CONFIDENTAL **April 18, 2017**

Ontario Power Generation

<u>Issue:</u> OPG has indicated that for the Trust to be consolidated into OPG there is a need to have at least 51% of the debt financing of the Trust originate directly from the external market. This requirement is supported by specific technical guidance on the topic as set out below.

IFRS 10 – Consolidated Financial Statements requires an investor to consider whether there are other parties who are acting on behalf of the investor by virtue of their relationship with it. That is, IFRS 10 requires consideration of whether the other parties (i.e. OPG) are acting as de facto agents for the investor (i.e. Province). If OPG is considered a de facto agent, the consolidation accounting objective will **<u>not</u>** be met.

There are a series of references in IFRS 10 (Section B75) that support this conclusion. Each of these elements must be examined in their totality to successfully address the consolidation principal of the Trust. The importance of each element is amplified due to the fact that OPG is a related party to the Province, which increases the importance of other tests being met. These tests include:

a) a party that received its interest in the investee as a contribution or loan from the investor.
OPG will receive a 44% equity injection from the Province of Ontario, indirectly through the Ontario Financing Authority. Given that currently, the <u>majority</u> (currently 51%) of the Trust debt will be from External Markets and not the Province, it can be argued that OPG did not receive the <u>majority</u> of its interest in the investee as a contribution or loan from the Province. This criterion is not met and shows that OPG is a principal, not a de-facto agent.

b) a party that has agreed not to sell, transfer or encumber its interests in the investee without the investor's prior approval
There is a proposed clause that the Trust cannot be wound up without approval from the Minister of Energy, this criterion is met.

c) a party that cannot finance its operations without subordinated financial support from the investor.
OPG can finance its operations without subordinated financial support from the Province – criterion is not met.

d) an investee for which the majority of the members of its governing body or for which its key management personnel are the same as those of the investor.
OPG is a related party of the Province of Ontario, therefore this criterion is met.

e) a party that has a close business relationship with the investor, such as the relationship between a professional service provider and one of its significant clients.
OPG is a related party of the Province of Ontario, therefore this criterion is met.

Given the number of factors met above, there may be a view that OPG could be considered a de facto agent of the Province through its related party relationship (4 out of 6 items are met). It is of vital importance, and as concurred by EY, that the majority of the debt in the Trust is not more than 44% funded by the Province (note that the remaining 5% of debt has to be funded externally by OPG in order to show that OPG has equity that is not sourced from the Province at risk). If the debt in the Trust is seen by the External Auditors as being principally funded by the Province, OPG would fail 5 out of 6 criteria above and be considered a de facto agent. As a result, proposed consolidation accounting would fail.