits to future rate payers.

In order for the clean energy adjustment to be characterized as a regulatory charge, the amount that could be refinanced would need to reflect the true value of the underlying assets being amortized over a longer period of time. According to a legal opinion by former Supreme Court Justice Binnie, there is a moderately high risk that the proposed change would be characterized as an unconstitutional tax rather than a valid regulatory charge because future consumers are being required to subsidize current consumers (see page 16- Legal Risk).

The bill establishes a structure in which the Independent Electricity System Operator (IESO) records the GA cost recovery deferral as a “regulatory asset” (regulated by the Ontario Energy Board (OEB)), supported at its foundation by the fact that the refinancing of the GA is not a reduction in the GA, but rather a deferral to be collected at a future time from “specified consumers” (“the Fair Adjustment” and “IESO deferral”). Specified consumers would receive a reduction in electricity rates from July 1, 2017 to June 30, 2018 as based on a 25% reduction for a prescribed typical residential consumer. IESO may then sell the regulatory asset, at which time it becomes an “investment asset.” The investment asset owner (OPG Trust/Special Purpose Vehicle (SPV) or “financing entities”) may then further sell or securitize all or part of the regulatory asset to other parties in exchange for a funding obligation.

The Minister, following the principles in the bill, would regularly calculate the “Fair Allocation Amount” to ensure a proper match of the allocation of the intergenerational costs and benefits in relation to each on the next 60 six month “reference periods.” The financings will be backed primarily by the clean energy adjustments payable by specified consumers. The clean energy adjustments will track the actual payment obligations incurred by the financing entities when they become due and payable.

OPG, in its role as the Financial Services Manager, will calculate the aggregate clean energy adjustment payable in each month of the reference period, and, to ensure intergenerational fairness, these amounts will be managed to align with the fair allocation amounts determined by the Minister. OEB would calculate the rates at which the clean energy adjustment could be collected from specified consumers. To recoup the costs associated with the fair adjustment, consumers would be invoiced the clean energy adjustment on their electricity bills through existing IESO and Local Distribution Companies' (LDC) processes, which will be channeled through to pay each financing entity's related funding obligations. However, electricity rates are projected to remain lower than would have otherwise been until about 2026-27 (pending the development of the fair allocation amount), and the clean energy benefit will appear on customer's bills once repayment of the accumulated debt begins.

OPG is planning to create a SPV or Trust to finance the partial GA refinancing. To maintain the integrity of the structure, OPG must have the ability to appoint and remove the Trustee (or Board of Trustees) of the SPV/Trust, with no veto right by the Province. No party shall have the ability to remove OPG from its role and authority in the SPV/Trust. The SPV/Trust will be consolidated by OPG, giving OPG the appropriate powers to impact its exposure to variability of the income in the SPV/Trust. OPG will have the ability to direct the financing of the SPV/Trust and both benefit from its financing strategy and be at risk as a result of it.

Once the OPG Trust/SPV has purchased the regulatory asset, which it is under no obligation to do, it will ultimately take on the risk and responsibility of financing the deferral through debt financed from OPG and external sources. OPG's debt would be funded through a combination of an equity investment by the Province through the OFA (see page 4: Table 1) and external financing through sale or securitization of the investment asset. The structure would result in increased gross debt of the Province (to finance the equity injection in OPG), increased interest on debt related to that Provincial debt, increased net investment in OPG (to offset the Provincial borrowing for no net debt impact), and increased earnings of OPG (to offset the interest on debt).

The legislation also provides that no action or omission by the OEB, the Minister, or the Crown is effective to reduce, impair, postpone or terminate the obligations of specified consumers to pay the clean energy adjustment. Additionally, to support the program, the government will be expected to provide certain performance guarantees, indemnities and bond-purchase covenants. The legislation enables these agreements. The terms of these obligations will be worked out over time in connection with the marketing of financings through OPG. The goal will be to achieve the highest rated securities, although that will depend on issues such as the strength of the undertaking not to adversely affect the program through subsequent legislation.

The potential cost to government associated with providing this type of guarantee and the cost of borrowing from private lenders is unknown at this time. It should be noted that the external borrowing by the OPG Trust will be at a higher interest cost than Provincial borrowing costs, which would affect the carrying costs that would need to be recovered from ratepayers in the future (see page 14- Risks and Considerations).

Key elements of this schedule of the bill include:

Specified Consumers

- The defined group of consumers to whom the “Fair Adjustment” applies. Prescribed consumers include residential consumers, farms, small businesses, condominiums, long-term care homes and co-operative housing. These are primarily consumers eligible for the RPP, and aligns with the eligibility under the *Ontario Rebate for Electricity Consumers Act, 2016* (ORECA).

Clean Energy Costs

- Clean energy costs are those costs that arise from the “clean energy initiative” and are allocated to the specified consumers for past, present and expected costs.
- The clean energy costs include estimated amounts to be paid by IESO in adjustments made under section 25.33 of the *Electricity Act*, *1998* (basically, the GA) which relate to contracts for:
    - Renewable energy generation or capacity, conservation and demand management, energy storage, and energy efficiency;
    - Natural gas generation and capacity (excluding certain contracts under section 78.2 of the *Ontario Energy Board Act, 1998* or as prescribed);
    - Payments made under section 78.5 of the *Ontario Energy Board Act, 1998*; and,
    - Other costs as may be prescribed.

Fair Adjustment

- The adjustment to rates to ensure intergenerational fairness.
- July 1, 2017- April 30, 2018- reduction in rates for “specified consumers” based on a 25% reduction for a prescribed typical consumer.
- May 1, 2018- June 30, 2021- the bill allows for rates to be set by regulation (see page 17- Fiscal Pressure).

Fair Allocation Amount

- Principles established in the bill require proper alignment over time between the costs of providing facilities for clean electricity generation and conservation (“clean energy costs”) and the consumers who benefit from these investments.
- The Minister of Energy sets the fair allocation amount, and is required to:
    - Fairly measure and allocate the estimated clean energy costs (and the clean energy benefits) among the “specified consumers” for applicable “reference periods” (typically every 6 months); and,
    - Take into account (in the fair allocation) funding obligations (financing) that have been incurred (see page 16- Legal Risk; page 17- Fiscal Pressure);

  - o Align these costs with clean energy benefits expected to be received by rate payers in the future.
- Subsequent calculations may be undertaken by other agents as prescribed.

