UNDERTAKING J2.7

Undertaking

To identify assets, liabilities, revenues, costs and other items set out in OPG's 2007 financial statements that are referred to in section 6 of regulation O. Reg. 53/05 for purposes of establishing payment amounts for the test period.

Response

Section 6 of O. Reg. 53/05 lists rules governing the determination of payment amounts by the Board. Sub sections 6.(2)5 and 6.(2)6 of the regulation state that in making the first payment order for OPG's prescribed facilities, the OEB shall accept the values in OPG's most recently audited financial statements. In addition, other parts of section 6 establish provisions for recovery of certain costs. OPG has prepared the attached schedule and notes which identify the items in the financial statements that are relevant to the revenue requirement in the test period, and must be accepted by the Board:

- Attachment 1, "Reliance on Audited Financial Statements," provides the names of the financial statement items that must be accepted, the financial statement note that contains values for the regulated operations that must be accepted, the dollar value that must be accepted for the regulated operations, and references to sections of the evidence that contain these figures.
- Attachment 2 contains notes that explain how the figures in the financial statements are used in the evidence, as well as references to sections of O. Reg. 53/05 that specify the methodology for determining payment amounts.
- Attachment 3 provides photocopies of OPG's audited financial statements as found in Ex. A2-T1-S1 Appendix A with the relevant numbers marked for ease of reference.

It is OPG's position that the Board must accept the regulated income and balance sheet amounts as reported in the attached schedule and notes.

RELIANCE ON AUDITED FINANCIAL STATEMENTS

Reliance on Audited Financial Statements (millions of dollars except where noted)	Ref *	**2007** F/S Reference	**2007** Regulated amount	Exhibits that rely on s6.2(5)* "Board shall accept amounts…in OPG's most recently audited financial statements…"
Income before interest and income taxes	A	Note 18	165	Historic ROE in Ex. C and determination of Income Tax Losses Ex. F3-T2-S1
Assets				
Fuel inventory	B	Note 18	231	Rate Base Ex. B (opening working capital balance in test period)
Materials and supplies - current assets	B	Note 18	74	Rate Base Ex. B (opening working capital balance in test period)
Long-term materials and supplies	B	Note 18	346	Rate Base Ex. B (opening working capital balance in test period)
		Total M&S	420	
Fixed assets in service, net	B	NBV Note 18	7,901	Rate Base Ex. B (in service assets excluding CIP). Fixed assets also include Asset Retirement Costs which represent costs to be recovered for decommissioning nuclear stations, and managing and disposing of used fuel, and low and intermediate level waste.
Construction work in progress	C	Note 18	509	CIP results in, in service addtions to test period rate base, as well as into future periods.
Regulatory assets:	F	Note 7		
Pickering A return to service costs			183	Variance/Deferral Ex. J
Nuclear liabilities deferral account			131	Variance/Deferral Ex. J
Nuclear development deferral costs and capacity			28	Variance/Deferral Ex. J
refurbishment variance				Variance/Deferral Ex. J
Hydroelectric production variance			7	Variance/Deferral Ex. J
Ancillary service revenue variance (Nuclear and Hydroelectric)			5	Variance/Deferral Ex. J
Transmission outages and transmission restrictions			2	Variance/Deferral Ex. J
		Total	356	
Liabilities				
Long-term debt due within one year	D	Note 9	400	Cost of capital Ex. C1-T1-S2 (determination of deemed interest expense in test period).
Long-term debt	D	Note 9	3,665	Cost of capital Ex. C1-T1-S2 (determination of deemed interest expense in test period).
Deferred revenue due within one year	E	Balance	12	Historic ROE and Bruce lease revenue in test period Ex. G2-T2-S2.
Deferred revenue	E	Sheet	120	Historic ROE and Bruce lease revenue in test period Ex. G2-T2-S2.
Regulatory liabilities: Other	F	Note 7	14	Variance/Deferral Ex. J

***** refers to paragraphs in Attachment 2

Notes

A. Income before interest and income taxes

Income before interest and income taxes for the regulated operations of $165M as per Note 18 of the 2007 audited financial statements (earnings of $249M for regulated hydroelectric and a loss of $84M for nuclear) is reported as Accounting EBIT on Line 1 of Ex. C1-T2-S1 Table 1. After making certain adjustments to reflect regulatory treatments, which are also described in this exhibit, the resulting regulatory earnings before tax (EBT) is calculated and reported on Line 14 as a loss of $84M. This regulatory EBT becomes the starting point for the calculation of regulatory income taxes at Line 1 of Ex. F3-T2-S1 Table 7.

