CONTINUATION OF EXISTING DEFERRAL AND VARIANCE ACCOUNTS

1.0 PURPOSE
This evidence provides a summary of the deferral and variance accounts that OPG is seeking approval to continue. OPG is not proposing any new deferral or variance accounts in this application.

2.0 OVERVIEW
OPG proposes to continue all existing deferral and variance accounts. Section 3.0 describes the operation of the accounts and the basis for their continuation. Unless otherwise stated, OPG proposes to record in the approved deferral and variance accounts differences between the amounts included in the approved payment amounts and the actual costs or revenues. Section 4.0 discusses application of interest to the balances in the accounts.

3.0 CONTINUED ACCOUNTS
OPG proposes to continue the following existing deferral and variance accounts:

- Hydroelectric Water Conditions Variance Account
- Ancillary Services Net Revenue Variance Account – Hydroelectric and Nuclear Sub-Accounts
- Hydroelectric Incentive Mechanism Variance Account
- Hydroelectric Surplus Baseload Generation Variance Account
- Income and Other Taxes Variance Account
- Tax Loss Variance Account (to be terminated on December 31, 2014 pursuant to the EB-2012-0002 Payment Amounts Order)
- Capacity Refurbishment Variance Account
- Pension and OPEB Cost Variance Account
- Impact for USGAAP Deferral Account (to be terminated on December 31, 2014 pursuant to the EB-2012-0002 Payment Amounts Order)
- Hydroelectric Deferral and Variance Over/Under Recovery Variance Account
- Nuclear Liability Deferral Account
• Nuclear Development Variance Account

• Bruce Lease Net Revenues Variance Account – Derivative and Non-Derivative Sub-Accounts

• Pickering Life Extension Depreciation Variance Account

• Nuclear Deferral and Variance Over/Under Recovery Variance Account

The origin and need for these accounts and their operation is described in further detail in the remainder of this section.

OPG proposes that all accounts applicable to the previously regulated hydroelectric facilities be extended to include the newly regulated hydroelectric facilities. Where applicable, for ease of record keeping and tracking, separate sub-accounts will be used to distinguish between account entries for the previously and newly regulated facilities. Unless a distinction is specifically made, all references to OEB-approved forecasts below in relation to hydroelectric facilities should be read as including both previously regulated and newly regulated hydroelectric facilities. Entries into the accounts in respect of the newly regulated hydroelectric facilities will commence on the effective date of the payment amounts for these facilities, proposed as July 1, 2014.

3.1 Hydroelectric Water Conditions Variance Account

The Hydroelectric Water Conditions Variance Account was originally established by O. Reg. 53/05 and subsequently approved by the OEB in EB-2007-0905 in recognition of the fact that water conditions are subject to a high degree of forecast risk due to factors that are beyond OPG’s ability to manage or control, such as weather. This account should continue to record the financial impact of differences between forecast and actual water conditions for the previously regulated hydroelectric facilities and, due to similar forecast risk for the newly regulated hydroelectric facilities, is proposed to be extended to include the these facilities. To that end, separate sub-accounts will be established as follows: Previously Regulated Sub-Account and Newly Regulated Sub-Account.

3.1.1 Previously Regulated Hydroelectric Facilities
For the previously regulated hydroelectric facilities, OPG will continue to determine the hydroelectric production impact of changes in water conditions by entering the actual flow values into the same production forecast models used to calculate the OEB-approved production forecast, holding all other variables constant. Deviations from forecast will be determined as the difference between the calculated production resulting from entering actual flows for the month into the forecast model and the energy production forecast approved by the OEB. The revenue impact of the production variance recorded in the Previously Regulated Sub-Account will continue to be determined by multiplying the deviation from forecast, as described above, by the approved payment amount for the previously regulated hydroelectric facilities.

The sub-account will also continue to record changes in the gross revenue charge costs from those reflected in the approved revenue requirement, as a result of differences in energy production from actual flows and the forecast energy production described above. Amounts recorded in the sub-account in respect of these costs will be determined by multiplying the production deviation by the applicable gross revenue charge rate. The sub-account also will continue to record any variances in the amounts payable to the St. Lawrence Seaway Management Corporation for the conveyance of water in the Welland Ship Canal from those reflected in the approved revenue requirement.

