

GETTING THE DEAL THROUGH

Electricity Regulation

in 31 jurisdictions worldwide

Contributing editor: Earle H O'Donnell

2008



Published by
GETTING THE DEAL THROUGH
in association with:

Araújo e Policastro Advogados
Arthur Cox
Berkemeyer, Attorneys and Counselors
Berwin Leighton Paisner LLP
bpv | Jádi Németh Attorneys at Law
Carey y Cía Ltda Abogados
Cavelier Abogados
Ćurković Janušić & Banić
Dewey & LeBoeuf Grzesiak LP
Dewey & LeBoeuf LLP
Estudio O'Farrell
Gorrissen Federspiel Kierkegaard
Headrick Rizik Alvarez & Fernández
Heuking Kühn Lüer Wojtek
Hoet Peláez Castillo & Duque
Kelemenis & Co
Kronbergs & Čukste
Lenz & Staehelin
López Velarde, Heftye y Soria
Macchi di Cellere Gangemi
McMillan Binch Mendelsohn LLP
Minter Ellison Rudd Watts
Nestor Nestor Diculescu Kingston Petersen
ÖztekinBoden
Peltonen Ruokonen & Itäinen, attorneys-at-law
Rodrigo, Elías & Medrano Abogados
Schönherr Rechtsanwälte
SimmonsCooper Partners
Stek
Tark & Co
Yukov Khrenov and Partners

Canada

Mike Richmond

McMillan Binch Mendelsohn LLP

Policy

- 1** What is the governmental policy and legislative framework for the electricity sector?

Canada is a federation with one federal government, 10 provincial governments and three territorial governments. The Canadian Constitution assigns jurisdiction over natural resources and electricity generation to the provinces, while reserving matters of international trade and commerce to the federal government. The construction and operation of international transmission lines and the regulation of power exports from Canada are therefore matters of national policy generally falling to the federal minister of natural resources, administered by the National Energy Board (NEB), a federal regulatory tribunal. Most other electricity policies are provincial matters administered by a variety of provincially established regulators, authorities and Crown corporations.

Alberta is the only province with fully competitive wholesale and retail electricity markets. Ontario opened its wholesale and retail markets to competition in 2002, but was partially reregulated a short time later in response to pricing issues. British Columbia completed a corporate separation of its generation and transmission operations and New Brunswick also completed a corporate separation of generation, transmission and distribution. The remaining provinces' systems are managed in large part by their respective provincially-owned, vertically-integrated utilities. As most of those systems are interconnected more on a north-south basis with the US than on an east-west basis with other Canadian provinces, the ability to import and export power and to leverage US market prices can have a significant but largely understated influence on provincial policy considerations.

Organisation of the market

- 2** What is the organisational structure for the generation, transmission, distribution and sale of power?

In 1998, Ontario's former provincial utility, Ontario Hydro, was split into five government-owned successor corporations, including Ontario Power Generation (OPG, a competitive generator), Hydro One (the monopoly transmitter whose privatisation was abandoned in 2002) and the Independent Electricity System Operator (IESO, administrator of the spot market and provider of open access to the grid system). Ontario's more than 400 municipal distribution utilities were incorporated and merged into just under 90 local distribution companies (LDCs), most of which are still municipally or provincially owned through Hydro One. The Ontario Power Authority (OPA) is charged with procuring new supply from private developers through competitive processes

or standard offer programmes and entering into 20-year power purchase agreements or revenue guarantees with successful proponents. Ontario now operates under a 'hybrid market' system, with power from new facilities sold through the open market operated by the IESO, and most power from existing or 'heritage' facilities subject to prices essentially frozen by regulation, contract or revenue cap.

Quebec's provincial utility, Hydro-Quebec (HQ), has split its production, transmission, distribution, construction, oil and gas, and research and development functions into separate divisions, but no plan to divest any division has been announced. The production arm remains the dominant generator in Quebec, with its 165TWh 'heritage pool' providing the bulk of supply to HQ Distribution. HQ Distribution procures load in excess of the heritage pool through a competitive bidding process (unless the resulting power purchase agreement is for a term of less than three months), in which private developers compete with HQ Production. In particular, wind power producers have made gains in the Quebec market. While HQ is the dominant generator of hydroelectric power in the province, it has recently issued requests for proposals (RFPs) for wind energy. HQ's transmission division, Trans-Énergie, operates the largest transmission system in North America on an open access and regulated tariff basis. HQ Distribution's exclusive distribution territory covers most of the province, where it provides service at regulated rates; together with a few other municipal distributors, it makes up the wholesale market through its purchases in excess of the heritage pool.