Clean Energy Adjustment

- Determined by Financial Services Manager (OPG), the clean energy adjustment is the amount that will be recovered from consumers in the future to pay principal, interest, transaction costs and administrative costs associated with the fair adjustment and consistent with the fair allocation amount.
- Will be subject to true-up process that will reconcile actual amounts collected with expected amounts.
- July 1, 2017- June 30, 2021- OPG to internally capitalize the costs related to the fair adjustment, which will result in increased financing costs during this time.
- July 1, 2021- April 30, 2047- to be invoiced to consumers and collected as part of the electricity bills through existing IESO and LDC processes. Note: it is not certain when the clean energy adjustment will ultimately appear on electricity bills as this will be tied to when repayment of the accumulated debt begins.
- In accordance with the regulations, the OEB to calculate the rate at which specified consumers are invoiced to recover the clean energy adjustment.

Regulatory Asset and Investment Asset

- A regulatory asset is created as IESO defers its right collect a portion of the rates that it would have otherwise received from customers/LDCs if not for the implementation of the Fair Adjustment.
- Subject to OEB approval, IESO records the funding shortfall as a regulatory asset, as IESO would also have collection rights to recover the funding shortfall, which may be sold. Collection rights are deferred until July 1, 2021.
- The Financing Plan contemplates the Financial Services Manager (OPG) establishing financing entities (OPG Trust/SPV) to buy the regulatory asset and the associated rights in exchange for a payment to the IESO. IESO would use the payment to offset the funding shortfall.
- This purchase and sale turns the regulatory asset into an investment asset for the investment asset owner. The transfer includes the rights to collect amounts related to the clean energy adjustment in a manner consistent with the bill.
- The investment interest owner may further sell all or a portion of its rights and interests. An investment interest owner may also grant a security interest over all or a portion of its right, title and interests to secure a funding obligation.
- After 4 years (July 1, 2021) the IESO has the right to collect its funding shortfall from ratepayers in the event that a portion of the regulatory asset is not bought and sold. If the regulatory asset is not sold, the IESO would require an alternative source of financing. IESO has requested a credit facility from the Ontario Financing Authority (OFA) (see page 17- Fiscal Pressure).

- The rights associated with the investment asset require IESO and LDCs to collect money from rate payers as agent of the investment asset owner.

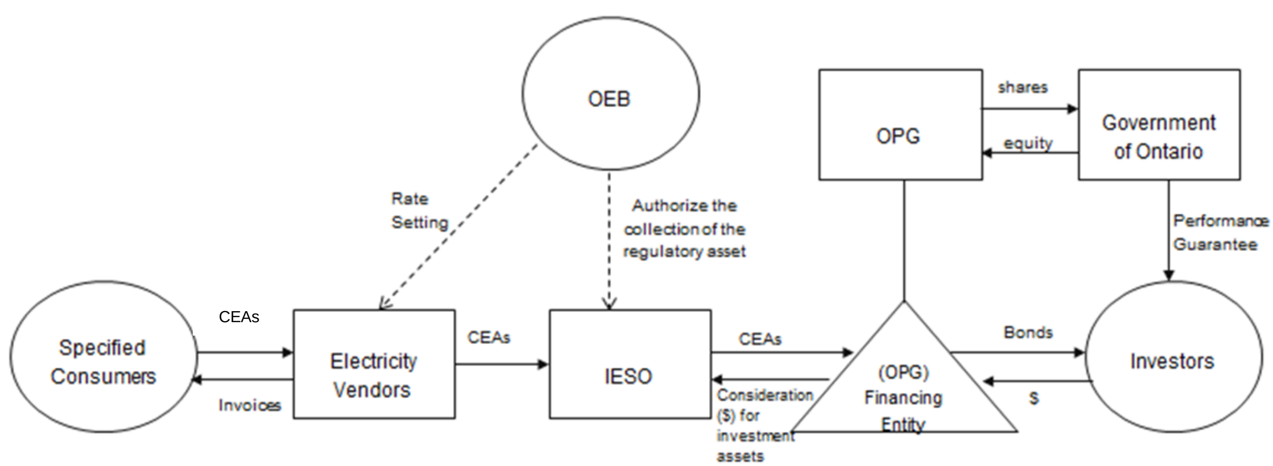
Financing Plan

- In practical terms, the Financing Plan is intended to show how debt (with varying incurrence dates, maturities and interest rates) will be used over time.
- Prepared by the Financial Services Manager (OPG), the Financing Plan is intended to set out when a “funding obligation” (financing) should be incurred so that the (OPG) financing entity can raise money to acquire the “investment interest” from IESO. Plan to be provided to the Minister of Energy.

Crown Undertaking (Guarantee or Backstop)

- The bill provides that no action or omission of the Crown, OEB, or the Minister would be effective to reduce, impair, or postpone or terminate the obligations of specified consumers to pay the clean energy adjustment.
- The Ministers of Energy and Finance together, with LGIC approval, may enter into agreements for compensation with any person in respect of the bill, including regarding the performance of the IESO or electricity vendors under the bill.
- The Ministers of Energy and Finance together, with LGIC approval, may agree to guarantee and indemnify any debts, obligations, securities or undertakings associated with the investment interest.

Figure 1: Financing Structure



Note: CEAs are “clean energy adjustments”.

External Opinions

The proposed structure’s impacts on IESO has been extensively reviewed by KPMG (IESO auditor), and the firm has provided a final draft accounting opinion confirming the validity of the structure under Public Sector Accounting Board (PSAB) standards, which will be updated after the legislation, regulations, and commercial arrangements are complete. KPMG advises that the variance account created by the proposed legislation meets the accounting criteria for the recognition of a “regulatory asset”. The KPMG opinion is highly technical and contains information pertaining to the proposed legislation. While it would be possible to make the opinion public, the ministry is not recommending this approach and is considering alternative options to propose.

If the government intends to keep rate increases to the pace of CPI from May 2018 to July 2021, this may require recourse to the fiscal plan to maintain the constitutionality of the GA refinancing structure.

For clarity, the below requirements were to be met to ensure the structure was defensible, and, based on the opinions received, the ministry is confident that the bill achieves these objectives:

- IESO requirements:
  - IESO can recognize a regulatory asset for the shortfall between the amounts collected from the LDCs and the amounts paid to the PGs using GAAP hierarchy to support regulatory asset under PSAB; IESO can derecognize regulatory asset upon sale to OPG; “Market books” are reflected on corporate books; and, OEB to act as regulator.
- OPG requirements:
  - OPG Trust/SPV purchases regulatory asset from IESO – classifies as intangible asset; OPG consolidates Trust/SPV; and, OPG retains GBE status.

