Ministry of the Attorney General
Briefing Note
Legal Services Division
Legal Services Branch – ENERGY/MEDG/MRIS/MOI/ADO/SB

ISSUE

Financing interest and costs for the financing entity before Clean Energy Adjustments are payable by electricity consumers ("specified consumers")

FACTUAL BACKGROUND

- In March 2017, the government committed to reduce hydro rates by a total of 25% through a variety of mechanisms and to keep increases to rates equal to inflation for the next four years.
- The *Ontario Fair Hydro Plan Act, 2017* (OFHPA) implements this plan in part (resulting in a reduction of about 17%) by allowing for Global Adjustment costs to be refinanced (GA Refinancing) in the present and paid in the future, recognizing the benefit that future generations will receive from current assets.
- In order to implement GA Refinancing, OPG acting as Financial Services Manager will develop a financing plan and cause financing entities to be created. Financing entities will seek financing from capital markets that will allow them to purchase the "regulatory asset" from the Independent Electricity System Operator (IESO). Upon purchase, financing entities will be investment interest owners.
- While "specified consumers" will eventually be required to pay for the financing obtained by financing entities through "Clean Energy Adjustments", the OFPHA prevents any amounts being charged to rate payers as Clean Energy Adjustments in the short term in order to preserve the government's commitment to lower rates and to keep increases to rates equal to inflation.
- Clean Energy Adjustments are amounts determined by the Financial Services Manager that reflect the financing cost of the GA and the true up amount. The true up amount reconciles actual amounts collected with amounts that are expected to be collected.
- Financing costs include interest and principal, as well as all other costs associated with GA Refinancing such as transaction costs, taxes, etc.
- OPG has advised that the financing entities need a revenue stream to pay for interest and transaction costs immediately.
    - The scope of the costs that must be paid immediately is under discussion. If those costs are limited to interest, the accounting treatment may be different than if those costs include a broader basket of transaction costs.
- OPG and IESO advise that the requirement for an immediate revenue stream directly impacts the accounting treatment for the financing entities and the IESO.

OPTIONS

Funding Rebate

- Under this option, the financing entity would receive from the IESO a funding rebate with the intent that the funding rebate could be used to pay immediate interest and other costs. For example, if the financing entity paid $100 for the regulatory asset, the IESO would rebate $3 to the financing entity.
- OPG has determined that it must record a financial asset, which reflects an obligation of the IESO, rather than an obligation of rate payers (which would be an intangible asset).
- IESO advises that its preliminary analysis suggests that an ongoing commitment to pay the funding rebate becomes a forward commitment of the IESO which then must be booked as a liability and valued in the amount of the total commitment ($1.3B over 4 years).
- If this accounting treatment is correct, then the Province's books will be impacted

>25% Rate Reduction

- OPG has suggested that the OFHPA mechanisms could be used to reduce rates below the approximately 17% currently contemplated (e.g. to 19%), and that this additional financing could be used to pay interest and costs, resulting in no net difference to rate payers.
- The OFHPA and its regulations use a base line bill for a proxy customer and then apply a discount to that base line. Because of this structure, a further reduction to rates would be apparent on the face of the regulation but would not be reflect in the bills of specified consumers.

NEXT STEPS

IESO, OPG and the Province will continue to discuss options to resolve the immediate cash requirement that meets the accounting and other requirements of all parties. IESO is to undertake further accounting analysis. OPG is to model the impact of cash flows on accounting.

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Prepared by: Carolyn Calwell, Legal Director