Alberta has a fully competitive generation market, although construction, operation and decommissioning continue to be regulated by the Alberta Energy and Utilities Board (EUB). The Alberta Interconnected Electric System (AIES) is owned by a number of utilities (known as transmission facility owners or TFOs) and open access to this province-wide transmission grid is managed by the Alberta Electric System Operator (AESO). Distribution systems remain regulated, with the EUB approving rates for investor-owned and some municipal LDCs. Other municipal LDCs have their rates set by city councils, whereas those owned by rural electrification associations have rates set by their boards.

British Columbia's provincial utility, BC Hydro, is primarily responsible for the generation and distribution of electricity in the province. BC Hydro created an independent, government-owned transmission corporation in 2003. The BC Transmission Corporation (BCTC) operates and manages BC Hydro's transmission assets and facilitates transmission access to industrial customers and independent power producers. Both BC Hydro and BCTC are regulated by the British Columbia Utilities Commission (BCUC).

Most other provinces have government-owned, vertically integrated utility monopolies, which own the bulk of generation and transmission assets, with distribution systems owned by the province or municipalities. In addition to energy, market participants have the ability to trade in other related products, such as transmission rights, black start capability and voltage support. These products and services may be controlled or regulated in each province by the local transmission company, the regulator or, most often, the system operator.

Regulation of electricity utilities – power generation

3 What governmental or administrative authorisations are required to construct and operate generation facilities?

The types of authorisations required vary by provincial jurisdiction, fuel type, location and the type and size of associated transmission facilities. Since the facilities are generally situated within one province, provincial approvals are the dominant requirement and of those, environmental approvals are the most significant. Each province has its own environmental assessment legislation and requirements.

Certain triggers, however, such as the involvement of First Nation communities, lands, navigable waters or fisheries, or federal legislation, lands or funding, necessitate a federal environmental assessment. In these cases, many provinces, including Ontario, Quebec and Alberta, have signed environmental assessment cooperation agreements to harmonise the provincial and federal environmental assessment processes. For provinces without cooperation agreements, such as Nova Scotia, ad hoc project agreements to establish joint federal-provincial review panels can be used to harmonise the processes.

Other provincial requirements may include approvals for air emissions, water taking and discharge, waste generation, noise and odour. Municipal permits may also be required for construction, land use issues such as zoning or amendments to a municipality's Official Plan, sewer use and other municipal matters. Once a facility is constructed, jurisdictions such as Ontario and Alberta require that the owner or operator be licensed by the relevant regulator (eg, the OEB or EUB) and authorised by the relevant system operator or ISO to sell the power into the electricity market. Where a vertically integrated monopoly exists, the licensing and permitting for operating is a less stringent internal process unless the facility is an independent power producer (IPP). In the case of IPP facilities, authorisations from the monopoly utility and the relevant regulator are required and the IPP may be required to sell its output to the monopoly generator.

4 What are the policies with respect to interconnection of generation to the transmission grid?

The policies vary depending on whether the jurisdiction is characterised by a vertically integrated utility or by markets with functionally separated generation, transmission and distribution. In a vertically integrated monopoly utility, interconnection to the transmission grid is largely a matter of internal review and authorisation, except where an IPP is interested in connecting to the monopoly-operated transmission grid. In such cases, transmission owners provide non-discriminatory access to the grid, provided certain conditions are met. When an IPP or a load customer wishes to interconnect, the transmission arm of the relevant monopoly utility will be involved in assessing the impact and cost of the connection on the system and in ultimately providing the interconnection authorisation. Varying policies affect

the allocation of costs associated with interconnection with the transmission grid.

Ontario's Transmission System Code (TSC) sets out the parameters for interconnection, including cost allocation and operational requirements. The TSC requires all interconnecting customers to enter into an OEB-approved standard connection agreement and that the cost of interconnection and network upgrades attributable to a new customer be borne by that customer. Network upgrades that benefit the system as a whole are spread among all transmission tariff customers.

In Alberta, the AESO manages the interconnection process pursuant to principles outlined in the Electric Utilities Act, which mandates that the AESO, as transmission administrator, provide non-discriminatory access to the AEIS if certain technical requirements, as outlined in the Technical Requirements for Connecting to the Alberta Interconnected Electric System (IES) Transmission System, and terms and conditions in the transmission administrator's tariff are met. The tariff requires interconnection applicants to pay a fee to defray the AESO's costs associated with evaluating the feasibility of the interconnection. Once the feasibility studies are complete, the generator may enter into a construction commitment agreement and post a performance bond; the AESO will then undertake construction of the facilities. The generator must next execute a system access service agreement prior to commissioning the facilities. Costs associated with the new facilities are categorised as either system-related or customer-related. System-related costs are rolled into the transmission rate base and customer-related costs are borne by the generator. The contribution from the customer is determined by the AESO in accordance with a formula in the tariff.