The ministry retained Blakes to provide external legal advice in the development of the legislation. The Blakes team provided securitization, constitutional law, energy sector and government expertise. This team was integral to balancing the accounting, legal and finaceability imperatives, as well as differing interests among OPG, IESO, OEB and investment dealers, in crafting the legislation. Blakes will continue to advise through the development of regulations and the commercial agreements that will ensue.

However, despite the fact that the structure has satisfied the fiscal, and accounting requirements and mitigated to the extent possible the legal risks outlined in the policy submission, there remain some fundamental risks:

- The structure is unique in Canada and possibly the world, which increases the risk or unknown factors impacting its performance. The use of securities mechanisms to address debt is more common in the Unites States, but officials are currently unaware of any example that would compare to the size, complexity or fluidity of the proposal;
- Complexity of the structure and length of deferral/recovery increases risk and decreases transparency;
- Government would have no ability to control electricity prices resulting from these changes outside of recourse to the fiscal plan;
- Government would not know the price of private borrowing that would be required for the OPG Trust to work and will have limited control over OPG’s direct operations as the Financial Services Manager; and,
- Private lenders and rating agencies may disagree with the assessment of the size of the Fair Allocation Amount which would increase the risk of the asset and

therefore its saleability. This could in turn, decrease the amount of rate reduction achievable under this mechanism.

2. Enhancing Electricity Supports and Shifting Costs to Government Funding:

Moving the Ontario Electricity Support Program (OESP) to Government Funding

The OESP is an income-tested, application based program that lowers electricity costs of the most vulnerable consumers by providing a rebate directly on electricity bills. The program was launched in January 2016 and has had roughly 30% enrolment. Under OFHP the program was recently expanded to increase the existing benefit credit amounts by 50% and provide additional credits to more households. Under the expanded program the basic OESP benefit scale increased from $30-$50 to $35-$75 a month and the enhanced OESP benefit scale would increase from $45-$75 to $52-$113 a month for eligible consumers.

The proposed bill amends the *Ontario Energy Board Act, 1998* to allow for the program to transition from the rate base to the government funding, and allow for the potential transition of the program administration to the Crown or other entity. The cost to the fiscal plan would be $186 million in 2017-18. The bill provides further amendments designed to allow information sharing between the Ontario Works (OW) and the Ontario Disability Support Program (ODSP) and the entity responsible for OESP. The intention is that this information sharing will allow for the automatic enrolment of individuals that are already enrolled under the ODSP or OW, but it is currently unknown to what extent this will significantly impact new enrolment under the program. The ministry is continuing to work with MCSS to increase the uptake of the program and automate enrolment of current social assistance clients. The ministry and OEB are also working with the Canada Revenue Agency (CRA) to eliminate the CRA requirement for “wet signatures” on OESP application forms to streamline the application process.

Enhancing RRRP (Delivery Charge Relief) and Moving to Government Funding

Rural or Remote Rate Protection (RRRP) helps to offset the higher costs to distribute electricity to Ontario residents who live in rural or remote locations all across the Province. Currently, RRRP is a $290M program paid for by the ratepayers. For an average residential customer, the cost of supporting RRRP is roughly $1.58 per month. For other customers, the cost to support the RRRP can range from $65 for a greenhouse to $8,000 for a medium industrial.

The proposed bill amends the *Ontario Energy Board Act, 1998* to enable the funding of existing RRRP for prescribed customers to be provided for through provincial revenues, rather than from electricity customers. The intention is to draft regulations permitted under this section to move the portion of RRRP costs used to support Hydro One R2 customers from rate payers to government funding. This is the majority of the cost associated with RRRP.

The bill would further amend the *Ontario Energy Board Act, 1998* to enable the creation of a government funded distribution rate protection program and the ability to prescribe a maximum distribution charge for prescribed classes of residential customers for certain prescribed high cost distributors. The intention is to draft regulations permitted under this section of the bill to prescribe residential customers of the following LDCs to receive distribution rate protection: Hydro One R1 and R2 rate classes, Algoma Power (excluding reclassified residential customers), Atikokan Hydro, Sioux Lookout Hydro, Lakeland Power – Parry Sound, InnPower, Chapleau PUC, and Northern Ontario Wires.

The OEB would continue its usual rate setting activities for prescribed LDCs, as authorized under the *Ontario Energy Board Act, 1998*, and prescribed LDCs would continue to collect the revenue they are entitled. However, prescribed customers (~800,000 customers) of prescribed LDCs would pay no more than the maximum charge determined by the OEB. The shortfall between the set maximum charge collected from customers and the approved OEB charge would be made up of out provincial funds.

Targeted broadened RRRP consumers would see additional savings on their monthly bill that would vary based on their consumption level. Cost to fiscal plan would be $344 million in 2017/18. If the legislation and required regulations are passed, the program would become active as of a prescribed effective date (planned: July 1, 2017).

<u>On-Reserve First Nations Delivery Credit</u>

First Nation and Political-Territorial Organization leaders have advocated for the need for electricity rate relief for on-reserve customers and the review of delivery charges associated with transmission and distribution within the context of historical grievances related to lands affected by energy developments.

The proposed bill amends the *Ontario Energy Board Act, 1998* to enable the creation of a government funded delivery credit program for on-reserve customers with the details to be prescribed in the regulations. The intention is to enact regulations that would eliminate the delivery charge for all on-reserve First Nation residential customers served by licenced electricity distributors, and eliminate the monthly service charge for customers of licensed distributors that charge a bundled rate.

Eligible recipients would be automatically enrolled in the program. The OEB estimates that, on average, customers would receive a monthly benefit of $85. The program will cost approximately $15M annually and be implemented by the prescribed effective date (planned: July 1, 2017).

RISKS AND CONSIDERATIONS

<u>Future Impacts to Electricity Rates</u>

The impact of proposed legislation to a typical eligible customer's bill in July 2017 is a 25% decrease (combined with the 8% rebate effective January 1, 2017, and shifting of the funding of OESP and RRRP to provincial revenues), followed by an increase in price over time. Between May 2018 and June 2021 electricity rates will be set in accordance with a methodology established by regulation which would enable rate increases to be kept in line with CPI (see page 17 – Legal Risk). Customers that are eligible for the RRRP enhancement, OESP, and the On-reserve First Nations Delivery Credit will see further reductions in their electricity rates by as much as 40-50%.

