OEB IFRS Consultation

Conversion to International Financial Reporting Standards (IFRS)

August 22, 2008

Impact of IFRS on Regulation of OPG

- Current Application: Forecast cost of service basis, 21 month test period from April 1, 2008 to December 31, 2009.
- Next Application: Forecast cost of service basis, 2 year test period from January 1, 2010 to December 31, 2011.
- Basis of Next Application: 2009 to 2011 business plan, 2008 audited financial statements, OEB's decision on OPG's current payment amounts application.
- Development of the 2009-2011 business plan is underway based on Canadian GAAP. OPG has a project underway to identify and assess the impact of differences between Canadian GAAP and IFRS for IFRS adoption effective January 1, 2011. Areas with the highest potential to impact OPG's accounting identified thus far include rate regulated accounting, accounting for fixed assets, accounting for asset retirement obligation, and initial adoption of IFRS under the provisions of IFRS 1, *First-time Adoption of IFRS*.

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- Next Application expected to be submitted to OEB during the Spring of 2009. To the extent that the progress on the project allows OPG to quantify any material differences, OPG may present them in the Next Application.

- The implications of implementation of IFRS for OPG may need to be addressed by incorporating a deferral account in the OEB's payment order for OPG's Next Application, or through a separate application for either an accounting order or payment rider(s). OPG's subsequent payment amount application is expected to be filed in the Spring of 2011. It would be based on a business plan prepared under IFRS, include quantified impacts of transition to IFRS, and propose regulatory treatment of transition adjustments as well as disposition of accounting orders or deferral accounts, if any.

- OPG's 2011 audited financial statements prepared under IFRS will include comparative 2010 audited results under IFRS.

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Conversion to IFRS – Current Status

- Since completion of the diagnostic exercise in December 2007, OPG, upon engagement of an external accounting advisor, has focused its conversion effort on the assessment of differences between Canadian GAAP and IFRS and identification of potential resolutions to these differences, consultation with European utilities who have undergone the conversion, as well as training, communication and project management across the company. Preliminary IT system impact consideration has also commenced.

- At this point, there is a potential impact on OPG's financial statements in converting to IFRS. This impact could affect OPG's future rate filings, including the calculation of revenue requirement, as well as other aspects of OPG's business, including debt covenants and stakeholder impacts (e.g., credit rating agencies).

- OPG is currently targeting substantial completion of the IFRS conversion project by the end of 2009. Into early 2009, OPG's focus will be completing the detailed GAAP analysis on a financial statement component basis, identifying data requirements and system impacts for conversion, and beginning to implement a training plan for affected staff. OPG will continue the assessment of regulatory filing implications.

- OPG disclosed the status of its IFRS conversion project in its Q2 2008 MD&A and will continue to provide updates in subsequent quarterly and annual financial reports.

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Potential Accounting Issues Being Assessed

Regulatory Accounting:

- Currently, no IFRS standards specifically relate to rate regulated enterprises. Regulatory assets and liabilities must meet the criteria of an asset or liability under the IFRS conceptual framework in order to be recognized.
- Variance and deferral accounts may require separate tracking for regulatory purposes; potentially higher administrative costs for applicant; regulators may no longer be able to rely on auditor assurance over account balances if not reported on financial statements
- Effective January 1, 2009, under Canadian GAAP, a regulatory asset (liability) will be recognized by regulated entities, which recover income taxes on a “flow-through” basis, to the extent that future income tax liabilities (assets) recorded for accounting purposes are expected to be recovered from (refunded to) ratepayers in the future. IFRS provides no similar guidance.

Provisions:

- IFRS explicitly requires both legal and constructive provisions to be recognized
- Provisions are required to be reviewed at the end of each reporting period and adjusted to reflect the current best estimate, including changes in applicable discount rates for provisions (such as asset retirement obligations) recorded on a present-value basis, including upon initial adoption of IFRS

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Potential Accounting Issues Being Assessed

Property, Plant and Equipment (PP&E):

- Separate identification and measurement of individual components of larger fixed assets is explicitly required under IFRS
- Identified components are to be depreciated based on their individual useful lives; definition of what constitutes a "component" requires judgment
- IFRS provides an option to measure an item of PP&E at fair value upon transition
- Potential impact on rate base and depreciation expense post implementation

Initial Adoption of IFRS under IFRS 1:

- Opening balance sheet on transition to IFRS is to be prepared as though IFRS has always been applied with full retrospective application (subject to exceptions and exemptions)
- IFRS 1 provides mandatory *exceptions* and optional *exemptions* from full retrospective application (e.g., exemption to recognize all cumulative actuarial gains and losses related to defined benefit post-retirement plans in retained earnings upon IFRS adoption)
- Initial adoption may result in adjustments to assets and liabilities being recorded directly to retained earnings, as opposed to being recognized as costs in the income statement (and recovered in rates) over a number of periods. The recovery of any transition adjustments may need to be addressed by regulators, who would likely need to balance intergenerational equity and regulatory efficiency objectives.

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