GA Smoothing – OPG Accounting Considerations

- An SPV/Trust is a stand-alone entity able to conduct business separately under a Trust agreement

The conditions required for OPG to consolidate the SPV/Trust are outlined in the following table

Issue	Response
1. Decision Making	• OPG must have decision making authority on the operation of the SPV/Trust (without a veto right by the Province), including naming of trustees, establishing operating plans and budgets, setting or changing financing policies. • The SPV/Trust while operating within the legislation, must be controlled by OPG to operate freely and to alter terms and conditions not specified in the legislation to ensure recovery of the deferred amounts
2. Business Risk	• The SPV/Trust must have variability of returns as a normal business enterprise would, including such things as interest charged on deferred amounts, decisions on how to finance these deferred amounts, the ability to make / lose and keep any spread from financing
3. Funding	• The Province cannot directly or indirectly fund more than 50% of SPV/Trust or any investment in the SPV/Trust • OPG must own at least 50% of the most exposed equity /sub-debt in the SPV/Trust
4. Directive	• Directive that is issued should not be prescriptive or direct OPG to set up this business. The directive should only be “guiding” i.e. to allow OPG to evaluate options and put forward to the OPG Board a recommended plan for Shareholder approval

GA Smoothing – OPG Accounting Considerations - continued

Issue	Response
5. Other required Attributes:	The legislation that supports the formation of the SPV/Trust must have the following attributes: • Must require interest, carrying and administrative costs be paid to the Trust to allow for Revenue recognition • The amount to be deferred must either be specified or be calculated based on a specific formula that is not subject to ongoing decision making by the Province. **<u>The Province cannot have the ability to override this formula</u>** • Legislation should be written to avoid the possibility of being revoked with wording to ensure the SPV/Trust and its debt holders would have their capital guaranteed and paid for directly by the Province if such a situation were to happen • The spirit of the legislation should be reflected in the Trust Indenture Agreement

GA Financing Structure Requirements

KEY ELEMENTS REQUIRED TO ENSURE THE DEFERRAL OF GA CHARGES CAN BE FINANCED:

Creation of Strong Property Rights

- Legislation enshrines the ability of the IESO to create a Right to charge customers in the future for the Global Adjustment (GA) deferred today including principal amount deferred, interest and other financing costs on the amount deferred and fees, expenses and other administrative costs.
- The Right can be sold to an appropriate Trust or Special Purpose Vehicle (SPV) to obtain funds to pay amounts due to generators under contracts or regulation. These SPVs are generally single purpose entities with no other operations that could add risk to the entity, dilute debt holder rights, allow parties from other operations to claim rights to the future recovery from customers or allow these other parties to initiate bankruptcy proceedings.
- Right must be irrevocable and if the Right is amended by future governments the debt holders have the right of action against the government to recover the amount outstanding including interest, fees, expenses and any damages resulting from the amendment.
- Right must specify the recovery period or the mechanism for setting the recovery rate including true up of the rate to ensure all amounts are recovered

Economic Factors

- Limits on the recovery amount (principal, interest, fees and expenses) charged to customers in future periods must have compensating elements such as longer recovery period to ensure the full amount deferred plus interest, financing and other administration costs is recovered from customers.
- Need to balance customer relief with debt holder risk. Longer recovery periods and larger deferred balances increase risk to the debt holder of future government intervention.
- The amount required by the SPV to purchase and service the Right will be funded 51% from debt holders, 5% from OPG through capital markets and 44% from OPG via equity injection to OPG from the Province. The funding from OPG will be loaned to the SPV as subordinated debt.

GA Financing Structure Requirements - continued

- SPV will be used to raise the GA financing and ring fence OPG from its legal obligations
- SPV will be structured to allow for GBE accounting consolidation into OPG
- Given that SPV will be consolidated into OPG for accounting purposes, the significant amount of debt required to fund the GA deferral will have a severe impact on OPG's credit rating. If 100% of the requirement is funded by debt OPG would be downgraded.
- To manage this exposure and minimize the cost of funding. The required funding would be split into 2 buckets:
    1. 56% from capital markets, and
    2. The remainder provided by the Province via equity injection, which would be loaned to SPV as subordinated debt.
- The use of equity to fund a portion of the GA deferral also allows for an improvement in both Net Income and EBITDA as incremental revenue is captured by the increase in the value of the deferral which would offset the fiscal impact of the borrowing at Province level.
- Credit rating metrics are generally maintained within established limits.