Request for Approval
Pursuant to Section 28 of the *Financial Administration Act* (Ontario)

1. MINISTRY REQUEST

On March 2, 2017, the Premier announced Ontario's Fair Hydro Plan (the "ONFHP"), under which the government proposes to take steps to lower electricity bills on an after-tax basis by 25 per cent for a typical residential customer relative to what those bills would otherwise have been without the ONFHP. This proposed 25 per cent rate relief measure will be inclusive of the 8 per cent rebate that is already in effect under the *Ontario Rebate for Electricity Consumers Act, 2016* and the savings that are anticipated to result from the proposed shifting of the Ontario Electricity Support Program ("OESP") and the Rural or Remote Rate Protection program ("RRRP") costs from ratepayers to provincial revenues. Changes to the Global Adjustment ("GA") are also proposed to be a component of the 25 per cent rate relief under the ONFHP.

On June 1, 2017, Bill 132 received royal assent, which marked the coming into force of the *Ontario Fair Hydro Plan Act, 2017* (the "*Act*"). The *Act* enables the implementation of the ONFHP. The implementation of the ONFHP will require the participation of Ontario Power Generation ("OPG") and the Independent Electricity System Operator ("IESO") among other government entities. Both OPG and the IESO have each requested an indemnity covering their respective corporations, directors, officers and employees in relation to their respective activities in carrying out the implementation of the ONFHP. OPG is also seeking an indemnity for its subsidiaries (not including any financing entities as defined in the *Act*) ("Subsidiaries") and their respective directors, officers and employees.

The Ministry is seeking the approval pursuant to section 28 of the *Financial Administration Act* (Ontario) to provide these indemnities, in the forms attached as Appendix "A" and Appendix "B" (collectively the "Indemnities" and individually the "Indemnity"), on behalf of the Crown to OPG and the IESO, respectively.

Timing:

Approval is sought by June 30, 2017. The Indemnities are required in conjunction with the coming into force of the *Act* (came into force on June 1, 2017).

2. RECOMMENDATION

Approve the giving of the Indemnities to OPG and IESO effective as of the date upon which the Act was passed (June 1, 2017).

3. BACKGROUND

OPG – Role in Implementation of ONFHP and Associated Risks

The *Electricity Act, 1998* ("EA") has been amended to contemplate that OPG's objects include those related to the ONFHP. This amendment was designed to ensure that OPG could participate in the ONFHP. OPG will play a central role in the implementation of the ONFHP, particularly with respect to the implementation of the GA refinancing component of the ONFHP. As part of the ONFHP, it was announced that a portion of the GA will be refinanced in order to fairly allocate costs across present and future generations of electricity consumers with respect to investments made to decarbonize (i.e., phase-out coal) and modernize Ontario's electricity system (i.e., build and maintain a reliable electricity system). This would result in a deferred GA amount that a special purpose entity created by OPG (i.e. a financing entity as defined in the *Act*) is expected to finance.

In carrying out this role, OPG will be carrying out activities that fall outside of its typical business activities and corporate mandate relating to power generation. As a result, OPG, its directors, officers, and employees may be faced with increased risk of liability. Examples of such risks related to financing, include without limitation:

- liability as a promoter under Canadian securities laws (or the equivalent, if any, under other applicable securities laws);
- secondary market liability under Canadian and/or other applicable securities laws;
- liability the signatories to the prospectuses will have (i.e., the individuals signing the prospectus); and
- liability of OPG as the Financial Services Manager under any of the transaction agreements (e.g., the Financial Services Management Agreement, the Administration Agreement, the MSSA, the Master Trust Indenture and any Supplemental Indentures).