The provinces of New Brunswick and Nova Scotia have adopted open access transmission tariffs (OATT) governing access to the grid. In 2007, the New Brunswick system operator conducted an open season under the OATT for 300MW of new transmission capacity which will become available between New Brunswick and the US state of Maine. Hydro-Quebec submitted the winning bid, giving it export priority for up to 300MW for 15 years. Maritime Electric Company, the Prince Edward Island utility, was also granted a 25-year reservation for up to 30MW flowing from the province of Prince Edward Island into New Brunswick.

5 Does the governmental policy or legislation foster power generation based on alternative energy sources such as renewable energies or combined heat and power?

Federal budget initiatives designed to offset the incremental costs associated with wind and other renewable power projects were initially abandoned by the new federal government elected in 2006, but were reintroduced in 2007. They include ecoEnergy for Renewable Power, which provides an incentive payment of 1 cent per kWh for up to 10 years to eligible low-impact, renewable electricity projects constructed between 1 April 2007 and 31 March 2011.

To stimulate the use of clean generation technologies, accelerated depreciation for capital spending on alternative energy sources is also permitted. The list of assets eligible for accelerated cost of capital allowance (CCA) has been expanded to include distribution equipment, such as pipelines, pumps and meters used in district energy systems and equipment used to produce biogas from the anaerobic digestion of farm manure. Further, qualifying equipment acquired between 23 February 2005 and 31 December 2011 that falls into set criteria for high-efficiency

cogeneration systems or renewable energy generation systems is eligible for a 50 per cent CCA depreciation rate for tax purposes. In addition, if a majority of a project's tangible property consists of eligible renewable or energy-efficient equipment, the project's expenses may qualify as Canadian renewable and conservation expenses, allowing certain start-up expenses to be deducted in full in the year incurred and carried forward indefinitely, or transferred to investors using flow-through shares.

Individual provinces offer certain corporate income and property tax incentives as well as power purchase agreements pursuant to request for proposal processes to encourage the construction of renewable power generation facilities. Many provinces have considered or adopted renewable portfolio standards. For example, Prince Edward Island is aiming for 100 per cent of its supply from wind. Ontario has launched a renewable energy standard offer programme for small renewable projects (less than 10MW) pursuant to which generators will be paid 11 cents per kWh for 20 years (42 cents per kWh for photovoltaic). British Columbia is in the process of developing a similar standing offer programme for small renewable projects (less than 10MW), at a proposed price of between 6.5 and 8.2 cents per kWh.

Many provinces have also launched various procurement programs to encourage the development of large-scale renewable energy and combined heat and power projects by private developers. In Quebec, with 1,000MW of wind power currently being built, HQ announced a second RFP for the supply of 2,000MW of wind power in October 2005. The 2005 RFP closed in September 2007, with over 7,700MW offered by private developers. In Ontario, the government has directed the Ontario Power Authority to procure an additional 2,000MW of renewable power. The OPA is set to launch an RFP for the first 500MW early in 2008. A separate RFP for combined heat and power projects is also in development. British Columbia released the BC Energy Plan in 2007, which calls for 50 per cent of incremental demand to be satisfied by conservation by 2020, with 90 per cent of actual generation to be in the form of renewable energy. Under this Plan, BC Hydro will launch a clean power call for tenders in 2008, seeking to purchase up to 5,000GWh of clean energy per year from independent power producers.

Regulation of electricity utilities – transmission

- 6** What governmental or administrative authorisations are required to construct and operate transmission networks?

In Ontario, the OEB approves the construction of electricity transmission lines of voltages higher than 50kV and longer than two kilometres. The OEB reviews a transmission project's effect on consumers with respect to price, reliability and quality of electricity service. The review of environmental issues associated with the construction of a transmission line is the responsibility of the Ontario Ministry of Environment, which examines construction-related effects and determines routing and construction procedures through the environmental assessment process. Transmission line operators must hold a transmission licence from the OEB and be an authorised market participant under IESO rules.

In Alberta, the EUB approves the construction of any transmission line greater than 60kV using the traditional tests of need and necessity. Quebec requires no authorisations for private transmission network owners or operators to construct and operate their networks. Private transmission networks must, however, negotiate a three-step process with HQ involving a preliminary integration study, pre-approval and a final proposal in order to

connect to the power system. HQ TransÉnergie's capital expenditures over C\$25 million and its reliability and technical standards are subject to regulatory approval. Environmental and land-use approvals may also be required for transmission construction.

Cross-border transmission connections (between Canada and the US) and those linking Canadian provinces also require the approval of the National Energy Board.

- 7** Who is eligible to obtain transmission services and what requirements must be met to obtain access?