B. Fuel Inventory, Materials and Supplies, and Fixed Assets

Fuel inventory for OPG's regulated operations is $231 million as per Note 18. This is reported as a closing balance of $233.0M on line 10 of Ex. B3-T6-S1 Table 1. The difference of $2M is due to rounding.

The sum of the short term and long term materials and supplies as per Note 18 is $419M for nuclear and $1M for regulated hydroelectric. The nuclear materials and supplies is reported as a closing balance of $418.4M on line 11 of Ex. B3-T6-S1 Table 1 and the regulated hydroelectric amount is reported as a closing balance of $0.6M on line 11 of Ex. B2-T6-S1 Table 1. The differences are due to rounding.

The **net** segment fixed assets in service as per Note 18 is $4,030M for nuclear and $3,871M for regulated hydroelectric. These are reported as follows:

	$M	Evidence reference
Nuclear		
property, plant and equipment	4,418.8	Ex. B3-T3-S1 Table 1 line 15, column (e)
accumulated depreciation	(1,593.2)	Ex. B3-T5-S1 Table 1 line 15, column (d)
net fixed assets	2,825.6	
Bruce		
property, plant and equipment		
accumulated depreciation		
net fixed assets	1,194.6	Ex. G2-T2-S1 Table 2 line 2, column (c)
Total net fixed assets per Evidence	4,020.2	
Total net fixed assets per Note 18	4,030.0	
difference	9.8	

The difference of $9.8M is noted on Chart 1 in Ex. B1-T1-S1 on page 8.

	$M	Evidence reference
Regulated Hydroelectric		
property, plant and equipment	4,410.1	Ex. B2-T3-S1 Table 1 line 9, column (e)
accumulated depreciation	(538.8)	Ex. B2-T5-S1 Table 1 line 9, column (d)
net fixed assets	3,871.3	
Total net fixed assets per Note 18	3,871.0	
difference	(.3)	

The difference is due to rounding.

Acceptance of the balances in Note 18, as described above, also leads to acceptance of the 2007 rate base (except for the cash working capital balance, which is based on a lead lag study, rather than the audited financial statements,). The 2008 rate base uses the average of the 2007 audited balances and the 2008 amounts. Similarly, the 2009 rate base is an average of the 2008 and 2009 fixed assets, and the portion of the 2008 rate base that relates to the 2007 audited fixed assets, also flow through to the 2009 rate base.

C Construction in Process (CIP)

The CIP balance as per Note 18 is $210 million for Nuclear and $299 million for regulated hydroelectric for a total of $509 million. The 2007 closing balances are expected to be placed in service in the test period and future years. Acceptance of these balances leads to acceptance of rate base additions in the test period, or the period in which these additions are placed in service. Since CIP is excluded from the rate base, continuity schedules are not provided in the evidence.

D Debt

Long term debt as reported in Note 9 of the 2007 audited financial statements can be summarized as.

	$M
Long-term debt (notes payable to OEFC)	3,665
Long-term debt due within 1 year	400
Less unregulated portion[1]	(230)
Total	3,835

[1] Unregulated portion of debt is for non prescribed facilities, Lac Seul ($20M) and Portlands Energy Centre ($210M).

Long term debt is used in the calculation OPG's cost of capital in Ex. C.

The long term debt of $3,835M reported as follows in the evidence:

		$M
Ex. C1-T2-S2 Table 3	lines 4 - 17	2,495
Ex. C1-T2-S2 Table 3b	Notes 1 to 4b	1,100
Ex. C1-T2-S2 Table 3	line 23	160
Ex. C1-T2-S2 Table 3b	Note 5 and next	80
	Total	3,835

E Deferred Revenue

Deferred revenue as reported in the 2007 audited financial statements.

	$M
Deferred Revenue due within 1 year	12
Deferred revenue (long term)	120
Total	132

Deferred Revenue represents prepaid rent from the lease of the Bruce generating stations to Bruce Power L.P in 2001 and the balance remaining as of December 31, 2007 is $132M. The annual amortization of $12M is reported as $11.7M on G2-T2-S1 Table 1 line 8 for 2007, 2008 and 2009.