OPG and its Subsidiaries, and their respective directors, officers, employees may also be faced with risk of liability to:

- underwriters/agents selling debt securities of the financing entities
- the purchasers of debt securities of the financing entities (both initial purchasers and subsequent purchasers of the debt securities in the secondary markets)
- counterparties to agreements (e.g. the trustee of a financing entity that is a trust or IESO)
- other stakeholders (the Province, as shareholder of OPG, pensioners, and employees) of OPG if OPG (or any Subsidiary of it) is liable for any claim or obligation and cannot meet its obligations to these stakeholders as a result of such claims.
- Regulators (e.g. the Ontario Securities Commission)
- Parties who may challenge the *Act* or any component of it and include OPG as a party to such challenge.

As a result, pre-existing indemnities and protections do not adequately protect OPG, its Subsidiaries and each of their respective directors, officers and employees as explained further below.

Providing the requested Indemnity would help facilitate OPG and OPG's Subsidiaries in undertaking their role with respect to the implementation of the ONFHP.

IESO – *Role in Implementation of ONFHP and Associated Risks*

The *Act* also imposes certain obligations and requirements on the IESO to carry out various activities in relation to the implementation of the ONFHP such as the deferral of costs related to the GA, the creation of a regulatory asset in relation to the GA financing component of the ONFHP, the conveyance of that asset to OPG's financing entities and providing a servicing role in recovering OPG's funding costs from future ratepayers. The IESO may also be required to play a role in potential securities offerings of OPG's financing entities. If so, this may come with heightened exposure to liability for the IESO, particularly for offerings into the U.S. market. The IESO has expressed concern that all of this drives an increased risk of liability to the IESO, its directors, officers and employees, which is over and above typical operations risks and arises solely due to the ONFHP.

Other examples of sources/activities giving rise to increased risk of liability for the IESO, its directors, officers and employees include the following:

- Investors in any ONFHP investments or underwriters and banks regarding the offering of the investment asset to investors, as well as any securities prospectus or underwriting arrangements, with the IESO named and/or IESO being involved;
- OPG (or the financing entity) in relation to the commercial arrangements regarding transfer of the regulatory asset and servicing of the investment asset, and related activities;
- Market participants, program participants for issues in liquidity (e.g. short pay);
- Taxation authorities where prior approval of IESO's treatment is not approved by taxation authorities;
- Securities commissions regulators (U.S./Canada); and
- Parties who may challenge the *Act* or any component of it and include the IESO as a party to such challenge.

As a result, pre-existing indemnities and protections do not adequately protect IESO and each of their respective directors, officers and employees as explained further below.

Providing the requested Indemnity would help facilitate the IESO's undertaking of the activities requested by the Province in order to facilitate the implementation of the ONFHP.

4. ANALYSIS SUPPORTING RECOMMENDATION

(a) Why the Indemnities are being sought?

(i) Indemnities are required to facilitate IESO and OPG in carrying out their respective roles in implementing the ONFHP

The provision of the Indemnities is required in order to facilitate the implementation of the ONFHP. Both OPG and the IESO are required to carry out activities that may fall outside the scope of their typical business activities and corporate mandate. As a result, these activities could be perceived as not being carried out in "good faith" or in the best interest of the corporation thereby exposing OPG, OPG's Subsidiaries, IESO, and their respective directors, officers and employees to increased liability.

Even if the corporate mandates of OPG and the IESO were updated to include their role in implementing the ONFHP, this may not eliminate the risk of the types of liabilities outlined above completely, particularly due to the novelty of the ONFHP and the types of roles that OPG and IESO will be taking on. For example, persons could still challenge the *Act* or any component of it and include OPG or the IESO as a party to such challenge.

While statutory protection from liability is provided to IESO's directors, officers and employees, and to OPG's employees these protections are limited to "good faith acts". Therefore, the statutory protections do not preclude persons from bringing a claim against the Protected Persons (as defined in the Indemnities) in relation to these activities on the grounds of "bad faith".

Generally speaking the Indemnities are intended to provide the Protected Persons with indemnification for losses/liabilities, including those for potentially “bad faith acts”, unless any such acts arise as a result of the Protected Persons’ dishonesty, gross negligence, or wilful misconduct. As described below in subsection (ii), the statutory protections also do not indemnify for costs relating to defending a claim. The statutory protections also do not extend to the corporations themselves.