The sub-account also needs to continue in order to record amortization of the year-end 2012 account balance approved in EB-2012-0002 and interest.

3.1.2 Newly Regulated Hydroelectric Facilities

As noted in Ex. E1-1-1, Section 3.5, energy production forecasts for 21 of the newly regulated hydroelectric plants, located on nine river systems, are produced using similar computer models to those used to forecast production for the previously regulated facilities. The models convert forecast water availability to forecast energy production using historical median monthly flows as the basis for determining the monthly energy production forecasts. Similar to the previously regulated hydroelectric facilities, for these 21 plants, on a monthly basis commencing July 2014, OPG proposes that deviations of actual flows from these
historical median monthly flows be used to determine the additions for the purposes of the Newly Regulated Sub-Account. These 21 facilities are listed in Ex. E1-1-1 Appendix 1. The revenue and gross revenue charge impacts will be calculated in the same manner as for the previously regulated facilities. The sub-account will also record any related variances in the amounts payable to the Government of Quebec for water rentals from those reflected in the approved revenue requirement (Ex. F1-4-1 Section 4).

Also as noted in Ex. E1-1-1, Section 3.5, no computer models exist to forecast production from the remaining 27 smaller newly regulated hydroelectric stations, which account for less than two per cent of total production from all regulated hydroelectric facilities. Therefore, given the small size of these 27 facilities, OPG proposes that they be excluded from the scope of the Hydroelectric Water Conditions Variance Account.

3.2 Ancillary Services Net Revenue Variance Account

The Ancillary Services Net Revenue Variance Account was originally established by O. Reg. 53/05 and subsequently approved by the OEB in EB-2007-0905. This account recognizes that ancillary services revenues are difficult to forecast accurately, with variances between forecast and actual ancillary revenues reflecting changing demand and system/grid operating requirements. For the same reasons, OPG proposes that the account be extended to the newly regulated facilities. The existing Hydroelectric and Nuclear Sub-Account will continue to capture the difference between actual previously regulated hydroelectric and nuclear ancillary services net revenue and the forecast amounts reflected in the revenue requirement approved by the OEB. The Newly Regulated Hydroelectric Sub-Account will be used to record differences between actual and forecast ancillary services revenues from the newly regulated hydroelectric facilities. Ancillary services revenues are discussed in Ex. G1-1-1.

The account also needs to continue in order to record the amortization of the year-end 2012 account balance approved in EB-2012-0002 and interest.

3.3 Hydroelectric Incentive Mechanism Variance Account
The Hydroelectric Incentive Mechanism Variance Account was originally approved in EB-2010-0008 to record a credit to ratepayers of 50 per cent of hydroelectric incentive mechanism (“HIM”) net revenues above a specific threshold. In this application, OPG is proposing a change to the operation of the HIM that eliminates the need for additions to the account in the future. The proposed mechanism is discussed in Ex. E1-2-1. The variance account needs to continue in order to record interest and amortization of the year-end 2013 account balance as proposed in this application.

3.4 Hydroelectric Surplus Baseload Generation Variance Account

The Hydroelectric Surplus Baseload Generation Variance Account was originally approved in EB-2010-0008. This account should continue in order to record the financial impact of foregone production at the previously regulated hydroelectric facilities due to surplus baseload generation (“SBG”) conditions, with the enhancements described in Ex. E1-2-1 Section 6.0, and, for the same reasons as originally established for the previously regulated hydroelectric facilities, is proposed to include the newly regulated hydroelectric facilities. To that end, separate sub-accounts will be established as follows: Previously Regulated Sub-Account and Newly Regulated Sub-Account. For the same reasons as noted in Section 3.1.2 above, OPG proposes that only the 21 newly regulated hydroelectric facilities listed in Ex. E1-1-1 Appendix 1 will be included in the scope of this sub account.

