

Financial Statements

**Fair Hydro Trust**  
December 31, 2022



# INDEPENDENT AUDITOR'S REPORT

To the Unitholders of the  
**Fair Hydro Trust**

## **Opinion**

We have audited the financial statements of the **Fair Hydro Trust** (the "Trust"), which comprise the balance sheets as at December 31, 2022 and 2021, and the statements of income and comprehensive income and statements of cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Trust as at December 31, 2022 and 2021, and its results of operations and its cash flows for the years then ended in accordance with United States generally accepted accounting principles.

## **Basis for Opinion**

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Trust in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## **Responsibilities of Management and those Charged with Governance for the Financial Statements**

Management is responsible for the preparation and fair presentation of the financial statements in accordance with United States generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Trust's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Trust or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Trust's financial reporting process.

## **Auditor's Responsibilities for the Audit of the Financial Statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Trust's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Trust to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

/s/ Ernst & Young LLP

Toronto, Canada  
April 19, 2023

Chartered Professional Accountants  
Licensed Public Accountants

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FAIR HYDRO TRUST

STATEMENTS OF INCOME AND  
COMPREHENSIVE INCOME

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Years Ended December 31

*(thousands of dollars)*

	2022	2021
<b>Revenues</b>		
Interest income <i>(Note 7)</i>	64,061	64,050
Other income	27	-
	<b>64,088</b>	64,050
<b>Expenses</b>		
Interest expense <i>(Note 4 and Note 7)</i>	64,061	64,050
<b>Net income and comprehensive income</b>	<b>27</b>	-

*See accompanying notes to the financial statements*

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**FAIR HYDRO TRUST****STATEMENTS OF CASH FLOWS**

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**Years Ended December 31***(thousands of dollars)*

	<b>2022</b>	<b>2021</b>
<b>OPERATING ACTIVITIES</b>		
Net income	27	-
Amortization of deferred issuance fees <i>(Note 4)</i>	377	367
Decrease in advances from related parties	(377)	(367)
<b>Cash provided by operating activities</b>	<b>27</b>	<b>-</b>
<b>Net increase in restricted cash</b>	<b>27</b>	<b>-</b>
Restricted cash, beginning of the year	361	361
<b>Restricted cash, end of the year</b>	<b>388</b>	<b>361</b>

*See accompanying notes to the financial statements*

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**FAIR HYDRO TRUST****BALANCE SHEETS**

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<b>As at December 31</b> <i>(thousands of dollars)</i>	<b>2022</b>	<b>2021</b>
<b>ASSETS</b>		
<b>Current</b>		
Restricted cash	388	361
Interest receivable	8,282	8,282
	<b>8,670</b>	8,643
<b>Non-current</b>		
Financing receivables <i>(Note 4 and Note 7)</i>	1,764,706	1,764,706
<b>Total assets</b>	<b>1,773,376</b>	1,773,349
<b>LIABILITIES AND UNITHOLDERS' CAPITAL</b>		
<b>Current</b>		
Interest payable <i>(Note 4)</i>	8,282	8,282
Advances from related parties <i>(Note 7)</i>	2,921	3,298
	<b>11,203</b>	11,580
<b>Non-current</b>		
Long-term debt <i>(Note 4)</i>	1,761,647	1,761,270
<b>Unitholders' capital <i>(Note 6)</i></b>	<b>526</b>	499
<b>Total liabilities and Unitholders' capital</b>	<b>1,773,376</b>	1,773,349

*See accompanying notes to the financial statements*

**Computershare Trust Company of Canada,**  
in its capacity as trustee of **Fair Hydro Trust,**  
by **Ontario Power Generation Inc.,**  
not in its individual capacity but solely as Manager

**Aida Cipolla (signed)**  
Chief Financial Officer and Senior Vice  
President – Finance  
Ontario Power Generation Inc.

**NOTES TO THE FINANCIAL STATEMENTS**

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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**1. DESCRIPTION OF BUSINESS**

Fair Hydro Trust (the Trust) is a special purpose trust established under the laws of the Province of Ontario (the Province) by Computershare Trust Company of Canada, acting as Issuer Trustee, pursuant to the Declaration of Trust dated December 20, 2017, and was caused to be established by Ontario Power Generation Inc. (OPG). The Trust was established as the financing entity contemplated by the *Ontario Fair Hydro Plan Act, 2017* (the Act), with the objective of deferring and refinancing a portion of the Global Adjustment costs charged to eligible consumers (Specified Consumers) over a longer period of time. The Global Adjustment includes the difference between Ontario's electricity market clearing price used to dispatch generation, and the prices paid to contracted and regulated generators in the province and the cost of conservation and demand management programs. The Act received Royal Assent on June 1, 2017 and the associated General Regulation came into force in June 2017. The General Regulation provided details on the structural, operational and financial elements required to implement the Act.

