

WHAT THE NEW DOUG FORD GOVERNMENT MEANS FOR THE ENERGY SECTOR – A DETAILED ANALYSIS

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With a new majority provincial government now fully in control of Ontario's policy landscape, McMillan LLP and McMillan Policy Vantage Group are pleased to provide their insight into what lies ahead for clients and investors in the Energy sector.

The New Energy Minister

Ontario's new Minister of Energy already has significant experience with the job ahead, having served in the equivalent federal portfolio in the Cabinet of former Prime Minister Stephen Harper. In that role, Hon. Greg Rickford would have engaged somewhat more on the oil and gas file than the electricity file, but having been responsible for the National Energy Board, he will be very familiar with the nuances of managing a regulated portfolio, and a regulator.

Minister Rickford is the MPP for Kenora-Rainy River, the most northerly of the PC Party's 76 ridings. He is also among the most educated, holding a nursing diploma from Mohawk College, a Bachelor of Science degree from Victoria University, civil and common law degrees from McGill University, and an MBA from Université Laval.

Working as a nurse early in his career, Mr. Rickford was stationed in remote First Nations communities across Northern Ontario. He continued to work with Indigenous groups in the north as a lawyer, and later as the federal MP.

The fact that Minister Rickford is one of only three members of the Ford executive with any Cabinet-level experience at all will serve him well, as he assumes the responsibilities previously carried by no less than three of his Liberal predecessors; in addition to Energy, he also serves as Minister of Northern Development, Mines, and Indigenous Affairs.

Parliamentary Assistants

Supporting Minister Rickford as Parliamentary Assistant for Energy will be his former colleague from Parliament Hill, Paul Calandra. Both Rickford and Calandra were MPs in Ottawa from 2008-2015. Calandra, the

newly-elected MPP for Markham-Stouffville, had a career in the insurance sector, prior to serving as Chief of Staff to MPP Steve Gilchrist in the Mike Harris era. While an MP, he served as Parliamentary Secretary to the Prime Minister.

Rickford will also be supported by Ross Romano, the MPP for Sault Ste. Marie, who will serve as Parliamentary Assistant for the Northern Development, Mines and Indigenous Affairs portfolios.

PC Party Election Platform on Energy

Premier Doug Ford ran and won on a platform labeled *For the People: A Plan for Ontario*. The platform set out Ford's energy plan, in its entirety, as follows:

We will:

- Clean up the Hydro Mess and fire the board of Hydro One and its \$6-million-dollar CEO. Our first act will be to end the Liberal practice of making millionaires from your hydro bills!
- Stop sweetheart deals by scrapping the *Green Energy Act*.
- Cut hydro rates by 12% for families, farmers, and small businesses by:
 - Returning Hydro One dividend payments to families.
 - Stopping the Liberal practice of burying the price tag for conservation programs in your hydro bills and instead pay for these programs out of general government revenue.
 - Cancel energy contracts that are in the pre-construction phase and re-negotiate other energy contracts.
 - Declare a moratorium on new energy contracts.
- Eliminate enormous salaries at Ontario Power Generation and Hydro One.
- Stabilize industrial hydro rates through a package of aggressive reforms.

What this will cost:

Hydro One Dividend - \$300-\$400 million per year.

Moving Conservation Programs to Tax Base - \$433 million per year.

What this may mean for Pre-NTP Projects

Developers, lenders, construction firms, installers, landlords and other clients with interests in contracts for projects which have not yet been granted Notice to Proceed (*NTP*) by the Independent Electricity System Operator (*IESO*) (or acceptance of Key Development Milestones for Large Renewable Procurement (*LRP I*) projects) have reason to be concerned.

While the platform was not long on detail, it was absolutely clear that where pre-construction contracts contain provisions allowing the IESO to terminate at or prior to NTP or other equivalent milestones, before expensive capital equipment has been delivered and installed, the Government will be directing the IESO to exercise those termination rights.

Anticipating such a directive, the IESO had already begun holding back on the issuance of NTP approvals for Feed-In Tariff (*FIT*) projects prior to the June 29 swearing-in, instead electing to issue NTP Deferral Notices. By doing so, the IESO is able to limit its liability for the eventual termination of those projects to the “Pre-Construction Liability Limit”, which is set at:

- \$400,000 plus \$2.00/kW for wind, biogas or biomass facilities;
- \$250,000 plus \$10.00/kW for solar facilities; or
- \$500,000 plus \$20.00/kW for waterpower facilities.