Both the IESO and OPG have specifically asked for these Indemnities in order to allow them to carry out their roles in implementing the ONFHP. Providing the requested Indemnities will provide OPG, OPG’s Subsidiaries, the IESO and each of their respective directors, officers and employees with assurance against liability in order to allow them to comprehensively carry out their respective roles in the successful implementation of the ONFHP.

(ii) Statutory Immunity does not preclude a person from bringing an action or other civil proceeding

Subsection 19(1) of the *Electricity Act, 1998* provides IESO directors, officers and employees with the following protection from liability:

> “No action or other civil proceeding shall be commenced against a director, officer, employee or agent of the IESO or a member of a committee or panel established by the board of directors of the IESO for any act done in good faith in the exercise or performance or the intended exercise or performance of a power or duty under any Act, the regulations under any Act, the IESO’s licence, the IESO’s by-laws or the market rules, or for any neglect or default in the exercise or performance in good faith of such a power or duty.”

The *Electricity Act, 1998* does not contain a similar statutory immunity for OPG’s directors, officers, employees or agents. However, under subsection 39(1) of the *Act*, a statutory immunity is provided to the OPG’s employees. This provision states:

> “No action or other civil proceeding shall be commenced against any employee of the Province or Ontario Power Generation Inc. for any act done in good faith in the exercise or performance or the intended exercise or performance of a power or duty under the Act, the regulations or for any alleged neglect or default in the exercise or performance in good faith of such a power or duty.”

Subsection 39(2) of the Act provides that nothing in subsection 39(1) limits the effect of subsection 19(1) of the *Electricity Act, 1998.*

The statutory immunities provided under the *Electricity Act, 1998* and the *Act* prohibit an action or other civil proceeding from being commenced against the enumerated persons for any act done in good faith in the exercise or performance of their duties. However, nothing precludes a person from bringing an action or other civil proceeding against these persons causing them to incur costs in defending the claim (for example, arguing that the act was not carried out in “good faith”).

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The immunity from suit provisions outlined above, are qualified by the words “for any act done in good faith in the exercise or performance or intended exercise or performance of a power or duty under this Act…” This is a question of fact that needs to be considered by a court of competent jurisdiction. As such, statutory immunity would not necessarily be a bar to litigation and does not ensure that the IESO’s and OPG’s employees, officer or directors (as applicable) would not become embroiled in litigation.

In the case of OPG, there is no similar statutory immunity explicitly provided for its directors, or officers so the risk of litigation is greater for these individuals.

For the reasons mentioned above, the Indemnities requested under this application would ensure that if a claim is brought against the Protected Persons as a result of carrying out their roles in implementing the ONFHP, they are fully protected for any costs, losses etc. subject to the limitations provided for in the Indemnities.

(iii) Insurance and indemnities that the IESO and OPG currently provide to its directors, officers and employees may not fully cover risk

OPG –Insurance and Indemnities

Currently, OPG has indicated that it maintains Directors and Officers liability insurance (“D&O Insurance”) with limits of USD $110 Million. The D&O Insurance includes persona coverage (side A) and corporate reimbursement coverage (side B). Under the side A coverage, OPG has advised that the policy pays losses where the organization is either not permitted by law or unable due to insolvency to indemnify the insured person under the policy (includes directors, officers and designated executives). This includes losses arising from a claim made during the policy period for a wrongful act (e.g. breach of duty, neglect, error, misstatement or omission) of such insured person. The full $110 Million limit is available for side A coverage.

Under side B coverage, OPG has advised that the policy reimburses the organization for losses incurred to indemnify an insured person under a D&O claim. The coverage is up to a maximum of USD $75 million, less the corporate deductible of $500,000.

OPG has advised that directors and officers have priority of payments over the organization for the entire $110M limit.