Pursuant to the Act, effective May 1, 2017, the Independent Electricity System Operator (IESO) began to defer the collection of a portion of the Global Adjustment costs. The Act allowed the IESO to transfer a portion of the deferred balance to a financing entity that would fund the deferral in exchange for an irrevocable right to recover the balance and associated financing and other costs from Specified Consumers in the future (Investment Interest). The legislation appointed OPG as Financial Services Manager under the Act and conveyed upon it statutory obligations, including the creation of one or more financing entities that may acquire Investment Interests from the IESO. The Trust is a financing entity under the Act.

The Declaration of Trust established the Trust to carry on activities for the exclusive benefit of its unitholders including FHP2017 Inc. (FHP2017), a wholly owned subsidiary of OPG, and the Indenture Trustee BNY Trust Company of Canada (BNY) (collectively, the Unitholders). The beneficial interest and rights generally of the Unitholders in the Trust are limited to the right to participate in distributions when and as declared by the Issuer Trustee and distributions upon the termination of the Trust. The legal ownership of the Trust's property and the right to conduct the activities of the Trust are vested exclusively in the Issuer Trustee and no Unitholder has any right of ownership in any of the Trust's property. The Unitholders are not subject to any liability arising out of the activities of the Trust.

In order for the Trust to finance the Investment Interest acquired from the IESO in 2017 and 2018, it incurred senior debt from capital markets and subordinated debt from OPG. The Trust's investment attracted financing amounts and other related fees.

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## Fair Hydro Trust

### NOTES TO THE FINANCIAL STATEMENTS

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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The Issuer Trustee, on behalf of the Trust, entered into a Management Agreement with OPG, as manager, whereby all of the powers and duties of managing the Trust have been delegated to OPG. OPG was entitled to charge the Trust a management service fee, composed of a base fee and a variable fee, and to recover costs and expenses incurred by OPG on behalf of the Trust or in relation to the establishment, management and administration of the Trust and its Investment Interest without margin. All fees charged by OPG as Financial Services Manager were subject to the provisions outlined in sections 10.1 to 10.15 of the General Regulation of the Act and were subject to an annual review by the Ontario Energy Board. OPG's entitlement to fees was subject to the payment priorities set forth in the Master Trust Indenture.

The IESO was required under the General Regulation to pay and remit to the Trust any amounts charged to the IESO by the Trust in respect of carrying costs incurred by the Trust from June 1, 2017 to July 31, 2021. Carrying costs included all funding costs, such as interest on all notes outstanding, and other expenses of the Trust, other than repayment of debt principal.

Effective November 1, 2019, under the Government of Ontario's *Fixing the Hydro Mess Act, 2019* (being the Act as so amended, referred to as the Fair Hydro Act), the Trust is prohibited from incurring further funding obligations and the Province is responsible for paying existing funding obligations of the Trust, including principal repayments. OPG continues as Financial Services Manager but is responsible for paying the operating costs of the Trust. The IESO no longer provides for the administration or servicing of the Investment Interest on behalf of the Trust effective November 1, 2019. The General Regulation made under the Act was revoked effective November 1, 2019. The Trust and the Province entered into a Funding Agreement effective December 1, 2019 that establishes the process and schedule for payments from the Province to the Trust to fund interest and principal on the Trust's obligations to its debtholders.

## 2. BASIS OF PRESENTATION

These financial statements have been prepared and presented in accordance with United States generally accepted accounting principles (US GAAP) and are presented in Canadian dollars.

The Trust has evaluated subsequent events and transactions through April 19, 2023 and has appropriately reflected events that require disclosure in the notes to these financial statements.

**NOTES TO THE FINANCIAL STATEMENTS**

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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**3. SIGNIFICANT ACCOUNTING POLICIES**

**Use of management estimates**

The preparation of the Trust's financial statements in accordance with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses. On an ongoing basis, management reviews these estimates. Changes in facts and circumstances may result in revised estimates and actual results could differ materially from those estimates.