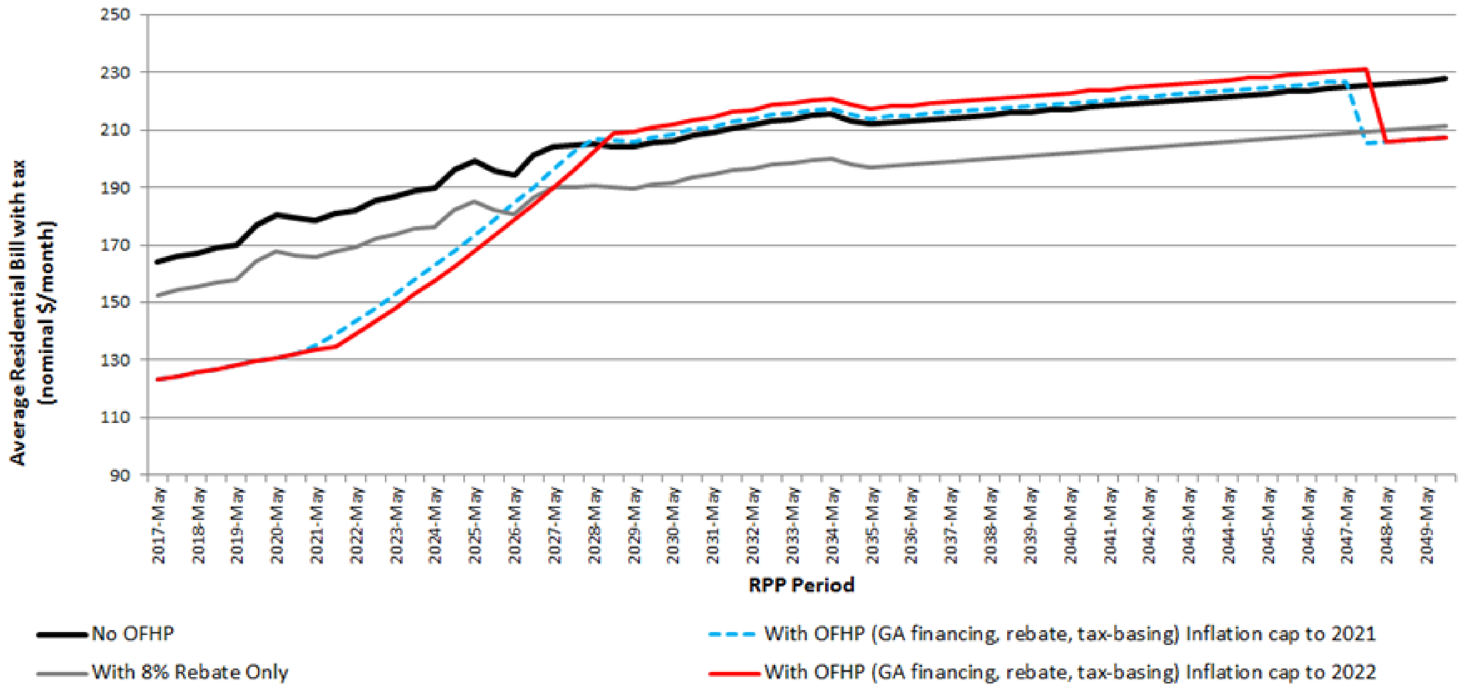
Original policy direction was to keep electricity rate increases in line with CPI until the end of 2021. While the government will have regulatory authority under the bill to establish rates after April 30, 2018, bills are expecting to begin to increase above the rate of inflation as of July 1, 2021 under current forecasts. This constitutes a variance from Cabinet direction. However, the government has publicly committed to 4 years of increases tied to the rate of inflation, which this plan addresses.

Borrowing money to refinance a portion of the GA costs for ratepayers lowers costs in the short term but results in substantial debt and higher electricity prices in the future. Under the plan, electricity prices have been projected to exceed forecast residential monthly bills by about 10% each year from what otherwise would have been from 2028 to 2047 (Note: Values are subject to change). Cabinet policy direction provided that electricity rates increases due to repayments should be capped at around 10% of the total electricity bill during the repayment phase of the plan. To maintain the integrity of the structure, the legislation does not provide a mechanism by which this level of bill increase can be ensured and therefore constitutes a variance from Cabinet direction. However, the debt rating will be impaired if the modelling suggests that rates could increase more than 10%, providing a cap in practical terms. The public may expect that the government is committed to reducing or holding constant the absolute cost of in the longer term and the government would not have the ability to control this portion of rates in the future.

Declining demand levels due to conservation, technology adoption, and self-generation would increase the costs borne by remaining customers to decease the debt associated with GA refinancing. IESO forecasted demand has historically been over-projected which also increases the risk of the static demand assumption. However, the reverse is also true, that if higher levels of electrification are achieved and demand increases, the cost of paying off the debt will be spread over a greater number of consumers. To partly mitigate against the risk that increased self-generation poses, the bill also provides that the clean energy adjustments may not be “set-off.” In other words, it would exist as a separate and distinct component of the bill that could not be reduced by methods such as net-metering.

The current model is based on a static interest rate of 5%. While this assumption is accurate within the current historically low interest rate environment, should interest rates increase above 5%, residential bills would also significantly increase during the repayment phase of the plan. All of these factors increase the risk that the province would have to absorb some of the debt in the future.

Figure 2: GA Smoothing for RPP-Eligible Only



	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	2038	2039	2040	2041	2042	2043	2044	2045	2046	2047	2048
Average monthly bill with OFHP ($/month)	124	126	129	131	137	146	155	165	176	187	199	207	207	209	212	214	216	216	214	215	216	217	219	220	221	222	223	224	225	226	216	206
Year-over-year change (%)	n/a	2.01	2.01	2.01	4.25	6.44	6.44	6.44	6.44	6.44	6.44	3.61	0.08	1.20	1.29	1.14	0.93	-0.04	-0.88	0.49	0.49	0.49	0.49	0.49	0.49	0.49	0.49	0.49	0.49	0.49	-4.37	-4.61
Impact of GA financing and tax-basing ($/month)	-29.9	-30.0	-35.0	-34.4	-28.8	-24.0	-17.8	-14.2	-3.3	3.4	12.2	16.4	16.5	16.7	16.9	17.1	17.2	17.1	17.0	17.1	17.2	17.3	17.4	17.5	17.6	17.6	17.7	17.8	17.9	18.0	-3.9	-4.0
Total accumulated debt ($B)	2.5	5.2	8.2	11.6	14.7	17.5	19.9	22.0	23.5	24.1	24.2	23.7	23.1	22.5	21.8	21.0	20.1	19.2	18.3	17.2	16.1	14.9	13.7	12.3	10.9	9.3	7.7	5.9	4.1	2.1	0.0	0.0
Total change in accumulated debt ($B)	2.5	2.6	3.0	3.5	3.1	2.8	2.4	2.0	1.6	0.6	0.1	-0.5	-0.6	-0.6	-0.7	-0.8	-0.8	-0.9	-1.0	-1.0	-1.1	-1.2	-1.3	-1.4	-1.4	-1.5	-1.6	-1.7	-1.9	-2.0	-2.1	0.0

