Ontario

Provincial Guarantee

Briefing for Minister of Energy

DRAFT – Thursday August 24th, 2017

CONFIDENTIAL & COMMERCIALLY SENSITIVE

Background

- The *Ontario Fair Hydro Act, 2017,* enables the IESO to establish a variance account to record the deferral amounts from the difference between collections from current ratepayers and payment obligations to generators and conservation, and to create a regulatory asset to recover the balance in the variance account
  - The IESO can then sell the regulatory asset – the right to recover those deferred amounts from specified consumers in the future
  - OPG, as the Financial Services Manager, is authorized to establish one or more financing entities that may incur funding obligations
  - The Financing Entity will purchase the regulatory asset, effectively financing the shortfall in current rates not received from ratepayers
- To purchase the regulatory asset from the IESO, the Financing Entity must borrow a portion of the funds from capital markets (planned to be 51%, with other financing to come from OPG and, indirectly, the Province)
  - OPG's financial advisors have indicated that without adequate protection against legislative, judicial and organizational risk, the debt would not be financeable or would result in higher financing costs, to be passed on to ratepayers
- OPG has requested that the Province provide a guarantee to the Financing Entity and prospective debt holders such that, under certain circumstances, the Province would step in and assume the funding obligations of the Financing Entity

Provisions Under the Act

- As contemplated under the Act, OPG is requesting a Provincial Guarantee to support the planned Financing Entity's ability to borrow to finance the deferral of global adjustment amounts
- Under s.5(3) of the OFHP Act,
    - *The LGIC may by order,*
        - *Authorize the Minister (of Energy) and the Minister of Finance, acting together on behalf of the Province,*
            - *To agree to guarantee or indemnify any debts, obligations, securities or undertakings associated with an investment interest, and*
            - *To determine terms and conditions of the guarantee or indemnity and the maximum liability for the guarantee or indemnity*
        - *Specify terms and conditions that must be included in any guarantee or indemnity given by the Minister and the Minister of Finance*
        - *Specify a maximum liability for the guarantee or indemnity*

Provincial Guarantee

- Certain events that would negatively impact holders of Fair Hydro Plan debt would activate the Provincial Guarantee, including:
  - Decisions by the Legislative Assembly, i.e., repeal of the *Fair Hydro Plan Act, 2017*, or amendments or new legislation that adversely affect the Financing Entity
  - A court decision that declares any funding obligations of the Financing Entity to be invalid or unenforceable
  - Changes to the organization, structure or operations of IESO adversely impacting the Financing Entity
- In the event the guarantee is triggered, the Province would take over the obligations of the Financing Entity including principal and interest payments on debt issued to date and any outstanding payments to service providers
  - The Province would service the debt and service providers rather than replace the debt with Provincial debt but could replace OPG as the financial services manager
- The guarantee would continue until all guaranteed obligations of the Financing Entity are fully discharged
- The guarantee may need to be revised at a future date, or approval from the Province may be required, if the financing entity must access US market as investors in that market will likely require additional compensation if the guarantee is triggered
- Additional details, including terms and conditions to be specified by the LGIC in an Order-In-Council (OIC), or by the Ministers, need to be settled on, as the approvals process proceeds

Considerations

- If a guarantee is not provided, the Financing Entity would either be unable to raise sufficient financing from capital markets to purchase the regulatory asset from the IESO or the cost of the financing will be potentially materially greater than it otherwise would be
- OPCD will need to review the details of the proposed Provincial Guarantee to be provided for any accounting implications
  - E.g., an unlimited Provincial Guarantee may cause the debt to be treated as Provincial debt
- If a guarantee is provided, the Province takes on a contingent liability
  - The creation of a contingent liability will not currently affect net debt
  - The amount of the liability will increase over the duration of the Fair Hydro Plan
    - The most recent estimate for total debt to be financed by a financing entity would be in the range of $11 billion (assuming a 5% interest rate)
- In the event the guarantee is triggered, the Province's net debt will most likely increase by an amount equal to the contingent liability at that point in time
  - The Province's interest payments will also increase by the debt interest servicing of the debt payment obligations it has assumed under the guarantee

Next Steps

- Continue to work through outstanding issues related to the provincial guarantee
- Finalize draft term sheet, working with OPG / OFA / MOF / Legal / Dealers
- Ministry of Finance to seek necessary approvals from TB / MBC
- Seek LRC / Cabinet approval for OIC
  - The term sheet would inform a proposed OIC
    - Whether to include a maximum liability amount would need to be considered in developing the TB submission and the request for the OIC
- The guarantee agreement would need to be drafted in accordance with the OIC