Provinces with government-owned vertically integrated utilities generally provide a regulated bundled service. In Ontario, transmitters provide an unbundled postage stamp-rate network transmission service to all suppliers and wholesale purchasers of energy on a non-discriminatory, open-access basis. In Alberta, the AESO offers an unbundled open-access, non-discriminatory transmission service to all market participants under its regulated tariff. The transmission cost of service is recovered from supply and load customers equally; postage stamp transmission rates for load (but not supply) customers are mandated by the Electric Utilities Act. Hydro-Quebec's TransÉnergie division provides tariff-regulated unbundled transmission services to eligible wholesale customers. An eligible customer must, among other things, meet creditworthiness criteria, enter into a standard-form service agreement and offer reciprocity to TransÉnergie over its (and its affiliates') facilities in interstate, inter-provincial or international commerce.

- 8** Are there any governmental incentives to encourage expansion of the transmission grid?

Transmission is generally owned and operated by government-owned utilities, and therefore no financial incentives are required.

Merchant transmission is a rarity in Canada. An 80km line was developed six years ago by five First Nations bands to connect several of Ontario's northern communities to the grid. Government assistance was negotiated on a one-off basis. A merchant line is currently under development between Alberta and the US, for which no government incentives were received on the Canadian side. There has also been a proposal for a merchant transmission line under the Great Lakes to connect Ontario with the US. No financial incentives have yet been offered.

- 9** Is there any tariff or other regulation regarding the rates and terms for the provision of transmission services?

In Ontario, transmission rates are set by the OEB to ensure they are just and reasonable. In Alberta, the AESO submits a single tariff setting out the rates, and terms and conditions that apply to each class of transmission system access service. The AESO contracts with the TFOs for use of their transmission facilities, and each TFO prepares a tariff setting out the rates AESO will pay for use of the facilities. The rates and terms and conditions of the TFO tariffs and the AESO tariff are subject to EUB approval. The EUB approves the prices and rates using a two-step process in which the first phase application determines the revenue requirement for the AESO. The second phase application determines the allocation of costs between the different classes of customers for the provision of system access services by the AESO. These rates are then charged to customers to cover AESO's operation costs. Electric tariffs in Alberta under the EUB's jurisdiction continue to

be regulated on a traditional cost-of-service basis, although the Electric Utilities Act does contemplate some form of performance-based ratemaking. In other provinces, transmission and distribution rates are reviewed or set by the provincial executive or regulator. In Quebec, the open-access transmission service tariff is determined by regulation on a cost-of-service, postage stamp basis, subject to the approval of the Régie de l'énergie du Québec (the Régie).

10 Which entities are responsible for assuring reliability of the transmission grid and what are their authorities and responsibilities?

In Ontario, the IESO is responsible for developing 18-month forecasts of electricity demand and reliability on a six-month 'rolling' basis, while the Ontario Power Authority has been charged with developing a 20-year Integrated Power System Plan, bringing together the responsibility for long-term planning and reliability of both the transmission and generation systems. The Plan will be reviewed by the Ontario Energy Board before being implemented, perhaps in 2008. In Alberta, the AESO assesses the current and future needs of market participants, plans the transmission system's ability to meet the needs of the market, and arranges for necessary enhancements and upgrades to the transmission system. The Alberta government implemented a Transmission Development Policy and a Transmission Regulation pursuant to which the AESO develops need documents and transmission system plans.

Alberta and British Columbia belong to the Western Electricity Coordinating Council (WECC), a voluntary organisation responsible for, among other things, coordinating and promoting electric system reliability. WECC is the largest and most diverse of the 8 regional councils of the North American Electric Reliability Corporation (NERC), its operations extending through the US to Mexico. Manitoba is a member of the Midwest Independent Transmission System Operator, a Federal Energy Regulatory Commission (FERC)-approved regional reliability organisation (RRO) that ensures equal access to the transmission system and maintains or improves electric system reliability in the Midwest. Canada and all of its provinces belong to NERC, an organisation established to ensure that the bulk electric system in North America is reliable, adequate and secure. NERC was certified by FERC as the electric reliability organisation (ERO) for the US in accordance with the US Energy Policy Act of 2005, with statutory authority to develop and enforce all US market participants' compliance with reliability standards.

Regulation of electricity utilities – distribution

11 What governmental or administrative authorisations are required to construct and operate distribution networks?

The type of approval varies across provinces. Ontario and New Brunswick require a licence prior to owning or operating a distribution system. In British Columbia, the BCUC must issue a certificate of public convenience and necessity before constructing or operating a distribution system. In Alberta, municipalities may grant a right to distribute electricity to the owner of a distribution system via 'franchise agreements', with the grant subject to EUB approval. Unless the owner is a subsidiary of the municipality, the distributor may be required to register with the operator of the transmission grid to withdraw electricity from the grid.