Notes: Assumes 30 year financing period and a nominal interest rate of 5% (compounded monthly). Ratepayer GA payments increase annually beyond 2020 such that the average monthly residential electricity bill increases by 6.3% per year to a maximum of $2.2 billion above the true cost of GA in any given year to cap repayment charges at around 10% of total bill. IESO forecast is based on IESO's revised OPO forecast as of February 2017. Includes the cancellation of LRP II and EFW, expansion of ICI. Does not include smoothed OPG rates. Above residential bill is based on a 750 kWh per month Toronto Hydro customer. Data shown above is by RPP period. Assumes RPP prices are adjusted in July 2021 instead of May 2021 to coincide with the end of the inflation cap. Fair allocation amounts subject to third party review.

Not all generating assets will continue operations at the end of their contract. If the fair allocation amount is not properly designed, future rate payers will be paying the cost for assets that are no longer in use, which would be unconstitutional, unless legislatively authorised as a tax (see page 16- Legal Risk). High capital costs, equipment obsolescence or surplus capacity / low demand conditions mean that some generators may shut down at the end of their contract. Future ratepayers would be paying for these assets that no longer produce power in paying down the refinanced GA and accumulated interest costs, and it would need to be justified that these assets are still providing some kind of benefit to the system after they cease operation.

Bill Presentment

Over the fall/winter of 2017, the Ministry will be working with LDCs to undertake a comprehensive review of electricity bill presentment regulations.

The ministry expects to prescribe LDCs:

- To include certain basic messaging on electricity bills;
- Starting July 1, 2017, for those eligible, include the On-reserve First Nations Delivery Credit as a line item; and
- Prescribe LDCs to include bill inserts over the next year with OFHP messaging.

With respect to the OFHP, while the 8% rebate is expected to continue to appear on eligible consumer's bills, the further reductions as part of the GA refinancing and moving social programs to government funding will not appear as a specific line item. It is uncertain when customers will begin to be invoiced the clean energy adjustment as a distinct item on their electricity bill. This will commence once repayment of the accumulated debt begins.

Accounting, Provincial Credit Rating and Borrowing

The significant amount of additional provincial borrowing needed to refinance the GA and associated risks and fiscal costs (interest rates, repayment timelines) could put pressure on the Province's credit rating and overall borrowing capacity.

The complexity of the structure and length of deferral (i.e., recovery of debt) increase the overall risk of the proposal and decrease transparency to the public. The structure of the GA refinancing was designed to result in an (1) increase in provincial borrowing (2) no increase in net debt, and (3) no impact on annual surplus/deficit. However, depending on funding to OPG from the Province, an increase in interest on debt and an increase on income from OPG will result. The structure is also contingent on the size of the partial GA refinancing that is seen as possible, which, as mentioned, increases the likelihood of pressures on the fiscal plan in the near future (see page 17- Fiscal Pressure).

In order to provide financing, OPG would develop a special purpose vehicle (SPV) which will use 100% debt financing to purchase the regulatory asset, financing 51% through capital markets as senior debt, with the remaining 49% being provided by OPG as subordinated debt.

- The 49% subordinated debt from OPG will be financed through debt OPG issues in its own capacity, through capital markets (up to 5%) with the remainder (44-49%) financed through equity injections from the Province. This will help to ensure OPG's capital structure remains in line.
- The ministry has received an appropriation for $1.1 billion operating asset to support these injections for the fiscal year 2017/18, and will report back through PRRT for future funding. Based on the final fair allocation amount calculation, the equity injections would be required until the period of recovery begins.
- The injections will be fiscally neutral for the province as they will be offset with the value of shares purchased from OPG.
- To further support the operations and mechanics of the OPG SPV/Trust, additional work will be done through the regulations and supporting agreements /documents. E&Y concurs with OPG's assessment that accounting requirements to support "consolidation" of OPG SPV / Trust with OPG Inc. can be met.

Rating agencies and investors in the Province's debt may view all of the borrowing (whether by the Province directly or the OPG Trust/SPV) as an obligation of the Province. Depending on the magnitude of the debt, the Province's borrowing cost may be impacted. The structure of the guarantees from the Province that will be required by the market at the transaction stage may also impact the accounting analysis. These will be negotiated at a later stage.

OPG will seek to achieve the highest possible credit rating (AAA is possible) in order to reduce borrowing costs and attract a wide investor base. Credit ratings will depend on provisions in legislation, regulation and agreements as well as the capital structure of the SPV/Trust. Despite these factors, rating agencies may see the Province's rating forming a ceiling given the contingent guarantees that the Province will provide.

The Ontario Auditor General (OAG) has been briefed on the proposal and has had access to the March 1, 2017, policy submission for Ontario's Fair Hydro Plan. While the auditors of OPG and IESO have provided assessments and the Office of the Provincial Controller Division (OPCD) has been engaged, the OAG has historically raised concern with "rate regulated accounting" and may take this into account when the provincial books are audited (i.e., it may impact whether the OAG qualifies the provincial books).

Based on early assessments, only a maximum of 18% rate relief can be justified by amortizing contracts over the useful life of the underlying assets. Reducing electricity rates up to or beyond this amount by this method could undermine the nature of the regulatory charge and could only be achieved by relying on increased borrowing.

<u>Legal Risk</u>

The current GA amount paid by consumers is a regulatory charge. One of the requirements of a valid regulatory charge (as opposed to a tax) is that the person paying the charge either benefits from the regulatory scheme or causes the need for regulation. In principle, refinancing the GA to spread the costs of generation and conservation assets over the useful life of the assets presents only a "low" risk of being an unconstitutional tax, as each cohort of consumers pays for a proportion of the GA cost roughly equal to the proportion of the benefit they receive from the useful life of the assets.

Former Supreme Court Justice Binnie has provided legal analysis of this proposal, stating that the amount that could be constitutionally financed as a regulatory charge as opposed to a tax would need to reflect the true value of the underlying assets being amortized over a longer period of time. Shifting too much of the current GA costs to future generations would jeopardize the nature of this being a regulatory charge.

