

Ontario's Power Trip: Still stranded after all these years

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Stranded debt of Ontario Hydro remains \$27.6-billion

By Parker Gallant

In 1998, as Ontario Hydro faced the equivalent of bankruptcy, the provincial power utility was split into four major entities. There was a generating company, a transmission company and a market operator. The fourth company was an outfit called Ontario Electricity Financial Corporation (OEFC). It was formed to hold the “stranded debt” left behind after the breakup and restructuring of Ontario Hydro. OEFC also took on additional debt related to what the province held as equity (\$8.9-billion) in the newly formed companies, including Ontario Power Generation (OPG) and Hydro One, the distribution company. OEFC also took on financial responsibility for so-called NUG (as in bug) contracts, long-term deals with private non-utility generating firms that received preferential long-term contracts to supply power at above-market rates.

OEFC, in other words, was an agglomeration of debts and money-losing operations. OEFC's first annual report — in March 31, 2000 — reported total debt of \$30.5-billion, money it technically owed to another branch of the government called the Ontario Finance Authority (OFA). OFA borrows the money on the market and funds the OEFC, which means Ontario taxpayers are liable for this debt.

Reading OEFC's first annual report gives you a warm and fuzzy feeling. It claimed two key guiding principles: “electricity prices are kept as low as possible” and “the commercial successor companies are provided with a solid financial footing and investment-grade capital structures.” The revenue and expense statement from this first report identified the sources of revenue and included the “debt retirement charge” found on Ontario electricity bills today, “payments-in-lieu-of taxes” from OEFC to the government, interest and also money collected to carry the cost of the money-losing deals for the NUG contracts and a nuclear power lease. In addition any profit from OPG and Hydro One in excess of the provincial interest carrying costs on the \$8.9-billion is also paid to OEFC.

First year revenue was \$3.3-billion. At the same time as its first annual report, OEFC issued a “Bulletin” which contained forward-looking information for 2001. It claimed a “projected cash surplus of \$1-billion in 2000-01.” So it looked like in the second year of operations it would reduce the debt by \$1.0-billion! So did OEFC meet their objective? On March 31, 2001, OEFC still owed \$30.5-billion despite revenue of \$3.7-billion for the year.

Fast forward to March 2005. OEFC had received revenue of \$20.5-billion and still owed \$27.7-billion. But the outlook for the next fiscal year contained a new item. “Providing financial assistance to the successor corporations of Ontario Hydro. Where required, the OEFC will facilitate the cash flow requirements of the successor corporations of Ontario Hydro.”

This new OEFC burden was the result of a new Ontario government initiative. In December 2004, the Dalton McGuinty Liberal government passed the Energy Restructuring Act and changed the landscape for OEFC. Suddenly the OEFC became bankers to OPG and the original principle of “investment-grade capital structures” was thrown in the trash bin. By March 31, 2009, OEFC had credit facilities established for OPG of \$1.45-billion and was reviewing an increase to handle the cost overrun of \$615-million for Big Becky — the Niagara tunnel. No need to be “investment grade” any more.

Since its formation, OEFC has received the staggering sum of \$36.3-billion from Ontario ratepayers. But the organization still owes the OFA \$27.6-billion. OEFC’s debt has declined by the princely sum of \$2.9- billion in the last 10 years. At that rate it will be 100 years before the old Ontario Hydro stranded debt is paid off.

However, now that OEFC has become the lender of last resort for the government-owned Ontario Power Generation. My guess is that OEFC may itself have to admit that its debt is stranded!

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Parker Gallant is a retired Canadian banker who began looking at his Ontario electricity bill and didn’t like what he was seeing.