



Backgrounder on PPAs and Balancing Pool Options March 31, 2016

1.0 Issue

The Independent Power Producers Society of Alberta (IPPSA) wishes to inform the discussion about the recent return of Power Purchase Arrangements (PPA) to the Balancing Pool.

The PPAs were integral to the province's move to restructure the electricity market beginning in the late 1990s¹. They were well contemplated, approved by the Energy and Utilities Board (EUB) and codified in legislation and regulation. They included rights and responsibilities associated with change in law issues, such as economic turnback of the PPA. This specific provision was supported by the government and approved by the EUB prior to the PPA sales to provide investor confidence as the PPAs went to market.

PPAs are legislative instruments that transferred the right to sell electricity from power plants that were built when the industry was regulated. They created PPA Owners, who are the original regulated utilities that built and still own and operate those power plants, and PPA Buyers, who are the investors that bought the rights to market the electricity from those plants.

PPAs were sold to Buyers during the Auction of 2000, the Market Achievement Plan of 2000, and the sale of the Sheerness PPA to TransCanada in 2005, among others. These three sales returned nearly **\$3 billion** to Alberta electricity consumers via monthly credits on power bills². This value was returned to ratepayers as the PPA Buyers saw incremental value above PPA costs. The Buyers were then free to market the output of the PPAs in Alberta's competitive electricity industry.

The PPAs worked, in concert with the market's restructuring, to:

- introduce new market participants at the dawn of Alberta's competitive electricity market,
- mitigate the market power that the incumbent utilities would have had in the new market,
- prevent the need of those utilities to forcibly divest their own assets,
- keep the Owners 'whole' for the costs calculated when the PPAs were determined and for the duration of the term of the PPA.

Alberta's competitive electricity market has been very successful and provided many benefits to electricity users, including:

- ensuring reliable supply of electricity for Albertans; against record growth in demand,
- introducing dozens of new power producers and the job creation that came with them,
- introducing competition and the downward pressure on electricity prices,
- alleviating the provincial government and ratepayers from the debt burden of new generation,
- introducing new choices for consumers in managing their power costs and enabling self-supply.

This document continues by providing further information on the PPAs, an overview of recent events and some concluding comments from IPPSA:

¹ http://www.aeso.ca/downloads/Path_to_Transformation

² Some \$4 billion has been returned to consumers since 2001 in total, with an additional \$1 billion from the profits earned by the Balancing Pool from sales of the unsold PPAs that it has retained. See balancingpool.ab.ca.

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2.0 Background

2.1 Nature of the PPAs

- The PPAs are included in legislation and regulations (and are **not** contracts). They comprise part of the legislative framework for Alberta's electricity market.
- The PPAs were approved by the Alberta Energy and Utilities Board following recommendations from the Independent Assessment Team in the late 1990s and were later codified in the Power Purchase Arrangement Determination Regulation (2000), the Electric Utilities Act (2003) and Power Purchase Arrangement Regulation (2003).
- This legislative framework establishes clear rights and obligations for Buyers, Owners, and the Balancing Pool in respect of the PPAs. These include:
 - The terms for both Owners and Buyers regarding financial payments, dispatch rights, operational control etc.
 - The terms under which Buyers can pursue termination, including change in law.
 - The terms under which the Balancing Pool can review and potentially dispute any termination claims.
 - The obligations for the Balancing Pool to fulfil all Buyer obligations and act as Buyer in respect of any unsold or Buyer-terminated PPAs, including payments to the Owners.

2.2 Recent Events

- The Balancing Pool has recently received notice that a number of Buyers are exercising their right to return the PPAs. Of note, these units are not being shut down as a result of these actions. (A schedule for their retirement is contemplated under the Federal Coal Regulation and most recently in Alberta's Climate Leadership Plan.)
- Those PPAs returned include Battle River #5 (368 Megawatts (MW)) from ENMAX, Sheerness (760 MW) and Sundance A (560 MW) from TransCanada, Sundance B (706 MW) from the ASTC Power Partnership (AltaGas Services and TransCanada) and Sundance C (710 MW) from Capital Power.
- At this point, one PPA remains with a Buyer; that is ENMAX's 762 MW from Keephills 1 & 2.
- With these decisions by the Buyers, the Balancing Pool may have nearly 4,000 MW of thermal PPAs, including the unsold Genesee 1 and 2 PPAs, under its management. The Balancing Pool also has a financial arrangement with TransAlta for its 800 MW hydro PPAs, which were excluded from the PPA Auctions.

2.3 Options Facing the Balancing Pool Options

- The legislative framework provides direction and options for the Balancing Pool with respect to its management of any unsold or terminated PPAs.
 - Dispatch the Unsold PPAs - The Balancing Pool "must manage generation assets in a commercial manner" in the Alberta electricity market, just like any other generator. The Balancing Pool will pay capacity and variable payments to the Owners, which were previously paid by the Buyers.
 - Sell the Unsold PPAs - The Balancing Pool can seek to auction off the PPAs in strips or through full PPAs sales, but the fair market value received through any sale *may* result in a loss.
 - Terminate the Unsold PPAs - The Balancing Pool can return the PPAs to the Owners with Net Book Value compensation calculated in accordance with the PPAs, and following consultation with consumer groups and the Minister and after providing six

months' notice to affected Owners. The Owners can then operate them as they choose adhering to the Federal and Provincial regulations/policies.

3.0 Impacts on the Market and Power Consumers

- IPPSA cannot speculate on the potential impact on the market and on consumers of the returning PPAs. This will ultimately be determined by decisions made by the Balancing Pool, including :
 - How it manages the PPAs, observing that - all else equal – historically low electricity prices reduce revenues to the Balancing Pool from the PPAs that it holds
 - Whether or not it sells some/all of the PPAs as strips/or full PPAs, and at what price.
 - Whether or not, and when, it may decide to terminate some/all PPAs in accordance with the terms of the PPAs, and the corresponding net book value amounts.
- Policy uncertainty impacts investor confidence and is therefore not in the long-term interest of consumers. Uncertainty regarding what the Balancing Pool will do with the PPAs in the near term will make it challenging for any company to invest in Alberta.
- Finally, changes in environmental costs and environmental policy will impact generators differently. As in any industry, costs imposed on producers need to be recovered from consumers or those producers exit the market.

IPPSA remains committed to working with policy makers and agencies to ensure a reliable, cost effective and environmentally responsible power market for the benefit of Albertans. IPPSA seeks to ensure that its members have the opportunity to earn a fair return on their investments.