PROVINCIAL GUARANTEE TO OPG FINANCING ENTITY

1. PROGRAM/BRANCH: Ontario Financing Authority

2. SUMMARY OF REQUEST:

Provide a guarantee or guarantees to one or more OPG Financing Entities established to perform under the Ontario Fair hydro Plan Act and such entity or entities prospective debt holders, that, under certain circumstances, the Province would assume the debt obligations of the Financing Entity.

This submission is to request that Treasury Board:

(a) Approve that the Minister of Finance and Minister of Energy provide a provincial guarantee, as contemplated under the *Ontario Fair Hydro Plan Act*, to one or more OPG Financing Entities under the terms set out in Appendix;

(b) Recommend that Cabinet approve an Order in Council, in accordance with section 5 of the Ontario Fair Hydro Act, that authorizes the Minister and the Minister of Finance, acting together on behalf of the Province,

(i) to agree to guarantee or indemnify any debts, obligations, securities or undertakings associated with an investment interest, and
(ii) 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; and

specify a maximum liability for the guarantee or indemnity.

(c) Note that the ministry of Energy will also be submitting to the Minister of Finance a request for approval, under Section 28 of the Financial Administration Act, contingent liabilities arising from the provision of the guarantee.

3. BACKGROUND:

On March 2, 2017, the government announced its proposed Ontario's Fair Hydro Plan (OFHP), which would lower bills by 25% for a typical residential consumer, starting in the summer of 2017. The OFHP includes the deferral of a portion of the Global Adjustment portion of the cost of electricity. The deferral is built around the principle that the costs incurred to put in place assets for generation and support conservation to move to a clean, reliable system, would last longer than their typical 20-year contract period and would be able to provide benefits for future ratepayers, and that the costs should be spread more fairly.

To this end, immediate rate relief to eligible ratepayers is provided by spreading the cost of electricity investments over a longer period of time. Under forecasts provided by the Ministry of Energy at the time of the OFHP announcement in March, the immediate reduction would be about $2.5 billion per year on average over the first ten years. This estimate is being updated and will be presented to TB/MBC as part of a report-back by the Ministry of Energy.

Under the *Ontario Fair Hydro Plan Act, 2017,* (the Act), which came into effect on June 1, 2017, the IESO is able to create a regulatory asset approximately equal to the difference between collections from current ratepayers and payment obligations to generators and conservation. The Act provides for the IESO to sell the regulatory asset and the right to recover those deferred amounts from specified consumers in the future. Under the Act, a Financing Entity will purchase the regulatory asset, effectively financing the shortfall in current rates not received from the ratepayers.

To purchase the regulatory asset from IESO, the Financing Entity must borrow a portion of the funds (planned to be 51%, with other financing to come from OPG and, indirectly, the Province) from the capital markets; however, OPG's financial advisors have indicated that without adequate protection against legislative, judicial and organizational risk, the debt would not be financeable. OPG is, therefore, requesting that the Government of Ontario 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.

Certain events that would negatively impact holders of Fair Hydro Plan debt would activate the Provincial Guarantee:

- Decisions by the Legislative Assembly, i.e., repeal of the Ontario 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; and

- 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 guarantee would continue until all obligations of the Financing Entity are fully discharged.

5. ADMINISTRATIVE IMPACTS:

To be managed by existing staff.

6. RISKS:

If the guarantee is not approved, the Financing Entity would either be unable to raise sufficient financing from capital markets to purchase the regulatory asset from IESO or the cost of the financing will be potentially materially greater than it otherwise would be.

If the guarantee is approved, the Government of Ontario takes on a contingent liability. The amount of the liability will increase over the duration of the Fair Hydro Plan and peak at an estimated [$24B to $26B (to be revised as Energy re-estimates)] of debt principal, along with associated interest payments.

In the event the guarantee is triggered, the Province's net debt will increase by an amount equal to the contingent liability at that point in time. The Province's interest payments will also increase by an amount equal to the weighted average cost of the debt it has assumed under the guarantee.

While it is difficult to estimate the actual impact to the Province's interest on debt (IOD) expense, the worst case scenario would be the Province assuming the debt at its peak. If so, IOD expense may increase between [$0.8B and $1.3B] per annum, depending on the interest rate at which the Financing entity will be able to borrow at.

It is important to note that, if the guarantee is triggered, and the Province assumes the obligation to service and pay down the debt, that the magnitude of the fiscal impact (IOD expense) will depend on whether or not some portions of the Act continue or not, in some form. If the payment streams from ratepayers in the Clean Energy Adjustment (CEA) continue, this would offset the debt and interest payments; however, if the CEA is ended (e.g., if determined by a court not to be constitutional) and not replaced by another authorized charge, the incremental IOD expense would impact the Government's fiscal plan and likely takes away fiscal resources that can be otherwise used. Also, debt incurred to benefit the ratepayer becomes the responsibility of the taxpayer.

7. RECOMMENDATION

(a) Approve that the Minister of Finance and Minister of Energy provide a provincial guarantee, as contemplated under the *Ontario Fair Hydro Plan Act*, to one or more OPG Financing Entities under the terms set out in Appendix;

(b) Recommend that Cabinet approve an Order in Council, in accordance with section 5 of the Ontario Fair Hydro Act, that authorizes the Minister and the Minister of Finance, acting together on behalf of the Province,

   (i) to agree to guarantee or indemnify any debts, obligations, securities or undertakings associated with an investment interest, and
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(c) Note that the ministry of Energy will also be submitting to the Minister of Finance a request for approval, under Section 28 of the Financial Administration Act, contingent liabilities arising from the provision of the guarantee.

APPENDIX

[Insert Final Term Sheet]