**Restricted cash**

Restricted cash represents restricted cash on deposit that is subject to contractual restrictions. Pursuant to the Master Trust Indenture, all of the Trust's bank accounts are under the exclusive control of BNY and have been established in its name. All amounts on deposit are restricted in purpose and the distribution of use is subject to the order of priority outlined in the Master Trust Indenture.

**Financing receivables**

Financing receivables are collectible from the Province in the future in accordance with the Fair Hydro Act. Financing receivables amounts are initially measured at the transaction price and subsequently measured on an amortized cost basis. The basis of amortization follows the effective interest method. Financing receivables were financed through the issuance of long-term notes and warehouse facilities by the Trust.

**Financial assets and financial liabilities**

Financial assets and financial liabilities are measured at amortized cost. Financial instrument transactions are recorded at fair value on the transaction date.

**Deferred bond issuance fees**

The Trust capitalizes the costs of obtaining long-term debt financing and records them as a reduction to the carrying amount of the debt liability. This amount is amortized over the life of the related debt on an effective interest basis and included in interest expense.

**Deferred issuance fees**

The Trust capitalizes the costs of obtaining short-term warehouse credit facilities and records the costs as a separate deferred asset regardless of whether the credit facility has an outstanding balance. The deferred asset is amortized on a straight-line basis over the term of the related credit facility and is included in interest expense.

**NOTES TO THE FINANCIAL STATEMENTS**

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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**Advances from related parties**

Advances from related parties represent a current liability for the amount of pre-funding received from the IESO in accordance with the Act and associated General Regulation, related to expected carrying costs calculated under an accrual basis of accounting. The pre-funding of carrying costs was required as the Trust is effectively debt funded and had no cash at inception to settle its liabilities. The balance of the liability is reduced when the corresponding expense is incurred or accrued by the Trust.

**Interest income**

Interest income represents the amount of accretion of the financing receivables balance calculated on a tranche-by-tranche basis using the effective cost of each underlying debt issuance.

**Fair value measurement**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly arm's-length transaction between market participants at the measurement date. Fair value measurements are required to reflect the assumptions that market participants would use in pricing an asset or liability based on the best available information. These assumptions include the risks inherent in a particular valuation technique, such as a pricing model, and the risks inherent in the inputs to the model.

**Income taxes**

Under the terms of the Trust, all taxable income is payable to the Unitholders so that the Trust does not have any liability for income tax. As such, no provision for income taxes is recorded in these financial statements.

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**Fair Hydro Trust****NOTES TO THE FINANCIAL STATEMENTS**

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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**4. LONG-TERM DEBT, FINANCING RECEIVABLES, AND DEFERRED ISSUANCE FEES**

Long-term debt consists of the following as at December 31:

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	<b>2022</b>	<b>2021</b>
Long-term notes		
Senior secured notes		
3.44% due 2033	<b>500,000</b>	500,000
3.60% due 2038	<b>400,000</b>	400,000
Subordinated secured notes		
3.68% due 2033	<b>382,353</b>	382,353
3.88% due 2038	<b>305,882</b>	305,882
Junior subordinated secured notes		
4.01% due 2033	<b>98,040</b>	98,040
4.27% due 2038	<b>78,431</b>	78,431
	<b>1,764,706</b>	1,764,706
Less: unamortized bond issuance fees	<b>(3,059)</b>	(3,436)
Long-term debt	<b>1,761,647</b>	1,761,270

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During the year ended December 31, 2022, deferred bond issuance fees of \$377 were amortized to interest expense (2021 – \$367).

Under the Fair Hydro Act, the Province is responsible for expenses of the Trust arising under existing funding obligations, such as principal and interest on debt and certain taxes.

Substantially all of the net book value of the assets of the Trust is pledged in favour of specified creditors of the Trust, including the senior debtholders and OPG in its capacity as subordinated debtholder of the Trust.

As at December 31, 2022 and 2021, financing receivables represent balances collectible from the Province in the future in accordance with the Fair Hydro Act.

The Trust's subordinated secured notes and junior subordinated secured notes are payable to OPG.