F Regulatory Assets and Liabilities

Section 6(2)5 of the regulation states that the Board shall accept the asset and liability balances recorded in OPG's 2007 audited financial statements. This clause applies to OPG's regulatory assets and liabilities, subject to certain conditions regarding recovery of costs in section 6 of the regulation. OPG has recorded regulatory assets and liabilities for both deferral and variance accounts in its financial statements. Section 6(2)5(i) specifically excludes variance accounts referred to in subsection 5(1), and therefore section 6(2)5 only applies to regulatory assets for deferral accounts, and does not apply to variance accounts that are established under section 5 of the regulation.

OPG's regulatory liability ($14M) as disclosed in Note 7 to the 2007 audited financial statements relates to the segregated mode of operations and water transactions variance account. This variance account was not established by section 5 of the regulation; therefore, the balance in this account should be accepted as reported in the audited financial statements as adjusted by Ex. G1-T1-S3. This adjustment for

$3.3M, which increases the regulatory liability in OPG's evidence, was made in May 2008 and therefore, is not reflected in the 2007 audited financial statements.

The chart below provides a comparison of the amounts in the financial statements for each regulatory asset as well as a reference to Exhibit J, which also includes these figures. The figures in the financial statements are equal to the amounts in the exhibits, with the exception of the Pickering A Return to Service (PARTS) Deferral Account, for which there is a $0.8M difference due to rounding in the financial statements. In addition, the nuclear generation development costs deferral account in the financial statements includes both nuclear development costs and capacity refurbishment costs which total $28M. The amounts for these two accounts are disclosed separately in Exhibit J1 as shown below ($11.7M for nuclear development and $16.2M for capacity refurbishment, for a total of $27.9M). Section 6(2)5 applies to the total cost of $28M in this account, including the capacity refurbishment variance account. The capacity refurbishment variance account was established under section 6(2)4(i) and not section 5 of the regulation and therefore is not excluded from the requirements of section 6(2)5.

Deferral Account	F/S ($M)	Evidence ($M)	Evidence Reference	Section of O.Reg. 53/05 that regulates recovery
PARTS	183	183.8	J1-T1-S1 Table 4, line 1	S6(2)3
Nuclear Liability	131	130.5	J1-T1-S1 Table 4, line 2	S6(2)7
Nuclear Generation Development Costs	28	11.7 Nuclear development	J1-T1-S1 Table 4, line 3	S6(2)4.1
		16.2 Capacity refurbishment variance account	J1-T1-S1 Table 4, line 3	S6(2)4(i)

Approval for any restructuring is required by note holders representing not less than 66 and two-thirds of the value of the Trusts.

OPG performed a valuation analysis as at December 31, 2007 to assess the amount of any impairment, taking into account the limited information available. The assessment considered the likelihood of achieving a successful restructuring based on the current proposal announced on December 23, 2007. OPG used a probability weighted cash flow model to determine the fair value of its third-party ABCP holdings. Since the majority of OPG's remaining ABCP is made up of combined traditional and synthetic assets such as Collateralized Debt Obligations ("CDO's"), the recoverability was estimated to be 85 per cent. An insignificant amount of OPG's remaining third-party ABCP is made up of ineligible assets, where the underlying assets or the collateral provided is supported by United States ("U.S.") sub-prime assets. The recoverability of these ineligible assets was estimated to be 70 per cent. OPG also considered alternative methods to assess the fair value of the investments. As a result of the analysis, OPG recorded an impairment loss of $9 million against the remaining holdings of $58 million, in addition to the $1 million loss related to the Skeena investments. The impairment loss is included in other gains and losses.

OPG reviewed the classification of its third-party ABCP holdings and has determined that a long-term classification is appropriate, based on the restructuring information available. OPG will continue to monitor developments with respect to ABCP and will continue to assess its position.

OPG has sufficient credit facilities to satisfy its financial obligations as they come due and does not expect any material adverse impact on its operations as a result of this current third-party ABCP liquidity issue.