In most provinces, construction of an extension to a distribution system is generally not subject to approval. Where a distributor is subject to rate regulation, the regulator may review the

cost of the capital projects to determine the appropriate amount to include in the distributor's rate base.

12 Who is eligible to obtain access to the distribution grid and what requirements must be met to obtain access?

The right to connect to a distribution grid depends on the province and, in some instances, whether the person requesting access is a generator, retailer or consumer. In Ontario, distributors must provide non-discriminatory access to consumers and retailers. However, distributor licences may contain conditions limiting the quantity of generation that may be connected to the distribution system. Alberta does not require distributors to provide access to the distribution system in a manner that is not unduly discriminatory. The person requesting access must obtain approval of the owner of the distribution system before gaining access. In Quebec, HQ Distribution must provide access on the terms and conditions set by the Régie. Usually, connection is completed once the distributor is satisfied that the connection is technically acceptable and suitable performance security has been provided.

13 Is there any tariff or other regulation regarding the rates or terms for the provision of distribution services?

In Ontario, distributors are required to charge only OEB-approved rates. In Alberta, investor-owned utilities have rates set by the EUB, municipally-owned distributors have rates set by the municipal council and distributors owned by a Rural Electrification Association (REA) have rates set by the board of directors of the REA. In British Columbia, rates for public utilities are approved by the BCUC. In Quebec, HQ charges uniform rates, approved by the Régie, across the province for each class of customer. The rates charged by the other distributors in Quebec are not regulated.

Regulation of electricity utilities – sales of power

14 What governmental or administrative authorisations are required for the sale of power to customers and which authorities grant such approvals?

In most Canadian provinces, retail customers purchase a bundled product from a single franchised or monopoly provider. Ontario and Alberta provide for wholesale and retail competition. Although in Ontario electricity retail customers are free to purchase energy from any retailer licensed by the OEB, price freezes introduced in late 2002 followed by tiered, regulated pricing for residential, low-volume and designated consumers have effectively eliminated any new retail choice other than retailers offering renewable alternatives. Retailers must hold an OEB licence to sell, offer to sell or act as agent or broker for a retailer or consumer. The OEB also issues wholesale licences that authorise the purchase of electricity from the IESO-markets or directly from generators and the sale of electricity through the IESO-markets to non-end use consumers. Local distribution companies providing energy supply at pass-through prices to those who do not acquire electricity from a retailer must hold an OEB licence to own and operate a distribution system and act as a default supplier.

Alberta consumers are free to purchase electricity from any retailer licensed by the EUB. Competitive retailers are licensed by Alberta Government Services (AGS) under the Fair Trading Act. In addition, AGS reviews the relevant retail contracts before granting a licence. For regulated service, the EUB regulates the

electric utilities and approves regulated rates for certain cities. Other municipally-owned utilities are regulated by their municipal councils. HQ Distribution is the exclusive distributor in most of the province of Quebec, with minor exceptions.

15 Is there any tariff or other regulation regarding power sales?

In Ontario, the OEB has been mandated to set the price for electricity to be paid by residential, low-volume and designated consumers, other than those who opt to purchase from a retailer. The price of electricity for eligible consumers is presently a tiered rate based on consumption. The price is based upon an OEB forecast of the cost to supply consumers of electricity over the next 12 months, as well as any accumulated difference between the amount consumers paid for electricity and the amount paid to generators in the previous period. This price may be revised every six months based upon an updated OEB forecast and any difference between the amount consumers paid for electricity and the amount paid to generators. Large-volume consumers continue to purchase power at unregulated prices.

Alberta has a Regulated Rate Option (RRO) for residential, farm, irrigation, and small business consumers who have not signed with retailers. The RRO, which will be in place until at least 2015, includes a blend of short- and long-term hedges, with the composition changing per year until 2010, when the goal is to use only short-term hedges. In Quebec, prices for wholesale or export sales are not regulated; retail service rates of HQ are set at regulated rates on a cost-of-service basis.

16 To what extent are electricity utilities that sell power subject to public service obligations?

In Ontario, distribution companies are obliged by law to sell power to consumers connected to their systems unless the consumers elect to purchase their power from marketers. In Alberta, owners of an electrical utility are required to appoint one or more retailers to act as default suppliers. The default supplier must provide retail electricity services to a customer that is unable to continue to purchase retail electricity services from the customer's retailer for any reason or where the customer is unable to obtain retail electricity services for any reason. In Quebec, a public utility with exclusive distribution rights must supply electricity to any person in its exclusive service territory who requests it. HQ Production must supply a heritage pool of up to 165TWh per year to HQ Distribution at a set average commodity rate. Similarly, in an effort to keep power prices down, Ontario's largest generator has been instructed by its sole shareholder, the Government of Ontario, to cap its prices on power generated by certain 'heritage' assets, and to refund a portion of its income if profits exceed a specified cap.

