Topic: OPG and Fair Hydro Plan accounting - OPG

1. OPG and Fair Hydro Plan

<u>Question:</u>
You have a lot of experience working in the electricity sector in other jurisdictions in North America. Could you tell us about whether you've seen this kind of arrangement elsewhere before – in which costs are deferred over a longer period of time than originally planned?

- **Programs similar in concept have been set up in the electricity sector, especially in the US. Several of these programs defer charges of one billion dollars or more.**
- **The most recent transactions that are similarly several billion in size occurred at Duke Energy and Long Island Power**
- **Florida and other states (approximately 18 in total) have passed similar securitization legislation to authorize recoveries by utilities of specified costs, such as hurricane recovery costs, environmental control costs, or costs associated with deregulation of the electricity market**
- **All of these take costs that have been incurred and spread their recovery over several years and decades through financing arrangements similar to the FHP.**

2. OPG and Fair Hydro Plan

<u>Question:</u>
Could you please tell us about what OPG's role is in the administration and ongoing operation of the Fair Hydro Plan?

- **OPG will be acting as the financing manager for the Fair Hydro legislation, basically arranging for a variety of debt financing.**
- **We will be setting up a financing entity (Trust), which is ring fenced from the generation activities of OPG in an effort to reflect the unique nature of this business and not co-mingle the operational activities of the two businesses.**
- **The financing requirements are determined by the legislation and the reduction consumers have on their bills and will be funded through the Trust.**
- **OPG will arrange for the third party debt, and supplement this funding with the Province, and OPG will contribute additional funds through increased**

equity and debt of the OPG operating company that will be leant to the Trust, also at equivalent market rates.

3. OPG and Fair Hydro Plan

Question:
But is it unusual for an organization like yours to take on this responsibility?

Could you please explain why OPG might be the appropriate entity to play this kind of role—do you think you are adding value to the process by acting as the Financial Services Manager?

- **OPG is uniquely positioned as we understand the supply / demand characteristics of the market, we regularly interact with the OEB, IESO and we have experience in Treasury operations in the marketplace including relationships with the credit rating agencies.**
- **OPG has recently successfully project financed hydroelectric investments from public markets and has an ongoing settlement relationship with the IESO.**
- **A simple comparison between direct borrowing by the Province and OPG's role in the Fair Hydro Plan is a bit of an apples to oranges comparison.**
- **A conventional Provincial borrowing program would raise funds based on the credit worthiness of the Province and the Provincial Guarantee.**
- **Under the Fair Hydro Plan, lenders will provide funds based on the underlying value of the specific asset. This value is created by the legislated framework rather than through a Provincial Guarantee.**
- **The Fair Hydro Plan will create a series of deferred assets that will have certain cash-flow payment streams going forward. The overall objective of the Plan is to spread the costs out. The financing has to be actually linked to the overall payment scheme going forward, and aligned with the benefits. Consequently, the financing actually lends itself toward a securitization structure with cash flows matched to specific benefits rather than as a conventional borrowing program**
- **OPG has the expertise and experience to manage a securitization program. The Ontario Financing Authority, does not, as far as I am aware, have direct experience in setting up or managing a securitization vehicle or program.**
- **This combination and diversity of skills position OPG to ensure an effective funding arrangement is put in place that clearly defines the electricity rate payer in context of the person receiving the initial benefit of the legislation.**

4. OPG Accounting and Transparency

Question:
Do you think the structure that's been created to administer and operate the Fair Hydro Plan—and that OPG plays a role in—is a structure that will provide for transparency as it related to the borrowing and the accounting?

- **The structure that has been set up in fact ensures a high level of transparency.**
- **As these deferred amounts are funded through third party financing, the process by design in financial market space requires disclosure and oversight including credit rating agencies, the OEB, external audit of the Trust itself, additional OPG disclosure in its reports, oversight from lenders through Trust indenture documents**
- **Ratepayers and taxpayers will be able to clearly see the financial results of the Trust as it relates to the legislation.**
- **All of this will be reported in OPG's financial reports on a quarterly and annual basis. OPG's financial reports are filed with the Ontario Securities Commission (OSC) and subject to OSC oversight.**

5. OPG Accounting and External Experts

Question:
Could you explain what sort of external expertise you enlisted, and please explain what counsel these experts provided with respect to the structure that has been set up and the accounting that will be used?

- **There are three specific areas that we supplemented our team with external resources.**
  - **First, was legal advice to ensure there is clear alignment between the legislation and the Trust and its related requirements and obligations.**
  - **The second was financing advice directed at the capital markets again to ensure alignment with the markets focused on achieving the most cost effective financing to ensure the rate payer impact is minimized.**
  - **The third was accounting advice directed at the set up and governance of the Trust and then to achieve the transparency in reporting that is critical.**

  As has been mentioned OPG has strong capabilities across these areas but felt it was prudent to ensure that all steps are taken to

establish the Trust and its activities in a clear and transparent manner.

6. OPG and the Fair Hydro Trust

Question:

Can you describe what OPG has been asked to do to minimize the customer impact of implementing the FHP?

- **OPG will act as the Financial Services Manager for the FHP Trust.**
- **There are 2 primary goals of the Financial Services Manager:**
  - **First of these, is to ensure that the activities envisioned under the FHP legislation, as they pertain to the Trust, are consistent with the electricity ratepayer both receiving the bill reduction and the corresponding collection of the costs related to the activities that have been invested in.**
  - **The second is to work on optimizing the FHP Trust financing to ensure that costs to ratepayers are minimized and reflect the benefit the ratepayer initially received.**
- **Speaking to the second point we have been working on a financing program that includes several elements including a securitization program, provincial equity support and OPG funding. These elements are being optimized in a manner that will achieve an effective financing program for the benefit of consumers.**
- **As we have worked through the program attention has been given to achieve a strong credit rating for the Trust again with the objective of mitigating the impact on the ratepayer through effective market pricing by the Trust of the funds being borrowed.**
- **It is also critical to my first point that the financing program have a high level of transparency so ratepayers can understand the nature of the program and the associated costs. The Trust will file all necessary financial reports that will ensure this transparency.**