These figures only represent liability caps. To be eligible even for these amounts, developers will have to be able to demonstrate that they incurred, after being awarded a FIT Contract, “soft” costs up to these amount for items such as environmental approvals, EPC and financing contract negotiations, land rights, resource assessments, connection cost deposits, equipment deposits and permitting. Costs spent on generating equipment (other than reasonable non-refundable deposits), and amounts representing lost profits, are not eligible.

Clients are advised to ensure that their contractual arrangements and invoicing documentation properly reflect the expenditure of such costs by the appropriate entities.

Counterparties to project developers, including suppliers, contractors, landlords and lenders, who have expended funds or incurred liabilities in order to be able to fulfill their obligations to project owners, may see their ability to recover limited to whatever contractual rights they had managed to negotiate. Even if those rights are well documented, such entities could find themselves unable to collect from a FIT or LRP developer that has essentially been shuttered. They are advised to ensure that any collateral security or bonding they may be entitled to is in hand, up to date, and to the extent possible, liquid.

What this may mean for Pre-COD Projects

Developers, lenders, construction firms, installers, landlords and other clients with interests in projects which are under construction but have not yet reached commercial operation (*COD*) should also take note.

While the FIT 1, FIT 2 and FIT 3 contracts did not permit the IESO to unilaterally terminate once NTP was issued, the FIT 4, FIT 5 and LRP I contracts all allow for an “optional” or “voluntary” termination by the IESO at any time prior to COD.

The termination payments due from the IESO for such terminations are significantly more extensive (while still only designed to make developers whole for their out-of-pocket expenses, not to compensate for loss of the project), but are equally contingent on contractual arrangements and invoicing documentation properly reflecting the expenditure of such costs by the appropriate entities, and being able to demonstrate that reasonable steps were taken to mitigate such losses.

Counterparties to project developers again have no direct right to any IESO funds. Supplier contract default provisions, security and bonding terms, and lien registrations may prove critical. However, at the end of the day, protecting rights through insolvency proceedings may be unavoidable.

In both Pre-NTP and Pre-COD termination cases, compensation assumes that the IESO will not default, or be directed to default, on its own obligations to pay termination fees. While sector participants have generally taken it as a given that this agency established by the Ontario legislature will honour its commitments, it is interesting to note that (i) the IESO has never posted any kind of security to support its obligation to pay termination payments, and (ii) Section 8 of the Electricity Act, 1998, quite explicitly states that “*The IESO is not an agent of the Crown for any purpose, despite the Crown Agency Act*”, which means the Government of Ontario, and more importantly the Ontario Treasury, do not necessarily stand behind the IESO’s obligations.

In any event, for projects which are close to commissioning, developers and all of their counterparties are significantly incentivized to accelerate final work cooperatively in an attempt to declare COD and submit all requisite COD paperwork – which should be 100% complete and accurate – before the IESO has a chance to issue a Termination or Stop Work Notice.

What this may mean for Post-COD Operating Projects

While FIT and LRP I projects which are already in operation are safe from unilateral termination (subject to any legislative or regulatory changes which drastically depart from the PC Party platform), owners and operators should become more vigilant about their contract compliance.

All of the contracts contain provisions allowing the IESO to terminate if the Supplier is in default, and the new Government has indicated that it plans to take advantage of those provisions wherever possible.

Based on the more detailed policy positions and resolutions adopted by the PC Party’s Policy Committee in 2017, we could expect that in such cases, project owners may be presented with a lose-lose choice: agree to re-open and renegotiate your FIT, LRP or other contract (terms to be revisited could include contract price, contract duration, and/or curtailment payments), or face immediate termination without any compensation.

There are plenty of seemingly innocuous actions and omissions which could trigger such a situation. They include missed milestone dates (do not expect deadlines to be extended going forward), reporting deficiencies,

and prohibited changes to the facility without consent. But inadvertent failures to maintain corporate records, minor changes to corporate ownership, corporate by-law discrepancies, threatened litigation, changes in residency, loss of licenses or permits, and a host of other fairly routine lapses could also lead to these significant consequences.