Regulatory authorities

17 Which governmental or administrative authorities determine regulatory policy with respect to the electricity sector?

The National Energy Board is involved in matters under federal jurisdiction, while provincial energy boards such as the OEB, EUB, BCUC and the Régie play various roles in matters of provincial regulatory policy. Ontario's IESO and Alberta's AESO set and administer policies for grid interconnection, transmission reliability and security, and spot market operation. Ontario's OPA has assumed responsibility for system planning in that province,

including transmission planning, which it shares in part with the OEB. Most projects will also be subject to environmental regulatory policy set by provincial ministries of the environment, and in some cases the Federal Ministry of the Environment. In provinces where a single vertically integrated monopoly utility still exists, such as Manitoba Hydro or Nova Scotia Power, those Crown corporations may play leading roles in setting provincial energy policy as well.

18 What is the scope of each regulator's authority?

The scope of a particular regulator will be found in the relevant legislation, which will inform the market as to whether the regulator is a policy-making or administrative body. The NEB determines regulatory policies for the construction and operation of international transmission lines and issues permits or licences for the export of power. Provincially appointed regulators (often as directed by their respective provincial governments) set policies for matters under provincial jurisdiction, including generation procurement and siting, intra-provincial transmission lines, transmission rates, distribution rates, retail issues, utility consolidation, consumer complaints and (except for those provinces with fully competitive electricity markets) commodity pricing. In Ontario, the OPA has responsibility for development of the Integrated Power System Plan, which sets priorities for the procurement of generation and for the construction of new transmission, but it must be approved by the Ontario Energy Board.

19 How is each regulator established and to what extent is it considered to be independent of the regulated business and of elected officials?

The NEB and provincial regulatory bodies are established under federal or provincial legislation, respectively. Their members are generally appointed by the relevant government, usually for fixed terms. These tribunals act as quasi-judicial bodies independent of the regulated businesses. Although in large part they exercise their powers free of politics and interference from elected officials, their jurisdiction is set out in legislation that may be amended by the relevant legislature. By statute some regulators are subject to direction from provincial or local governments. In particular, Ontario has been more active than most in issuing directives to the OEB and OPA. Some independent authorities, such as the IESO and the OPA in Ontario, are also subject to oversight in part from other regulators, such as the OEB, through the power to approve the authority's costs and rates.

20 To what extent can decisions of the regulator be challenged or appealed, and to whom? What are the grounds and procedures for appeal?

The basis for appealing a regulator's decision is usually found in the statute establishing the tribunal. Although the precise scope for appellate review varies between jurisdictions, as a general principle a regulator's decision may be appealed to or reviewed by a court – the Federal Court in the case of the NEB, and the provincial superior courts or courts of appeal in the case of provincial regulators. In some jurisdictions the right to appeal is not automatic but requires leave of the court. In others, such as Quebec, the decisions of the regulator are not subject to appeal or judicial review. Appellate review usually is limited to questions of law or jurisdiction. Federal and provincial courts tend to give deference to regulators on matters of economic policy and rate-setting within a regulator's jurisdiction, but will not give deference to questions involving the regulator's jurisdiction or questions

of law. Some regulators will also review their own decisions if they suspect an error of law or jurisdiction or if new information becomes available.

Acquisition and merger control – competition

- 21** Which governmental body or bodies have the authority to approve or disapprove mergers or other changes in control over businesses in the sector or acquisition of utility assets?

The Competition Tribunal under the Competition Act has the ability to issue remedial orders with respect to any merger that is likely to substantially lessen or prevent competition. The Minister of Industry under the Investment Canada Act also approves certain acquisitions by non-Canadians that are ‘likely to be of net benefit to Canada’.

Most of the provincial electricity regulators also have the power to review mergers and changes in control over regulated utilities. For instance, in British Columbia, the BCUC must approve changes in control and in Ontario the applicant must seek leave from the OEB to complete the merger or change in control. Note that in Ontario, the sale of a distribution utility attracts a ‘transfer tax’ of 33 per cent. However, the government has approved a ‘transfer tax holiday’ where the purchaser is another publicly-owned utility and the transaction is completed by 17 October 2008.

- 22** What criteria and procedures are applied with respect to the review of mergers, acquisitions and other transfers of control? How long does it typically take to obtain a decision approving or disapproving the transaction?