While this insurance provides coverage for directors and officers of OPG, there is no similar coverage provided for OPG’s employees. Further, any liability stated over the maximum amounts would not be covered by the insurance policy. Pursuant to section 2(a) of the IESO Indemnity and section 3(a) of the OPG Indemnity, a Protected Person shall not be entitled to indemnification to the extent that coverage is provided under an insurance policy and such Protected Person is actually paid under such insurance policy.

OPG has indicated that they provide their directors an indemnity but not to their directors or employees. OPG has not provided information about the scope of this indemnity. However, the Indemnities provide that a Protected Person shall not be entitled to indemnification to the extent that other indemnities are already provided to a Protected Person to the extent that the Protected Person is actually so indemnified. This language is meant to ensure that the covered losses under the Indemnities will be covered by other applicable indemnities first, before being covered by this indemnity.

OPG has not provided any information about insurance coverage and indemnities that its subsidiaries provide to their directors, officers and employees.

IESO – Insurance and Indemnities

The IESO has informed that it carries Directors & Officers insurance providing a maximum $15 million limit and $200,000 retention per claim. Employees are also included in the definition of Individual Insureds. The IESO also carries Professional liability insurance providing a maximum $75 million limit.
Aside from indemnification arising by operation of common law for employees acting within the scope of their employment, the IESO has informed that it has provided formal indemnity as follows:

- IESO has provided an indemnity to its board members.
- There is an indemnity provided to members of the Society of Energy Professionals pursuant to their collective agreement, whose members form a subset of all employees at the IESO.

Existing Indemnities to OPG and IESO from the Province

Existing indemnities previously provided by the Province to OPG have been limited to specific directives provided to OPG by the Province (e.g., in connection with the Bruce Lease). Accordingly, the scope of the existing indemnities provided by the Province would not cover the ONFHP. We are not aware of any indemnities provided to the IESO by the Province.

(b) Description of Risk and any Risk Mitigants.

The ONFHP is a novel program, the first of its kind in Canada. Because the work to be undertaken by OPG (and OPG's subsidiaries where applicable) and IESO in carrying out their roles in implementing the ONFHP will fall outside of the usual operations/business risk that these corporations face, there is a risk that these corporations may be subject to increased liability specifically due to their roles with the ONFHP. This risk arises in part because of the kind of market that OPG, and IESO indirectly, are to participate in, and the steps that investors could take to protect their investments as described in section 3 above.

The exact nature and scope of the risk to the Province of giving the Indemnities is undeterminable at this time, but the risk of liability for the Province arising may be low, with respect to directors, officers and employees, as any such risk may be mitigated by the following factors:

1) In the case of the IESO, the existence of a statutory immunity under subsection 19(1) of the *Electricity Act, 1998* may mitigate against a liability arising against its directors, officers and employees, but does not eliminate such risk.

2) In the case of OPG, the proposed statutory immunity under subsection 39(1) of the *Act* may mitigate against a liability arising against its employees, but does not eliminate such risk.

3) The Indemnities are limited to claims arising in relation to the Protected Persons' respective roles in relation to implementing the ONFHP.

4) The Indemnities do not apply with respect to Losses for which coverage is provided under insurance or another indemnity, to the extent already paid under such insurance, or so indemnified under such indemnification in relation to the claims.

5) The Indemnities do not apply to Losses that are a result of the Protected Person's dishonesty, gross negligence or willful misconduct.

With respect to the corporations themselves (and in the case of OPG, its Subsidiaries as well) the risk may be higher, but is undeterminable at this time. The likelihood of risk to the Province is characterized as medium, given that OPG and IESO have not identified any insurance or indemnities that would cover the corporations themselves (or in the case of OPG, the Subsidiaries themselves) in the event that such liability arises, nor is statutory protection provided for the corporations themselves.

A contingent liability table is attached as Appendix "C".