No forecast of foregone production due to SBG conditions has been applied to reduce the hydroelectric production forecasts proposed for establishing new payment amounts for the previously and newly regulated hydroelectric output. OPG will continue to determine the revenue impact of SBG recorded in the Previously Regulated Sub-Account by multiplying the foregone production volume due to SBG by the approved previously regulated hydroelectric payment amount. The revenue impact is proposed to be calculated in the same manner for purposes of the Newly Regulated Sub-Account.

OPG will also continue to record in the Previously Regulated Sub-Account changes in the gross revenue charge costs, as a result of SBG, from those reflected in the revenue requirement approved by the OEB. The amounts to be recorded will be calculated by
multiplying the foregone production volume at the prescribed hydroelectric facilities due to SBG conditions by the applicable gross revenue charge rates. Gross revenue charge impacts are proposed to be captured in the Newly Regulated Sub-Account in the same manner. OPG will also continue to record in the Previously Regulated Sub-Account any variances in the amounts payable to the St. Lawrence Seaway Management Corporation for the conveyance of water in the Welland Ship Canal as a result of foregone production due to SBG. OPG also proposes to record in the Newly Regulated Sub-Account any related variances in the amounts payable to Government of Quebec (see Ex. F4-1-1 Section 4) as a result of foregone production due to SBG.

The reconciliation of the sub-accounts will be based on a methodology of calculating spill arising from SBG conditions as described in Ex. E1-2-1 Section 3.0.

The variance account also needs to continue in order to record interest and amortization of the year-end 2013 account balance as proposed in this application.

### 3.5 Income and Other Taxes Variance Account

The Income and Other Taxes Variance Account was originally approved in EB-2007-0905. A similar account is available to electricity distributors. This account needs to continue in order to record the financial impact on the approved revenue requirement of:

- Any differences in payments in lieu of corporate income or capital taxes that result from a legislative or regulatory change to the tax rates or rules of the *Income Tax Act* (Canada) and the *Taxation Act, 2007* (Ontario) (formerly the *Corporations Tax Act* (Ontario)), as modified by the regulations under the *Electricity Act, 1998*, and any differences in payments in lieu of property tax to the Ontario Electricity Financial Corporation that result from changes to the regulations under the *Electricity Act, 1998*;
- Any differences in municipal property taxes that result from a legislative or regulatory change to the tax rates or rules for OPG’s prescribed assets under the *Assessment Act, 1990*;
Any differences in payments in lieu of corporate income or capital taxes that result from a change in, or a disclosure of, a new assessing or administrative policy that is published in the public tax administration or interpretation bulletins by relevant federal or provincial tax authorities, or court decisions on other taxpayers; and

Any differences in payments in lieu of income or capital taxes that result from assessments or re-assessments (including re-assessments associated with the application of the tax rates and rules to OPG’s regulated operations or changes in assessing or administrative policy including those arising from court decisions on other taxpayers). OPG continues to be subject to tax audits from prior years dating back to 2009.

The income tax provision reflected in the approved revenue requirement will be used to calculate any variances in income taxes to be recorded in the Income and Other Taxes Variance Account.

The account also needs to continue in order to record the amortization of the year-end 2012 account balance approved in EB-2012-0002 and interest.

For the same reasons as established for OPG’s other regulated facilities, OPG proposes that this account should apply to the newly regulated hydroelectric facilities starting on the effective date of the payment amounts for these facilities.

### 3.6 Tax Loss Variance Account

The Tax Loss Variance Account was originally approved in EB-2009-0038. OPG ceased recording additions to the account effective March 1, 2011. OPG will continue to record only interest and amortization in the account. Pursuant to the EB-2012-0002 Payment Amounts Order, the regulated hydroelectric and nuclear portions of the remaining account balance as at December 31, 2014 will be transferred to the Hydroelectric and Nuclear Deferral and Variance Over/Under Recovery Variance Accounts, respectively. Following this transfer, the Tax Loss Variance Account will be terminated on December 31, 2014.
3.7 Capacity Refurbishment Variance Account

The Capacity Refurbishment Variance Account was originally approved in EB-2007-0905 pursuant to Section 6(2)4 of O. Reg. 53/05. This account will continue to record variances between the actual capital and non-capital costs and firm financial commitments incurred to increase the output of, refurbish or add operating capacity to a prescribed generation facility listed in O. Reg. 53/05, Section 2 and those forecast costs and firm financial commitments reflected in the revenue requirement approved by the OEB. The prescribed generation facilities include all newly regulated hydroelectric facilities. As required by O. Reg. 53/05, Section 6(2)4, this account will continue to include assessment costs and pre-engineering costs and commitments.