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**Fair Hydro Trust****NOTES TO THE FINANCIAL STATEMENTS**

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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The remaining undiscounted contractual maturities, including principal and interest, of long-term debt are as follows as at December 31, 2022:

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	<b>Principal</b>	<b>Interest</b>
2023	-	63,683
2024	-	63,683
2025	-	63,683
2026	-	63,683
2027	-	63,683
Thereafter	1,764,706	495,821

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**5. FAIR VALUE MEASUREMENT**

The fair values of Trust's financial instruments as at December 31 are as follows:

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	<b>Fair Value</b>	<b>Carrying Value <sup>1</sup></b>	<b>Balance Sheet Line Item</b>
<b>As at December 31, 2022</b>			
Financing receivables	<b>1,600,379</b>	<b>1,764,706</b>	Financing receivables
Long-term debt	<b>(1,600,379)</b>	<b>(1,761,647)</b>	Long-term debt
<b>As at December 31, 2021</b>			
Financing receivables	1,918,341	1,764,706	Financing receivables
Long-term debt	(1,918,341)	(1,761,270)	Long-term debt

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<sup>1</sup> The carrying values of other financial instruments including restricted cash, interest receivable, interest payable, and advances from related parties approximate their fair value due to the immediate or short-term maturity of these financial instruments.

Valuation models use general assumptions and market data and therefore do not reflect the specific risks and other factors that would affect a particular instrument's fair value. The methodologies used for calculating the fair value adjustments are reviewed on an ongoing basis to ensure that they remain appropriate.

The fair value of the senior, subordinated and junior subordinated debt is based on indicative pricing from the market. The fair value of the financing receivables is based on the fair value of the debt. The fair value of these instruments is based on Level 2 inputs.

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**Fair Hydro Trust****NOTES TO THE FINANCIAL STATEMENTS**

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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**6. UNITHOLDERS' CAPITAL**

FHP2017 holds one million units representing 99.9999 percent and BNY holds one unit or 0.0001 percent of the Trust. Unitholders' capital as at December 31 is as follows:

	<b>FHP2017</b>	<b>BNY <sup>1</sup></b>	<b>Total</b>
Unitholders' capital – December 31, 2021	499	-	499
Net income for the year	<b>27</b>	-	<b>27</b>
Unitholders' capital – December 31, 2022	<b>526</b>	-	<b>526</b>
Unitholders' capital – December 31, 2020	499	-	499
Net income for the year	-	-	-
Unitholders' capital – December 31, 2021	499	-	499

<sup>1</sup> BNY's capital is less than one dollar.

**7. RELATED PARTY TRANSACTIONS**

The Trust's majority unitholder, FHP2017, is a wholly owned subsidiary of OPG. As the Province owns all of the shares of OPG, related parties of the Trust include the Province and entities controlled by the Province, including the IESO. The transactions between the Trust and related parties are in the normal course of business and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

The related party transactions are summarized below for the year ended December 31:

	<b>2022</b>		<b>2021</b>	
	<b>Revenue</b>	<b>Expense</b>	<b>Revenue</b>	<b>Expense</b>
Province				
Interest income	<b>64,061</b>	-	64,050	-
OPG				
Subordinated and junior subordinated interest expense	-	<b>32,818</b>	-	32,818
	<b>64,061</b>	<b>32,818</b>	64,050	32,818

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## Fair Hydro Trust

### NOTES TO THE FINANCIAL STATEMENTS

*As at and for the years ended December 31, 2022 and 2021  
(thousands of dollars unless otherwise stated)*

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The balances between the Trust and its related parties as at December 31 are summarized below:

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	2022	2021
Financing receivables		
Province	1,764,706	1,764,706
Interest receivable		
Province	8,282	8,282
Current liabilities		
Interest payable – OPG	4,269	4,269
Advances from related parties – IESO <sup>1</sup>	2,921	3,298
Long-term debt		
Subordinated notes payable – OPG	688,235	688,235
Junior subordinated notes payable – OPG	176,471	176,471

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<sup>1</sup> The balance relates primarily to unamortized amounts previously collected from the IESO to fund deferred issuance fees.

The Province has provided a limited guarantee to specified creditors of the Trust. The limited guarantee would be triggered in the event that (1) the Trust's ability to receive amounts in respect of its Investment Interest to pay for certain funding obligations is adversely affected due to either of the following events: a) the Province changes the Act or any other legislation or regulation; or b) the Province undertakes a significant change in Ontario's electricity market; or (2) a court declares that the Act is invalid or unconstitutional.

### 8. ECONOMIC DEPENDENCE

The Trust is dependent upon OPG to provide financial management and ongoing administration services pursuant to the Management Agreement between the Trust and OPG. OPG is responsible for the Trust's operating costs. The Trust is dependent upon the Province, pursuant to the Funding Agreement, to fund the Trust's interest and principal obligations to its debtholders.