(c) Scope of liability in the Indemnities

The Province would agree to indemnify and hold harmless the IESO and OPG, and OPG's subsidiaries as well as their respective directors, officers and employees from any claims, liabilities, costs or losses that might arise to the Protected Person as a result of their roles in carrying out activities related to the implementation of the ONFHP.

Under the Indemnities, a Protected Person would not be entitled to be indemnified in respect of Losses, or a portion thereof:

(a) for which coverage is provided under an insurance policy or claims fund to the extent that such Protected Person is actually paid under such insurance policy or claims fund;

(b) for which other indemnities are already provided to a Protected Person to the extent that the Protected Person is actually so indemnified for those Losses by such indemnities;

(c) that are the result of such Protected Person's dishonesty, gross negligence or willful misconduct, but only if such dishonesty, gross negligence or willful misconduct on the Protected Person's part has been established by a final and non-appealable judgment or other final adjudication adverse to the Protected Person; or

(d) in the case of a criminal or administrative action or proceeding that enforces a monetary penalty, if such action or proceeding arises from any circumstances in which a Protected Person did not have reasonable grounds for believing was reckless as to their belief that the Protected Person's conduct was lawful in the case of a criminal or administrative action or proceeding that enforces a monetary penalty.

(d) Other Substantial Variances from the Province's Indemnity Template

The other substantial variances in the Indemnities includes a waiver provision whereby the Province waives its right to bring any claim it could otherwise make against a Protected Person who is an individual relating in any way to the Protected Persons' activities in the implementation, or otherwise relating to the ONFHP (including where a Protected Person is acting at the request of the corporation, in a different capacity than as a director, officer or employee of the Corporation – e.g. for example, where a financing entity is a trust, OPG's directors/officers/employees may need to sign the securities offering documents, but not in the capacity as OPG's directors/officers/employees, as the offering documents will not be the offering documents of OPG. The directors/officers/employees will be performing these functions as a result of OPG acting as a Financial Services Manager of the financing entity).

However, this waiver does not apply to gross negligence, dishonesty or willful misconduct claims that may be brought by the province against the applicable Protected Persons. The risk associated with providing this waiver is likely low given that it is consistent with the gross negligence carve out provided for in the Indemnity Agreements (section 2(c) in the IESO Indemnity and section 3(c) in the OPG Indemnity) and because the Province is unlikely to bring a claim against a Protected Person for Losses they have agreed to indemnify them for.

OPG has indicated that the inclusion of this waiver is very important to their Board given that its directors and officers are undertaking the ONFHP activities at the request of the Province. Accordingly, the directors, officers, employees do not want to take on liability towards the Province, as shareholder of OPG. The Indemnity is being provided to the IESO for consistency.

The Indemnities also include a representations and warranties section (section 8 in the IESO Indemnity and section 9 in the OPG Indemnity), which includes general representations and warranties with respect to the Province's authority to enter into these agreements and confirming that they have obtained the appropriate FAA approvals. We do not believe this variance poses a significant risk to the Province.

(e) Effect of failure to obtain section 28 approval

If the requested Indemnities are not provided, this could impact the OPG, OPG's Subsidiaries and IESO's (including their respective directors, officers and employees') willingness to fully undertake their roles in implementing the ONFHP. This may potentially jeopardize the successful implementation of this plan. For example, IESO directors may not be willing to carry out certain activities that would fall outside of the scope of its typical business activities and mandate if they view these as creating a risk of liability. Providing the Indemnities, would allow OPG, OPG's Subsidiaries, and IESO, along with their directors, officers and employees to more confidently carry out their role in implementing the ONFHP.

APPENDIX "A"

PROPOSED INDEMNITY AGREEMENT FOR OPG
(Attached as a separate document)

APPENDIX "B"

PROPOSED INDEMNITY AGREEMENT FOR IESO
(Attached as a separate document)

APPENDIX "C"

CONTINGENT LIABILITY TABLE
(Attached as a separate document)