What this may mean for Nuclear Refurbishment Projects

Technically, the written pledge to cancel all pre-construction energy project contracts and re-negotiate others could equally apply to Ontario's nuclear refurbishment projects, particularly given the relative scope of the budget for such projects as compared to FIT and LRP projects.

Within days after the election, then Premier-Designate Ford declared both in a speech and in writing that the Pickering Nuclear Generating Station would remain open until 2024 (presumably subject to concurrence by the Canadian Nuclear Safety Commission, which would have to extend the current license beyond September 1, 2018). No mention was made of the Darlington or Bruce refurbishment programs, however.

The Refurbishment Implementation Agreement for Bruce includes a number of explicit off-ramps, including in cases where the IESO simply determines that the capacity is no longer needed. Bruce Power and those associated with the project will want to ensure that this conclusion is not reached by the IESO or the new Minister to which it reports, or alternatively that the costs of using such an off-ramp become prohibitively high.

What this may mean for Conservation Programs and Projects

The PC Party election plan did not call for the termination of conservation programs; it merely called for them to be funded by the Government from general tax revenues rather than by electricity customers on their hydro bills.

That said, the elimination of cap and trade and the dismissal of any carbon tax replacement means that the general revenues which might have continued to fund such programs will no longer be available. As a result, any continued funding of conservation programs would have to come at the expense of funding for other general government spending, such as health care, infrastructure, child care or education.

It is not surprising, therefore, that as a first step, the web site for the Province's Green Ontario Fund (*GreenON*) was recently changed to state that that all of the GreenON residential and commercial programs are now closed.

What this may mean for Utility Mergers

The Ford Government will be actively looking for, and promoting, any undertaking which is likely, or guaranteed, to lead to a reduction in customer's hydro bills or rates in the short term.

To the extent that merging utilities can identify efficiencies and savings from business combinations, and to the extent that those savings are committed through OEB proceedings to being passed through to customers through rate reductions – at least in the short term (until after the next election) and at least for the customers of one of the affected utilities – there would appear to be little reason to for the new Government to stand in the way of any proposed transactions.

Proponent utilities will want to consider what form they are prepared to have such assurances take.

What this may mean for Innovators

The new Ontario Government can be expected to test all proposals, pitches and policies against the following measures:

1. Is it “For the People”, in that the benefits (financial or otherwise) can be enjoyed by large segments of the population?
2. Does it make life more affordable, by reducing costs, reducing spending, reducing fees or charges, or reducing consumption?
3. Are the benefits realized in the short term, such that they will be visible or realized, at least in part, prior to the 2022 provincial election? This is not to say that the Government will avoid any long-term projects, but merely that, as with any Party subject to a 4-year election cycle, it is always more attractive to engage in matters where credit will accrue to the Leader who actually made the decision to implement, rather than to his or her successor.

Anyone seeking an audience with any official, whether in the Ministry of Energy or elsewhere, to pitch a program, policy or proposal, should be sure to tailor their submissions accordingly.

What this may mean for the Ontario Energy Board

Regardless of what programs, incentives or policies the Government of Ontario may adopt, at the end of the day, electricity rates remain within the exclusive control of the Ontario Energy Board (OEB). Regardless of what efficiencies are found, distribution and transmission rates will not decline unless and until the OEB approves or demands a rate reduction. Similarly, generation and capacity charges are predominantly recovered through the Global Adjustment Mechanism – which is in theory subject to OEB approval – rather than market mechanisms.

Membership, staffing, processes, procedures and modernization will all be viewed through this lens. To the extent that the current OEB structure, personnel and processes fail to deliver lower bills for customers, one should expect material changes, whether through Ministerial Directive or regulatory or legislative amendment.

What happens next

Big changes are afoot in Ontario's energy sector. Miscues, mismanagement and skyrocketing hydro bills were major factors in the demise of the prior Liberal government and the rise of the new PC-dominated legislature. Electricity in particular was a main focus for candidates and voters not only during the campaign, but also in the three years preceding it. Premier Ford and Minister Rickford will be under significant pressure to take immediate remedial action, and to be seen to be doing so.

Government actions which are both substantial and speedy can have material impacts on industry players. Those impacts can be negative or positive. Sector participants are urged to reach out to their McMillan LLP or McMillan Vantage Policy Group contacts for expert advice and guidance to ensure that those positive impacts are maximized, and negative impacts mitigated.

by Mike Richmond

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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