7. Regulatory Assets and Liabilities and Summary of Rate Regulated Accounting

The regulatory assets and liabilities as at December 31, 2007 and 2006 are as follows:

(millions of dollars)	**2007**	**2006**
Regulatory assets		
Pickering A return to service costs	**183**	249
Nuclear liabilities deferral account	**131**	-
Nuclear generation development costs	**28**	-
Hydroelectric production variance	**7**	-
Ancillary service revenue variance	**5**	-
Transmission outages and transmission restrictions variance	**2**	2
Total regulatory assets	**356**	251
Regulatory liabilities		
Hydroelectric production variance	**-**	4
Other	**14**	7
Total regulatory liabilities	**14**	11

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9. Long-Term Debt

Long-term debt consists of the following:

(millions of dollars)	2007	2006
Notes payable to the OEFC	3,665	3,165
Share of non-recourse limited partnership debt	**188**	194
	3,853	3,359
Less: due within one year		
Notes payable to the OEFC	400	400
Share of limited partnership debt	7	6
	407	406
Long-term debt	**3,446**	2,953

Holders of the senior debt are entitled to receive, in full, amounts owing in respect of the senior debt before holders of the subordinated debt are entitled to receive any payments. The OEFC currently holds all of OPG's outstanding senior and subordinated notes.

The maturity dates as at December 31, 2007 for notes payable to the OEFC are as follows:

		Principal Outstanding *(millions of dollars)*		
Year of Maturity	**Interest Rate (%)**	**Senior Notes**	**Subordinated Notes**	**Total**
2008	5.90%	400	-	400
2009	6.01%	350	-	350
2010	6.00%	595	375	970
2011	6.65%	-	375	375
2012	5.72%	400	-	400
2016	4.91%	270	-	270
2017	5.35%	900	-	900
		2,915	750	3,665

In September 2005, OPG reached an agreement with the OEFC to provide debt financing for the Niagara Tunnel project. The funding, which is up to $1 billion over the duration of the project, will be in the form of 10-year notes, which will be issued quarterly to meet the project's obligations. Interest will be fixed for each note issued at the time of advance at a rate equal to the prevailing Benchmark Government of Canada 10-Year Bond, plus a credit spread determined by the OEFC based on a survey of market rates. As at December 31, 2007, OPG issued $240 million against this facility, which included new borrowing of $80 million under the facility in 2007. In January 2008, $40 million of new borrowing was issued under the facility.

In December 2006, OPG reached an agreement with the OEFC to provide debt financing for the Lac Seul Hydroelectric Generating Station and the Portlands Energy Centre projects. There will be up to $50 million available for the Lac Seul project and up to $400 million available for the Portlands Energy Centre project under each credit facility. The credit facilities will be drawn as needed to fund the respective projects over the construction period. The funding will be in the form of 10-year notes with interest rates fixed for each note issued at the time of advance at a rate equal to the prevailing Benchmark Government of Canada 10-Year Bond, plus a credit spread determined by the OEFC based on a survey of market rates. As at December 31, 2007, OPG issued $20 million against the Lac Seul project credit facility and $210 million against the Portlands Energy Centre credit facility, which included new borrowing of $120 million under the Portlands Energy Centre facility in 2007. In January 2008, $35 million of new borrowing was issued under the Portlands Energy Centre facility.

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Excerpt from Ex. A2-T1-S1 Appendix A

Segment (Loss) Income for the Year Ended December 31, 2007	**Regulated**		**Unregulated**			
	Nuclear	**Hydro-electric**	**Hydro-electric**	**Fossil-Fuelled**	**Other**	**Total**
(millions of dollars)						
Revenue	**2,581**	**695**	**763**	**1,713**	**135**	**5,887**
Revenue limit rebate	**-**	**-**	**(64)**	**(163)**	**-**	**(227)**
	2,581	**695**	**699**	**1,550**	**135**	**5,660**
Fuel expense	**133**	**244**	**81**	**812**	**-**	**1,270**
Gross margin	**2,448**	**451**	**618**	**738**	**135**	**4,390**
Operations, maintenance and administration	**2,061**	**123**	**207**	**573**	**10**	**2,974**
Depreciation and amortization	**426**	**68**	**68**	**82**	**51**	**695**
Accretion on fixed asset removal and nuclear waste management liabilities	**499**	**-**	**-**	**8**	**-**	**507**
Earnings on nuclear fixed asset removal and nuclear waste management funds	**(481)**	**-**	**-**	**-**	**-**	**(481)**
Property and capital taxes	**31**	**11**	**10**	**21**	**12**	**85**
(Loss) income before other gains and losses	**(88)**	**249**	**333**	**54**	**62**	**610**
Other (gains) and losses *(Note 17)*	**(4)**	**-**	**4**	**(20)**	**10**	**(10)**
(Loss) income before interest and income taxes	**(84)**	**249**	**329**	**74**	**52**	**620**