A proposal for refinancing the GA that appears to cross-subsidize near-term consumers at the expense of long-term consumers by back-loading costs more than if costs were spread equally over the estimated lifespan of generation and conservation assets presents a moderately high risk (more likely than not) of constituting a tax. If the government fails to establish that the relevant electricity generating assets and conservation investments will continue to perform economically over the 30 year period, or if the GA charge is in the opinion of the Court disproportionately backend loaded, the GA will not qualify as a regulatory charge and would be characterized as a tax. If characterized as a tax, in the event of a challenge, it would be struck down by a court as unconstitutional and consumers would be entitled to recover their payments. This risk could be eliminated, either up front or retroactively, by the imposition of a valid tax.

The degree of constitutional risk is in direct proportion to the extent the government is not able to show a proper match between the cost of providing facilities for electricity generation and conservation and the group of consumers who benefit year to year from those facilities and investments. By shifting costs to the 20-30 year customers, the government may in reality be disproportionately back-end loading the GA with the effect that the 20-30 year consumers will be subsidizing the 1-20 year consumers. In short, the bigger the reduction in charges to current consumers, the greater the constitutional risk.

Mr. Binnie concluded that the proposed charge faces a moderately high risk of being characterized as an unauthorized tax rather than as valid regulatory charge because (1) there is a disproportionate back-end loading of the charge on 2021-2047 consumers for the benefit of 2017-2021 consumers and (2) because an unknown number of generating assets whose financing costs will be partly recovered from 2021-2047 consumers will not benefit them as they will no longer be in operation.

In addition, the structure of the GA refinancing means that the infrastructure included as part of the clean energy adjustment (i.e. amortized over 30 instead of 20 years) will need to be in service over the entire 30 year amortization period or provide benefits to the system in some way over the whole period. In practice this may mean that the government will have limited ability to alter the generation mixture included under the clean energy adjustments, including natural gas generation facilities, which may at some point be seen as inconsistent with the province’s commitments to reduce greenhouse gasses.

The legislation contains provisions to mitigate the constitutional law risks, including requiring the Minister of Energy to reallocate estimated clean energy costs attributable to each reference period in a way that takes into account the need to align those costs with the estimated clean energy benefits attributable to the same period. Limiting the near-term rate reductions to such amounts which can be justified as counterbalancing disproportionate GA payments during the 2005-2017 period ensures that the statutory 25% reduction is consistent with proportionate reallocation.

The bill also provides for provincial assurances, guarantees and a statutory cause of action. The provincial assurance provision is intended to mirror as closely as possible the language of a similar provision that appears in legislation in the United States that purports to limit a state legislature's ability to enact legislation that would affect the transaction. The main legal risk associated with the provision is that its precise legal purpose and intended effect are not clear. Under Canadian law, it is not possible for legislation to limit the future exercise of legislative power by the Legislature, including the power to amend or repeal statutory provisions or to expropriate private rights conferred under past statutes.

In light of this limitation, the U.S. provision has been modified to focus on possible actions by the executive branch of government that might undermine the value of the proposed securities (including regulation-making), rather than seeking to constrain the Legislature's powers. However, in the absence of some future statutory amendment, it is not clear what, if any, executive action could have the effect of undermining the payment obligation that would be imposed on consumers under the Act and, therefore, it is not clear what practical risk the provision is designed to mitigate against. This uncertainty creates a risk that a reviewing court could construe the provision in unanticipated ways.

The guarantee provisions are intended to backstop the provincial assurance provision and provide that:

- the Minister of Energy and Minister of Finance may, with LGIC approval, enter into agreements regarding the performance of IESO or electricity vendors; and
- the Minister of Energy and Minister of Finance may, pursuant to LGIC order, agree to guarantee and indemnify any debt, obligation, security or undertaking associated with an investment interest.

Legal risk to the province will be assessed as the agreements are negotiated and drafted.

A statutory cause of action may be created by LGIC regulation. Much like the provincial assurance provision, the statutory cause of action provision is intended to mirror features of US legislation. Legal risk to the province will be assessed as the regulation defining the statutory cause of action is developed.

<u>Fiscal Pressure</u>

This proposal aligns with the 2017 Budget's fiscal plan, but involves significant ongoing risks. Parts of the proposal do not include a scheduled review period or an end date, resulting in an ongoing fiscal pressure, which may increase in the out years, and could only be removed by a legislative amendment.

The cost projections are highly sensitive to interest rates and other assumptions:

- The proposal assumes GA refinancing does not have a fiscal impact because the associated legal authority and accounting treatment requirements are met. If the costs of GA refinancing were accounted for as an expense to the fiscal plan, the fiscal impact would be significant ($2.5B in 2017-18, escalating annually).
- The term and timing of the GA refinancing are highly dependent on the IESO's forecast of GA costs and actual interest rates.

The extent of fiscal pressures is also dependent on other factors (i.e., OAG could qualify Ontario's books or issue an adverse opinion). Due to the complexity and size of the proposal, the government has commissioned external opinions on the fiscal and accounting requirements, and external legal advice. IESO auditor, KPMG, has provided a final draft accounting opinion that the principles of the structure are sound, which will be updated after the legislation, regulations and commercial agreements are complete. KPMG advises that the variance account created by the proposed legislation meets the accounting criteria for the recognition of a "regulatory asset." This opinion can be released publicly if desired; however, given that the KPMG opinion is highly technical and contains information pertaining to the proposed legislation, the ministry is not recommending its immediate release and is considering alternative options to propose. In addition, the opinion may not change the likelihood of a contrary opinion by the OAG, but does provide a tool for government to point to in justifying its decisions.

There is also a risk that credit rating agencies and the market may take a view as to the size of the GA refinancing that is possible before becoming unconstitutional. If the fair adjustment and fair allocation amounts exceeds this outlook, it may increase the perceived risk of the investment asset and therefore its financeability/saleability, which would result in reduced market uptake and reduce the amount of near term rate reduction that would be achievable under this mechanism. This may require rate increases greater than the rate of CPI to maintain the integrity of the structure. This is why the increases in electricity rates between May 2018 and June 2021 are to be set by regulation as opposed to legislating that they increase by CPI.

It may not be possible to legally hold the rate reductions to increase by CPI, and if the government wanted to hold to this commitment, the difference would need to come out of the tax base, which has not been forecasted nor included in the fiscal plan. Each percentage point of reduction that the structure cannot provide would need to be addressed by an appropriate alternative mechanism and would result in an approximate $125-150M cost to the government annually.

Further, if IESO is not able to sell the regulatory asset (i.e., the OPG SPV/Trust is unable to get financing to purchase it), then IESO would require financing from an alternative source. IESO has requested a backstop credit facility from the OFA. This would be associated with a fiscal impact risk.