The Competition Act establishes mandatory pre-merger notification for mergers involving the acquisition of a Canadian business where certain financial thresholds are met. If notifiable, the merger cannot be completed before the expiry of no-close periods ranging from 14 to 42 days. The commissioner of competition will review mergers and may challenge a transaction; the Competition Tribunal is the ultimate decision-making authority. Review by the minister of industry under the Investment Canada Act also may be required, depending on the target’s asset value and other criteria. Reviews typically last at least 45 days.

Provincial electricity regulators also have their own processes for reviewing mergers and acquisitions. For instance, in Ontario, the OEB must approve any change in control of voting securities of a transmitter or distributor and any disposition of a significant part of a transmission or distribution system. In Alberta, a ‘designated public utility’ (which includes all investor-owned electric utilities) must seek the approval of the EUB before it may issue any stocks, bonds, debentures or other evidence of indebtedness; capitalise certain parts of its business, including contracts or leases; sell, lease, mortgage or otherwise encumber its property; or merge or consolidate its property. Generally, the provincial electricity regulators are primarily concerned with the impact of the transaction on the ‘public interest’. Public interest is a broad term that may encompass a variety of factors, including the impact on customer tariffs, the financial stability of the purchaser, and changes to the intended operation of the utility. The duration of approvals depends on the nature and extent of opposition to the transaction.

- 23** Which governmental or administrative authorities have the power to prevent or prosecute anti-competitive or manipulative practices in the electricity sector?

The Competition Act is of general application and gives the commissioner of competition the power to investigate anti-competitive practices in the electricity sector through the Act’s civil abuse of dominance, criminal price-fixing and other provisions. The Competition Act also contains provisions relating to consumer protection, such as misleading advertising, that could be applied to the electricity sector.

In addition to the general application of the Competition Act, electricity markets are generally monitored by a provincial organisation such as the Market Surveillance Administrator (MSA) in Alberta or the OEB’s Market Surveillance Panel (MSP) in Ontario. Participants in the electricity industry may also have to comply with the requirements of the provincial regulators on consumer protection-related competition issues. The provincial regulators generally have the ability to levy fines or other sanctions and revoke licences. In Ontario, the Competition Bureau and the OEB have entered into a memorandum of understanding regarding their roles in preventing and prosecuting anti-competitive behaviour.

- 24** What substantive standards are applied to determine whether conduct is anti-competitive or manipulative?

In general, competition law violations are concerned with a ‘substantial prevention or lessening of competition’. Therefore, an in-depth analysis is required to determine what impact the conduct has had or may have on the market. Competition law provides both civil and criminal sanctions. Therefore, the burden of proof that the commissioner of competition must meet varies depending on the nature of the act.

Provincial market surveillance organisations, such as the MSA in Alberta, are generally concerned with the integrity of trading in the market and ensure that participants cannot game the market. In Ontario, the MSP monitors the wholesale markets and the conduct of market participants to identify inappropriate or anomalous market conduct or abuse of market power. In addition, licensing bodies are generally more concerned with consumer protection (false or misleading statements) found in regulations or codes of conduct than with market activities.

- 25** What authority does the governmental body have to preclude or remedy anti-competitive or manipulative practices?

Under section 79 of the Competition Act, the Tribunal may make an order to remedy an abuse of dominance if it determines that one or more dominant firms have engaged in a practice of ‘anti-competitive acts’ that has resulted in a substantial prevention or lessening of competition. The Tribunal can issue orders prohibiting parties from engaging in anti-competitive acts and take any action the Tribunal deems reasonable and necessary to overcome the effects of the practice, including divestment of assets or shares. Similar sanctions are possible for the violation of other civil provisions of the Competition Act.

Section 45 of the Competition Act forms the core of Canadian cartel law. This provides that everyone who conspires, combines, agrees or arranges with another person to prevent or lessen competition unduly is guilty of an indictable criminal offence and liable to imprisonment for a term not exceeding five years, or to a fine not exceeding C\$10 million, or both.

Provincial electricity regulators may impose a variety of

Update and trends

Renewable generation

Although Canada is a signatory to the Kyoto Protocol, it does not have a plan or legislation in place to achieve its Kyoto targets. Provincial governments are nonetheless keen to be seen to be moving forward to reduce greenhouse gases. As a result, almost all provinces are rapidly expanding their procurement of renewable power projects through renewable portfolio standards, competitive green power procurement processes, or financial and contractual support of green power projects in neighbouring provinces. The coming year will see a continued expansion of wind power capacity in Canada, with the beginnings of growth in the solar and biomass sectors as well.