For ease of record keeping and tracking OPG will use the following sub-accounts to make entries into the account, as applicable: Nuclear Sub-Account, Previously Regulated Hydroelectric Sub-Account and Newly Regulated Hydroelectric Sub-Account.

The account will also continue in order to record the amortization of the portion of the year-end 2012 account balance approved in EB-2012-0002 and interest. The account will also record the amortization of the portion of the year-end 2013 account balance proposed to be cleared in this application.

3.8 Pension and OPEB Cost Variance Account

The Pension and OPEB Cost Variance Account was originally approved in EB-2011-0090 and subsequently continued in EB-2012-0002. As reflected in the approved Settlement Agreement in EB-2012-0002, this account will continue to record the difference between: (i) the pension and OPEB costs, plus related income tax PILs, reflected in the current revenue requirement approved by the OEB, and (ii) OPG's actual pension and OPEB costs, and associated tax impacts, for the prescribed generation facilities.

The differences between the forecast and actual amounts will continue to be calculated and recorded in a manner consistent with that underpinning the approved account balance as at December 31, 2012. Actual pension and OPEB costs used in the calculation of the difference
will be calculated using the same accounting standards as those used to derive the OEB-approved forecast amounts.

The account also needs to continue in order to record the amortization of the year-end 2012 account balance approved in EB-2012-0002.

Pursuant to the EB-2012-0002 Payment Amount Order, the balance in this account as at December 31, 2012, including interest accrued to that date, was split into the Historic Recovery and Future Recovery components. The Historic Recovery component was set at 2/12ths of the total December 31, 2012 balance. The Future Recovery component was set at 10/12ths of the total December 31, 2012 balance. The EB-2012-0002 Payment Amounts Order reflected the terms of the approved Settlement Agreement, which specified that no interest is to be recorded on the Future Recovery component of the December 31, 2012 approved balance during the period from January 1, 2013 to December 31, 2014. Additionally, during this period, OPG is not recording interest on account additions arising during 2013 or 2014.

Effective January 1, 2015, OPG will resume the application of interest to the opening monthly balance of the remaining balance of the Future Recovery component and all additions recorded after December 31, 2012. The rationale for applying interest to other deferral and variance accounts also applies to the Pension and OPEB Cost Variance Account. An interest cost on the account balance is borne by OPG or ratepayers as a result of the accumulation, for future recovery from, or refund to, ratepayers, of amounts related to a current period. The application of interest on the balance recognizes the time value of money associated with the lag between the period in which amounts recorded in the account arise and the period in which they are settled between ratepayers and OPG.

As noted in Ex. H1-1-1, Section 4.8, in order to facilitate the presentation of entries into the account, OPG has shown in Ex. H1-1-1 Table 1 the projected account additions for 2013 as a separate component. For administrative purposes, OPG will use the following sub-accounts for the three components of the account, effective December 31, 2013: the Historic

OPG proposes that the variance account apply to the newly regulated facilities starting on the effective date of the payment amounts for these facilities, as the same factors resulting in differences between actual and forecast pension and OPEB costs affect both the newly and previously regulated facilities.

3.9 Impact for USGAAP Deferral Account

The Impact for USGAAP Deferral Account was originally approved in EB-2011-0432. This account captured the financial impacts of OPG’s transition to and implementation of USGAAP. Effective January 1, 2013, pursuant to the EB-2012-0002 Payment Amounts Order, OPG ceased recording additions to the account. OPG will continue to record only interest and amortization in the deferral account. Pursuant to EB-2012-0002 Payment Amounts Order, the regulated hydroelectric and nuclear portions of the remaining account balance as at December 31, 2014 will be transferred to the Hydroelectric and Nuclear Deferral and Variance Over/Under Recovery Variance Accounts, respectively. Following this transfer, the Impact for USGAAP Deferral Account will be terminated on December 31, 2014.

