Ministers' Speaking Points – Meeting with the Auditor General to discuss the Special Report on the Ontario Fair Hydro Plan

Policy Intent

- Ontario's Fair Hydro Plan (OFHP) is delivering the single-largest reduction in electricity rates in the province's history.

- Since 2003, nearly $70 billion has been invested in the electricity system, including more than $37 billion in electricity generation to ensure the system is clean and reliable.

- The majority of the province's electricity generators operate under 20-year contracts.

- Third-party experts have confirmed that many of these generators will be able to continue to operate beyond their contract lives.

- Refinancing the Global Adjustment (GA), which pays for the bulk of the recent investments in the electricity system, provides significant and immediate rate relief by matching the cost of electricity investments with the expected useful life of the generation that has been built.

- The GA refinancing design most effectively achieves the goals of the refinancing program and ensures that the deferred costs are borne by the rate-base, as the beneficiaries of the electricity system, and not the tax-base.

- In developing OFHP, the government considered a range of implementation options and consulted with legal, accounting, financial and energy sector third-party experts to provide advice and ensure due diligence was completed.

Financing

The report claims that consumers will pay an additional $4 billion in interest costs over the life of OFHP since OPG and its Financing Entity will pay a higher rate of interest compared to the Province.

- The policy objective of the OFHP is to smooth the cost to ratepayers over the useful life, not the contractual life, of the electricity generating assets. Therefore, it was a primary policy objective to ensure that the costs are borne by the beneficiaries of the electricity system - the rate payers - not the tax-base.
    - The Province has never calculated a differential between the Province and the Financing Entity's borrowing costs, because of this policy decision.

- It is appropriate for ratepayers to pay for the financing of electricity assets.
    - The rate base has a different risk profile than the tax base, resulting in higher interest costs.

- The $4 billion figure was sourced from the FAO's May 2017 report, and a similar figure was never calculated by the Province.
    - However, it is important to note, that the FAO's calculation was based on preliminary estimates of the program when peak debt estimates for the thirty year program were substantially higher and interest costs were forecast to be higher than current projections.

<u>Accounting</u>

The report claims that the accounting treatment proposed in the Fair Hydro Act violates government accounting and is not in line with Canadian Public Sector Accounting Standards. It also claims that the government knew that the risk of a qualified audit opinion was high when developing the OFHP, but chose to accept the risk in order to avoid showing a deficit/increased debt.

- The government's financial statements are prepared in accordance with Public Sector Accounting Standards (PSAS), and will continue to follow these standards for the transactions resulting from the Ontario Fair Hydro Plan in 2017-18 and in future years.

- As previously discussed with your office, there are two fundamental accounting assertions in the report that we disagree with, related to legislated accounting and rate-regulated accounting.

- First, as has been previously communicated to your office, the Ontario Fair Hydro Plan Act does not create accounting rules or legislate the accounting. [**Note that the OAG has now defined "legislated accounting" for the purposes of the report as creating an asset through legislation.]*

- Second, in regards to rate-regulated accounting, PSAS are silent on the use of regulated accounting.

    - PSAS acknowledges that it does not provide guidance on all possible transactions and notes that it is necessary to refer to other sources of guidance that are consistent with the PSAS framework.
    - We believe US GAAP, with the most developed guidance on rate-regulated accounting, is the appropriate guidance to reference.

- Many entities in Canada, including OPG and Hydro One use rate-regulated accounting.

    - The OAG can refer to the CPA Canada research study that was shared.

    - Rate-regulated accounting is well understood in the electricity sector.

- IESO management, IESO's Audit Committee, IESO's Board of Directors, IESO's external auditor, and the Office of the Provincial Controller all support the use of rate-regulated accounting by IESO.

- In the development of the Fair Hydro Plan, the government consulted with several third party advisors in the application of accounting standards. This is normal course of business governments take for complex transactions.