Segment Income (Loss) for the Year Ended December 31, 2006	**Regulated**		**Unregulated**			
	Nuclear	**Hydro-electric**	**Hydro-electric**	**Fossil-Fuelled**	**Other**	**Total**
(millions of dollars)						
Revenue	2,665	685	780	1,430	165	5,725
Revenue limit rebate	-	-	(44)	(117)	-	(161)
	2,665	685	736	1,313	165	5,564
Fuel expense	122	245	88	643	-	1,098
Gross margin	2,543	440	648	670	165	4,466
Operations, maintenance and administration	1,942	92	189	524	5	2,752
Depreciation and amortization	368	66	69	133	53	689
Accretion on fixed asset removal and nuclear waste management liabilities	490	-	-	9	-	499
Earnings on nuclear fixed asset removal and nuclear waste management funds	(371)	-	-	-	-	(371)
Property and capital taxes	44	18	15	19	10	106
Income (loss) before other gains and losses	70	264	375	(15)	97	791
Other (gains) and losses *(Note 17)*	-	-	-	22	-	22
Income (loss) before interest and income taxes	70	264	375	(37)	97	769

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Excerpt from Ex. A2-T1-S1 Appendix A

	Regulated		Unregulated			
(millions of dollars)	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	Total
Selected Balance Sheet Information						
As at December 31, 2007						
Segment fixed assets in service, net	**4,030**	**3,871**	**2,996**	**422**	**508**	**11,827**
Segment construction work in progress	**210**	**299**	**88**	**322**	**31**	**950**
Segment property, plant and equipment, net	**4,240**	**4,170**	**3,084**	**744**	**539**	**12,777**
Segment materials and supplies inventory, net:						
Short-term	**73**	**1**	**-**	**51**	**-**	**125**
Long-term	**346**	**-**	**3**	**4**	**-**	**353**
Segment fuel inventory	**231**	**-**	**-**	**373**	**-**	**604**
As at December 31, 2006						
Segment fixed assets in service, net	4,213	3,907	3,012	408	544	12,084
Segment construction work in progress	165	252	78	145	37	677
Segment property, plant and equipment, net	4,378	4,159	3,090	553	581	12,761
Segment materials and supplies inventory, net:						
Short-term	63	1	-	48	-	112
Long-term	320	-	3	3	-	326
Segment fuel inventory	183	-	-	486	-	669
Selected Cash Flow Information						
Year ended December 31, 2007						
Investment in fixed assets	**207**	**80**	**66**	**270**	**43**	**666**
Year ended December 31, 2006						
Investment in fixed assets	173	171	81	71	141	637

19. Related Party Transactions

Given that the Province owns all of the shares of OPG, related parties include the Province, the other successor entities of Ontario Hydro, including Hydro One Inc. ("Hydro One"), the IESO, and the OEFC. OPG also enters into related party transactions with its joint ventures. The transactions between OPG and related parties are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Excerpt from Ex. A2-T1-S1 Appendix A

CONSOLIDATED BALANCE SHEETS

As at December 31 *(millions of dollars)*	**2007**	**2006**
Liabilities		
Current liabilities		
Accounts payable and accrued charges *(Notes 12 and 19)*	**953**	989
Revenue limit rebate payable *(Note 16)*	**100**	40
Short-term notes payable *(Note 8)*	**-**	15
Long-term debt due within one year *(Note 9)*	**407**	406
Future income taxes *(Note 11)*	**-**	3
Deferred revenue due within one year	**12**	12
Income and capital taxes payable *(Note 11)*	**66**	128
	1,538	1,593
Long-term debt *(Note 9)*	**3,446**	2,953
Other long-term liabilities		
Fixed asset removal and nuclear waste management *(Note 10)*	**10,957**	10,520
Other post employment benefits and supplementary pension plans *(Note 12)*	**1,556**	1,396
Long-term accounts payable and accrued charges	**184**	150
Deferred revenue	**120**	132
Future income taxes *(Note 11)*	**217**	246
Regulatory liabilities *(Note 7)*	**14**	11
	13,048	12,455
Shareholder's equity		
Common shares *(Note 14)*	**5,126**	5,126
Retained earnings	**1,664**	623
Accumulated other comprehensive income	**17**	-
	6,807	5,749
	24,839	22,750

Commitments and Contingencies (Notes 2, 8, 9, 10, 11, 13, 15, and 18)

See accompanying notes to the consolidated financial statements

On behalf of the Board of Directors:

Honourable Jake Epp (signed)
Chairman

M. George Lewis (signed)
Director