3.10 Hydroelectric Deferral and Variance Over/Under Recovery Variance Account

The Hydroelectric Deferral and Variance Over/Under Recovery Variance Account was originally approved in EB-2009-0174. This account should continue in order to record the differences between the amounts approved for recovery in the hydroelectric deferral and variance accounts and the actual amounts recovered based on actual regulated hydroelectric production and approved riders. While there are currently no deferral or variance account balances for the newly regulated hydroelectric facilities, such balances are anticipated in the future, as OPG proposes to extend existing accounts to include these facilities. As such, this account is also proposed to be extended to include the newly regulated hydroelectric facilities.
The account also should continue in order to capture the transfer of the hydroelectric portion of the balances remaining in the Tax Loss Variance Account and the Impact for USGAAP Deferral Account as at December 31, 2014, and, as ordered by the OEB, other accounts as they may expire from time to time.

The account also needs to continue in order to record the amortization of the year-end 2012 account balance approved in EB-2012-0002 and interest.

3.11 Nuclear Liability Deferral Account
The Nuclear Liability Deferral Account was originally approved in EB-2007-0905 pursuant to O. Reg. 53/05. Pursuant to O. Reg. 53/05, this account will continue to record the revenue requirement impact of any change in OPG’s nuclear decommissioning liability arising from an approved reference plan measured against the forecast impact reflected in the revenue requirement approved by the OEB. OPG will continue to record the return on rate base in the account using the weighted average accretion rate on its nuclear liabilities of 5.37 percent.

The “nuclear decommissioning liability” is defined as “the liability of Ontario Power Generation Inc. for decommissioning its nuclear generating facilities and the management of its nuclear waste and nuclear fuel.” An “approved reference plan” is defined as “a reference plan, as defined in the Ontario Nuclear Funds Agreement, which has been approved by Her Majesty the Queen in the right of Ontario in accordance with that agreement.”

The account will also continue to record the amortization of the year-end 2012 account balance, as approved in EB-2012-0002. Pursuant to the terms of the approved Settlement Agreement, as stipulated in the EB-2012-0002 Payment Amounts Order, no interest will be recorded on the balance of the Nuclear Liability Deferral Account.

3.12 Nuclear Development Variance Account
The Nuclear Development Variance Account was originally approved in EB-2007-0905 as mandated in O. Reg. 53/05. This account will continue to record variances between the
actual non-capital costs incurred and firm financial commitments made in the course of planning and preparation for the development of proposed new nuclear generation facilities and those forecast costs and firm financial commitments reflected in the revenue requirement approved by the OEB. As noted in Ex. F2-8-1, OPG does not propose to include a forecast of these costs in the test period revenue requirement.

The account will also record interest and amortization of the year-end 2013 account balance as proposed in this application.

### 3.13 Bruce Lease Net Revenues Variance Account

The Bruce Lease Net Revenues Variance Account was originally approved by the OEB in EB-2007-0905 in order to ensure that OPG recovers its actual costs associated with the Bruce facilities and that the regulated payment amounts are adjusted to reflect the actual revenues net of costs earned from the Bruce lease. This account should continue in order to capture differences between (i) the forecast revenues and costs related to the Bruce lease that are factored into the nuclear revenue requirement approved by the OEB, and (ii) OPG’s actual revenues and costs in respect of the Bruce facilities. These revenues and costs are discussed in Ex. G2-2-1.

The variance recorded in this account will continue to be measured by comparing the Bruce lease revenues net of costs credited to customers monthly through the approved nuclear payment amount to the actual monthly Bruce lease revenues net of costs realized by OPG.

The monthly Bruce lease revenues net of costs credited to customers will continue to be equal to the rate of recovery reflected in the nuclear revenue requirement approved by the OEB multiplied by OPG’s actual nuclear production. The rate of recovery will continue to be calculated by dividing the forecast Bruce lease revenues net of costs reflected in the OEB-approved nuclear revenue requirement by the OEB-approved nuclear production forecast.