Legislative Officers

The Ontario Auditor General (OAG) has expressed views on rate regulated accounting, which will likely be raised again upon the implementation of this suite of initiatives. The OAG was provided copies of the Cabinet Submission seeking policy approval for

Ontario's Fair Hydro Plan and has been briefed by officials from the Ministry of Energy. The OAG will have opportunities to publicly state her views through the 2017 Public Accounts based on the IESO adoption of regulated accounting in its 2016 financial statements, as well as in the Public Accounts committee in the summer of 2018 and in her pre-election report.

Data and assumptions that underpin the GA refinancing proposal have been submitted to the Financial Accountability Officer (FAO). The FAO is expected to have an opinion on how this proposal may impact the state of the province's finances.

<u>OPG Mechanism</u>

There are several risks associated with the proposed OPG mechanism:

- Accountability:
  - Bill attempts to balance the independence of the OPG Trust/SPV with regulatory oversight and the market's need for certainty in recovering the GA financing;
  - As mentioned, no party will have the ability to remove OPG in its role as the investment asset owner. The mechanism could be criticised for not providing for an appropriate level of accountability to the government or the public, due to the limited amount of government control of the entity, and future rate increases. However, this is seen by the markets as an essential component for the structure to operate.
- New structure:
  - The structure is complex and involves: IESO as originator of the regulated asset and responsible for flow of funds; OEB as regulator of the new mechanism; OPG responsible for financing and managing the mechanism; and Ontario providing ongoing equity capital infusions to OPG and backstop.
  - The addition of financial agency to the current operational obligations of OPG is not the current expertise of OPG. However, OPG has experience managing large financial assets and liabilities through the jointly managed Ontario Nuclear Funds as well as its own pension fund. In addition, this new role could possibly dilute OPG's focus on current high priority responsibilities (i.e., electricity generation and nuclear refurbishment).
  - This financing structure would be unique to Canada – uniqueness reduces likelihood of all risks being known/mitigated. Highly specialized expertise required.
  - There is a risk that at the next opportunity to review the OPG compensation framework, they make the case that there is no national comparator for this aspect of their work and they should therefore receive further exemptions from the rules (OPG nuclear executives do not need to find national comparators for compensation determination).
  - It is unknown what the magnitude of transaction, administrative, and consultant costs that OPG would incur would be. OEB would review OPG's cost as the Financial Services Manager to ensure appropriateness.

- Debt:
  - Opportunity for significant shifting of the Ontario's electricity sector over the lifespan of the repayment (30 years). Through sector/policy/government position shifting, possibility of new entity/structure abandoning debt and Ontario having to take a write down.
  - Risk transfer / portion of debt that Ontario would be responsible for would be the higher risk portion.
  - Repayment plan and impact on rate payers highly dependent on interest rates
- The public could claim that the government is simply putting off a problem and making it worse for future generations. The complexity of the structure may be seen as government attempting to cover up its actions.

Program Design and Implementation

The proposal relies heavily on LDCs as a partner for implementation. Many of these changes will need to take place simultaneously and amongst the 70 LDCs in Ontario there is variety in size, efficiency and ability to implement change.

- Program design will require an evaluation of whether the existing programs are effective and achieving their outcomes (e.g. the OESP has a current uptake of 30% and program changes are proposed in advance of an increased effort to reach 100% uptake)
- The OESP matrix no longer follows the Low Income Measure (LIM) which creates inconsistencies between how programs are applied and may put pressure other provincial programs to increase funding amounts.

Connection to the Province's Next Long-Term Energy Plan

Ontario produces and publishes a Long-Term Energy Plan (LTEP) every three to four years, with the next LTEP scheduled for release in the summer of 2017. LTEP principles that will guide decision-making are affordability, reliability, clean energy, community and Indigenous engagement, and conservation. Through extensive consultation with the public, stakeholders and Indigenous partners through the fall of 2016, the ministry has identified key priorities, and, OFHP combined with new policy or program announcements in the LTEP, will provide the comprehensive future planning perspective for Ontario's energy sector. Note: The legislation associated with GA refinancing establishes a framework for the period after the ratepayer relief is set. By design, to achieve financing requirements there is limited control once the plan is set.

STAKEHOLDER AND PARTNER CONSIDERATIONS

General public (including residential and small businesses) – Likely support a proposal that is projected to provide 25% in average rate relief (including the 8% announced in 2016) and other targeted relief for vulnerable Ontarians, but likely to question the longer term implications. Some individuals and organizations will perceive the GA smoothing as unduly burdening future generations. Ability of the public to understand current and recent changes will heavily depend on government communications. There may be also some criticism that additional fiscal pressure and risk is being taken to benefit some customers that are not in as much need of rate relief as others (i.e., those that own second homes or cottages).

Large Industrial and Commercial Consumers – Will continue to be concerned with the impact of cap and trade on electricity prices and the commitment in the Climate Change Action Plan to use GGRA funds to “keep electricity rate affordable”. Will likely respond positively to the recent changes to expand ICI eligibility to some manufacturing and greenhouse Class B customers, but may be more neutral on the rest of the initiatives.

The impact of cap and trade has been added to electricity bills as of January 2017. Class B consumers have raised concerns about the cost of electricity and its impact on their business competitiveness. Although Class A electricity consumers have access to ICI, they are also concerned about the impact of cap and trade on their electricity costs. They are expecting that GGRA funds will be used to mitigate their costs. There is an expectation government is going to take specific action to mitigate their increases due to cap and trade, and given the initiatives proposed in this submission, there is no plan to provide further relief through the Greenhouse Gas Reduction Account. Funding electricity support programs through government funding rather than the rate base will provide some saving to both Class A and B consumers.

Tenants – Likely to support any future price mitigation measures that directly benefit them; likely to react negatively if no mitigation measures target them.

Northern communities – Likely to support the targeted RRRP delivery relief.

Indigenous communities – First Nation members who live on reserves are likely to support the proposal because of the targeted delivery relief. Other Indigenous communities (i.e., Métis, non-status, First Nations without reserve land bases) are likely to react negatively at being excluded from the delivery charge relief.

eNGOs – May react negatively towards any price relief that is not directly tied to energy conservation. May criticize the inclusion of natural gas electricity generators as part of the clean energy costs.

Solar PV sector – May react negatively to price relief as it can be seen to undercut the economics of net metering.

LDCs – Have expressed the need for an additional tool to provide assistance to their customers who are having difficulty with their electricity bills.

DELIVERY

If passed, the legislation will enable the price mitigation measures to begin to take effect on July 1, 2017. The 2017 LTEP will be released to the public in the summer 2017 and would reinforce/integrate with Ontario’s Fair Hydro Plan. Regulations are required under the major components of the legislation in order to fully implement the initiative and clarify program details.