Nuclear power

The debate over the status of nuclear power rages on in at least three provinces, and at the federal level. Existing reactors in Ontario and New Brunswick are nearing the end of their useful lives, and decisions are being made whether to incur the capital costs of refurbishment, or simply shut the plants down. In Ontario, where 50 per cent of all power consumed comes from the province's 20 nuclear reactors, the government has announced its intentions to build one or two new nuclear facilities. In Alberta, participants in the energy-intensive oil sands developments have started to discuss the possibility of local nuclear power as a potential resource for the oil and gas exploration and refining sectors. However, the issues of nuclear waste management, siting, and technology (Canada's own heavy-water CANDU versus a light-water model from AREVA or another competitor) remain open.

Furthermore, federal government musings about the possible privatisation of the government-owned Atomic Energy of Canada Ltd, the developer of CANDU, have triggered much speculation about the future of nuclear power in Canada.

East-west transmission grid

As previously stated, Canadian provinces are interconnected more on a north-south basis with their American neighbours than on an east-west basis with other Canadian provinces. This is because of the geographic proximity of most of Canada's loads to the US border, compared to the vast distances between provinces. Several provinces, however, including Manitoba, Ontario, Quebec and Newfoundland & Labrador, have been promoting the idea of strengthening the east-west grid capacity to connect provinces. This trend owes its emergence to proposals to build major hydroelectric facilities in Manitoba (Conawapa) and Labrador (Lower Churchill River). Ontario, in the midst of closing its coal-fired generating stations, is eager to acquire the clean supply from both projects, but thousands of kilometres of new transmission lines would be required. Quebec, located between Labrador and Ontario, is eager to resume its role of middleman and agree to wheel the power through its territory from source to load, for a price. Manitoba and Labrador are obviously eager to develop the projects and sell the power. The costs of transmission are significant, however, and therefore the provinces are now promoting nationalist arguments in order to convince the federal government to provide funding.

sanctions, including fines, prohibition orders and revocations of the ability to participate in the electricity industry. The available remedy depends on the nature of the act, the legislation and the manner in which the regulator opts to pursue the offending party.

International

26 Are there any special requirements or limitations on acquisitions of interests in the electricity sector by foreign companies?

As noted above, certain acquisitions by non-Canadians are reviewable under the Investment Canada Act and subject to

McMILLAN BINCH MENDELSON

Mike Richmond
Chris Germanakos

mike.richmond@mcmbm.com
chris.germanakos@mcmbm.com

Brookfield Place, Suite 4400
Bay Wellington Tower, 181 Bay Street
Toronto, Ontario, M5J 2T3
Canada
Tel: +1 416 865 7000
Fax: +1 416 865 7048
www.mcmbm.com

1000 Sherbrooke Street West
Suite 2700
Montreal, Quebec, H3A 3G4
Canada
Tel: +1 514-987 5000
Fax: +1 514 987 1213

approval by the federal minister of industry. Transactions below the applicable monetary thresholds are subject to a tick-box notification process that may be completed post-closing. If a transaction is reviewable, the purchaser may be prohibited from acquiring, required to divest, or asked to provide undertakings in respect of, the Canadian business if the Minister is not satisfied that the acquisition is likely to be of net benefit to Canada.

The provincial electricity legislation that provides the regulatory scheme may also include restrictions on foreign ownership. Ontario, British Columbia and Quebec do not restrict foreign ownership. Alberta prohibits a municipality from granting rights to any person beyond the jurisdiction of Alberta unless that person agrees to submit to the jurisdiction of the EUB.

27 What rules apply to cross-border electricity supply, especially interconnection issues?

Cross-border movement of electricity is common, with most provinces having interconnections with neighbouring states in the US. The NEB must grant a permit or licence to a company that intends to export electricity to the US. Licences and permits may be issued for as long as 30 years but are generally issued for 10 years. Provincial requirements may also govern exporting electricity, including registering with the market operator. In Quebec, the provincial government may authorise the exports of HQ. In addition, the operation of the grid generally must meet certain standards established by the organisation of system operators (ie, NERC).

The construction of a new interconnection is subject to the approval of the NEB. A corresponding application for the construction on the US-side would be required from FERC.

Transactions between affiliates

28 What restrictions exist on transactions between electricity utilities and their affiliates?

Restrictions on agreements between affiliates may be found in regulations or codes of conduct and the particular restrictions vary by jurisdiction. Generally, the restrictions are intended to prevent regulated utilities from using their monopoly position to benefit non-regulated affiliates or prevent the regulated company from cross-subsidising non-regulated activities of the affiliate, thereby providing it with a competitive advantage.

29 Who enforces the restrictions on utilities dealing with affiliates and what are the sanctions for non-compliance?

Generally, the provincial regulator, such as the OEB or Régie, or the market surveillance administrator, enforces the affiliate restrictions. The Régie reviews specific contracts where HQ or one of its affiliates is the only or lowest tender. Sanctions include penalties, fines and the ability to reject commercial agreements and include only prudently incurred costs in the regulated utility's tariffs.