This account will continue be divided into two sub-accounts as follows:
Derivative Sub-Account: The Derivative Sub-Account will continue to record the following additions as determined in accordance with generally accepted accounting principles for unregulated entities: changes in the fair value of the derivative liability for the conditional supplemental rent rebate provision of the Bruce lease (recognized as change in accounting income) and associated income tax impacts on Bruce lease net revenues, and income tax impacts on Bruce lease net revenues of rent rebates resulting from the above provision.

Non-Derivative Sub-Account: The Non-Derivative Sub-Account will continue to record variances related to all non-derivative aspects of Bruce lease revenues net of costs.

The cost impact of any changes in OPG’s liability for decommissioning the Bruce nuclear generating facilities and the management of nuclear waste and nuclear fuel related to the Bruce stations will also continue to be recorded in this account and will be reflected in the Non-Derivative Sub-Account.

The two sub-accounts will also continue in order to record the amortization of the applicable portions of the year-end 2012 account balance approved in EB-2012-0002.

To the extent that the actual supplemental rent rebate amounts paid to Bruce Power differ from the approved forecast amounts, such differences will be reflected in the Derivative Sub-Account in order to be carried forward to adjust amortization amounts the next time the account balance is cleared.

The terms of the approved Settlement Agreement reflected in the EB-2012-0002 Payment Amounts Order specified that no interest is to be recorded on the balance of either sub-account during the period from January 1, 2013 to December 31, 2014. Additionally, during this period, OPG is not recording interest on additions to either sub-account arising during 2013 or 2014.

Effective January 1, 2015, OPG will resume the application of interest to the opening monthly balances in the account, including all additions recorded after December 31, 2012.
3.14 Pickering Life Extension Depreciation Variance Account

As discussed in Ex. H1-1-1, Section 4.14, pursuant to the EB-2012-0002 Payment Amounts Order, this variance account was established in order to record a credit amount of $3.9M per month for the period from January 1, 2013 until the effective date of new nuclear payment amounts (excluding payment riders), reflecting the revised service lives, for depreciation purposes, of the Pickering stations. The nuclear payment riders established for 2013 and 2014 were reduced by an equivalent amount, resulting in an amortization debit entry being recorded in this account starting in 2013.

As the proposed revenue requirement reflects the revised Pickering service lives, starting on the effective date of the new payment amounts, the account will no longer record a credit addition. As the EB-2012-0002 payment rider continues until December 31, 2014, the account will continue to record an amortization debit entry during 2014 as approved in the EB-2012-0002 Payment Amounts Order. This will result in an accumulation, by December 31, 2014, of a balance to be recovered from ratepayers. This operation of the account is outlined in the approved EB-2012-0002 Settlement Agreement (Ex. M1-1, p. 30) and avoids the double-counting of the impact of the revised service lives that would otherwise result once new payment amounts are effective.

As per the EB-2012-0002 Payment Amounts Order, the account balance will continue not to attract interest.

3.15 Nuclear Deferral and Variance Over/Under Recovery Variance Account

The Nuclear Deferral and Variance Over/Under Recovery Variance Account was originally approved in EB-2009-0174. This account should continue in order to record the differences between the amounts approved for recovery in the nuclear deferral and variance accounts and the actual amounts recovered based on actual nuclear production and approved riders. The account also should continue in order to capture the transfer of the nuclear portion of the balances remaining in the Tax Loss Variance Account and the Impact for USGAAP Deferral
Account as at December 31, 2014, and, as ordered by the OEB, other accounts as they may expire from time to time.

The account also needs to continue in order to record the amortization of the year-end 2012 account balance approved in EB-2012-0002 and interest.

4.0 INTEREST

OPG proposes to record interest on all deferral and variance accounts effective January 1, 2014, unless specified otherwise in the account descriptions above. Interest will be applied to the monthly opening balances of these accounts at the interest rate set by the OEB from time to time pursuant to its interest policy for deferral and variance accounts.