

UNDERTAKING J10.9

Undertaking

To provide relevant documents on OPG's interpretation of accounting rules.

Response

Canadian Generally Accepted Accounting Principles ("GAAP") require entities to monitor depreciation life estimates on an on-going basis. The end-of-life dates for OPG's property, plant and equipment are impacted by a variety of factors including internal factors (such as station and unit condition, and OPG's operating strategy) and external factors (such as regulatory requirements, the Ontario electricity market, and decisions by the Province of Ontario and Government of Canada).

As discussed at Ex. F4-T1-S1, Attachment 1, pages 5 and 6, for financial accounting purposes, OPG's Depreciation Review Committee ("DRC") recommends changes to existing generation station end-of-life dates and asset class service lives if they have a high-degree of confidence regarding the need for the change, after considering internal and external factors.

Specifically, OPG's planning instructions for the DRC process state the following:

For financial statement purposes, changes to existing station service lives require a high degree of confidence when station service lives are being extended. Indicators of a high degree of confidence are as follows:

- External indicator such as shareholder directive or instruction from the CNSC.
- Explicit board [of directors] approval to proceed with a plant life extension e.g. refurbishment investment decision.
- Board [of Directors] approved business plan coupled with assurance that there is not a further assessment trigger that is ultimately required to demonstrate high confidence e.g. board [of directors] approved business plan to proceed with plant life extension but the ultimate extension is contingent on a successful technical assessment. Consideration should also be given to any required approvals from regulators such as the CNSC.

OPG's external auditors must be satisfied with the underlying support for the recommendations to change service lives. When considering any plant life extension, OPG should consider the risk of volatility resulting from frequent changes associated with service life estimates, as this would result in volatility in depreciation expense impact to the income statement and volatility in the Asset Retirement Obligation estimates.

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2 The planning instructions also specifically direct the DRC to consider internal factors:
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4 The DRC report and decision framework for station life will include
5 documentation of the principles used for station life assessment in the
6 context of: i) technical assessment of life limiting components; ii)
7 operating experiences; and iii) refurbishment plans.
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9 OPG also notes that the period over which the existing book values of a capital asset
10 and new capital expenditures on such an asset aimed at extending its life are
11 depreciated must be consistent with the accounting trigger for capitalization. The trigger
12 for capitalization is inherently predicated on having a high confidence in the success of
13 achieving the extended useful life of the existing asset. Therefore, the commencement of
14 capitalization of expenditures relating to a project such as Darlington Refurbishment and
15 the extension of the useful life of the underlying asset (in this case, the Darlington
16 Nuclear Generating Station) must, and did, occur in conjunction with each other.
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18 Provided below is OPG's interpretation of accounting rules regarding capitalization of
19 expenditures for long-term projects involving rehabilitation, improvement and
20 maintenance of existing assets, which is applicable to the case of the Darlington
21 Refurbishment project. The decision rule is designed to meet the requirements of
22 Canadian GAAP. OPG's capitalization methodology is also detailed at Ex. A2-T2-S1,
23 pages 5 - 7.
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- 25 • All costs incurred prior to the date of the selection of the alternative to
26 implement are charged to OM&A.
27
- 28 • Project development costs should be capitalized once the preferred
29 alternative for a new capital asset or capital improvement to an
30 existing asset is selected. This stage, normally known as the definition
31 phase, is the step where costs are better defined and the necessary
32 approvals are obtained.
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34 The application of OPG's interpretation of Canadian GAAP with respect to changes to
35 depreciation life estimates as well as capitalization criteria has been found to be
36 appropriate by OPG's external auditors and is reflected in OPG's consolidated financial
37 statements, on which the auditors opine in accordance with Generally Accepted Auditing
38 Standards. In the case of the Darlington Refurbishment project, OPG's external auditors
39 considered the change in the end-of-life date for the Darlington station and agreed that it
40 was appropriate having regard to the approval given by OPG's Board of Directors and
41 OPG's internal policies.