1. Partial Refinancing of the Global Adjustment:

The ratepayer benefit of the OFHP will be in place as of July 1, 2017. The establishment of the regulatory asset and purchase by OPG is expected to take three to six months to implement following the coming into force of the enabling legislation. The IESO has requested a credit facility from the OFA to provide an interim source of financing.

The bill includes a transition provision in circumstances where for technical or operational reasons invoices cannot be adapted in time for the issuance of the first invoices under the program. In these cases, adaptation of invoices must be implemented by August 1, 2017, followed by a subsequent lump sum credit to the consumer once the invoice is adapted.

2. Enhancing Electricity Supports and Shifting Costs to Government Funding:

OESP Enhancements

Changes to regulation will be required to establish and define the parameters for the proposed changes. The financial flow-through mechanism would likely be modeled after processes used for the ORECA (8% rebate). The amendments made in this bill allow for a transition period where the program continues to draw on the existing IESO variance account. IESO is required to notify the Ministry of Energy when it expects the variance account to be depleted (likely sometime in the fall).

The OEB and utilities implemented the 50% credit increase and added the additional eligibility so that more households could qualify for the program as of May 1, 2017.

RRRP Enhancement

Regulations would be required to establish the details of the program. It is possible that for technical reasons not all LDCs will be able to implement the changes required under the program in time for the prescribed effective date. In this case, the regulation will dictate the eligibility of July 1st and give until October 1, 2017 for LDCs to get their systems in place. The LDCs would provide a lump sum credit to customers that would otherwise have been eligible for benefits under the program starting.

On-Reserve First Nations Delivery Credit

The ministry is consulting with affected LDCs, the OEB, the IESO and Chiefs of Ontario (COO) to help develop a plan to identify eligible on-reserve consumers, as well as identify any potential implementation issues.

It is possible that for technical reasons not all LDCs will be able to implement the changes required under the program in time for the prescribed effective date (planned: July 1, 2017). The bill includes transitional provisions that would ensure customers remain eligible for the delivery credit from the prescribed date. Once available, the rebate would appear on the eligible customer’s electricity bills as a credit for their delivery line.

There is a risk that either non-status Indigenous communities without reserves or Metis could challenge the program on the grounds that it discriminates against them contrary to section 15 of the Charter. This risk is mitigated by the ameliorative purpose of the program and because targeting First Nations communities for a reserve-based program corresponds to the distinct circumstances of reserve-based communities, relative to other Indigenous communities. A genuinely ameliorative program that targets some people but excludes others is shielded from a section 15 challenge if it serves or advances the ameliorative goal.

LINKAGES

Long-Term Energy Plan (LTEP) – Ontario is preparing to release a new LTEP in summer 2017. These plans identify needs for investments over the shorter term, while broadly mapping out the direction of the sector over a 20 year timeframe. The LTEP will balance the principles of affordability, reliability, clean energy, community and Indigenous engagement, as well as conservation and demand management.

Electricity Rate Mitigation Initiatives – The *Ontario Rebate for Electricity for Electricity Consumers Act, 2016*, (ORECA) put in place an 8% rebate for residential, small business customers and farms beginning January 1, 2017.

The Ontario Clean Energy Benefit (OCEB) – Was a five-year legislated program put in place as a broad-based, transitional measure to a cleaner electricity system. OCEB was also put in place following the implementation of the Harmonised Sales Tax (HST). Unlike the previous provincial Retail Sales Tax (RST), the HST (and GST) included electricity in the taxable base. OCEB program ended on December 31, 2015.

Debt Retirement Charge – On January 1, 2016, the government ended the electricity DRC on residential users earlier than planned. For all other consumers the DRC will be removed by April 2018.

Industrial Conservation Initiative (ICI) – Implemented in January 2011 to help large industrial consumers reduce electricity costs by reducing consumption in peak periods. As part of OFHP, ICI eligibility was recently expanded to allow for the participation of the manufacturing and greenhouse sectors with an average month peak demand greater than 500 kilowatts (kW) and less than or equal to 1 megawatt (MW). ICI benefits all consumers by decreasing the need for costly peaking generation over the long term.

Affordability Fund – Approved as part of OFHP, and under development, the Affordability Fund is intended to provide energy efficiency measures to Ontarians who are not eligible for low income conservation programs, and who are otherwise unable to make energy efficiency improvements without financial assistance.

Ontario's Climate Change Action Plan (CCAP) – The CCAP, released in summer 2016, reiterated the 2016 Budget commitment and stated that Ontario intends to invest in initiatives that both reduce greenhouse gas (GHG) emissions and ensure that the net impact of cap and trade would not result in an overall increase in electricity costs for commercial and industrial consumers, and that there would be a modest benefit of up to $2 per month, on average, to residential consumers. This commitment to residential consumers was exceeded by the January 2017 8% rebate.

The commitment to mitigate the cap and trade impact on electricity costs for commercial and industrial consumers (i.e., Class A and B) has not been fully addressed, though the two recent expansions to the ICI provides for significant potential savings. Funding electricity support programs through government funds rather than the rate base will also provide saving to Class A and B consumers.

The CCAP committed to a new Climate Change agency that would act as one window for the delivery of climate change-related programs. The Green Ontario Fund (GreenON) - is tasked to develop programs and services designed to:

- Reduce greenhouse gas emissions from housing from buildings and the production of goods; and,
- Increase uptake and overcome market barriers of low-carbon technologies and processes.

The CCAP committed that the government consult on and develop options to mitigate the impact of carbon pricing and resulting increased utility costs on residential tenants. The mitigation is proposed because tenants do not usually have the opportunity to make changes to their building envelope (e.g. windows, insulation) or major appliances that would allow them to address utility costs themselves. On April 24, 2017, the government introduced the *Rental Fairness Act, 2017* which, if passed, would remove above-guideline rent increases for utilities, to protect tenants from carbon costs and encourage landlords to make their buildings more energy efficient.

Proposed Cabinet Minute

Approval of draft bill for introduction

Cabinet approved version 1-TP of this draft legislation for introduction, subject to the following:

1. The Office of Legislative Counsel is authorized to prepare a French version and to make minor adjustments to the English version, for the purpose of ensuring consistency between the two versions and making other improvements or correcting mistakes discovered in the translation process.

2. ENERGY report back, pending Royal Assent, with regulation and associated regulatory amendments for approval.

3. ENERGY work with Cabinet Office and Premier’s office to develop a communications plan.