May 5th, 2011

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge St., Suite 2700
Toronto, ON, M4P 1E4

via RESS and email

RE: **Staff Discussion Paper – Transition to IFRS – Implementation in an IRM Environment: EB-2008-0408**

Dear Ms. Walli:

On March 31, 2011, the Ontario Energy Board (the "Board") released a Staff Discussion Paper (the "Paper") on the transition to International Financial Reporting Standards ("IFRS"), with particular focus on the implementation of IFRS in an Incentive Regulation Mechanism ("IRM") environment. The Board invited comments on the recommendations and alternatives put forth in the Paper from all interested stakeholders. Following are the comments of the Coalition of Large Distributors ("CLD") which is comprised of Enersource Hydro Mississauga, Horizon Utilities Corporation, Hydro Ottawa Limited, PowerStream Corporation, Toronto Hydro-Electric System Limited, and Veridian Connections Ltd.

Issues Arising on Transition to IFRS

Issue #1 –For distributors that have rebased under CGAAP but who have subsequently adopted IFRS, what, if any, additional guidance does the Board need to provide as to how to recognize accounting changes between CGAAP and modified IFRS in an IRM application? Examples of problem areas include calculations for off-ramps, Z-factors, and the incremental capital module. What level of audit assurance, if any, should the Board require for reconciliation of CGAAP to modified IFRS for these calculations in IRM applications?

Staff Recommendation

Board staff recommends that, for those distributors who rebased under CGAAP, the financial information supporting various specified components of an IRM application (those listed on Page 4 of the Paper), must be provided under CGAAP, and that the adjustments to rates be made on the basis of the CGAAP filing. The CLD supports this recommendation.

The CLD further agrees with the recommendation that a reconciliation of the CGAAP-based financial information to the relevant information in the last annual RRR reporting under modified IFRS is required.

The CLD notes, however, that no guidance has been provided as to the level of detail required within the reconciliation. The CLD understands that most distributors will not be maintaining full sets of financial records at transactional levels under CGAAP after the adoption of IFRS. There would likely be significant additional costs in maintaining multiple transaction level ledger systems. The CLD submits, therefore, that reconciliations could only be reasonably provided at high levels (those not requiring transactional data).

The CLD suggests that the recommendation for Issue #1 be amended to include wording that provides for high level reconciliations and the acknowledgement that detailed, transactional level data will not be available for inclusion in such reconciliations. The CLD submits that specification of the expectations around such “high level reconciliations” would be helpful as guidance to distributors.

The CLD further agrees with the staff recommendation that the Board not require any additional level of audit assurance to be filed for the required reconciliations.

Alternative

The CLD does not support the proposed alternative that no reconciliation to MIFRS information be filed. The CLD believes that the distributor would require the specified reconciliations in preparing input to the IRM application, regardless of whether such was a filing requirement within the application. The requirement to submit the reconciliation would serve to streamline the interrogatory process and provide consistency across applications.

Issue #2 – Should any differences between costs recorded in the balance sheet accounts and costs built into rates that:

- **arise in the time period between rebasing in CGAAP and the first rebasing under MIFRS, and**
- **are driven by changes in accounting for capital or operating costs, prompted by the adoption of MIFRS,**

be recovered from or refunded to ratepayers? If yes, on what basis?

Staff Recommendation

Board staff recommends that, only those differences relating to the Property, Plant and Equipment components of rate base, when properly calculated, should be recoverable from, or refundable to, ratepayers. Staff recommends the use of a deferral account to capture these differences, the intention of which is to capture the result of the accounting policy changes only, not to capture performance differences during the IRM period. Staff further proposes that the disposition of the amounts in the account would be considered by the Board in a distributor’s next cost of service application and that the account be closed to further posting of differences at that time.

The CLD supports the Board staff recommendation regarding tracking of these differences.

In point 1 of the proposal (bottom of page 6), Staff propose *"Utilities should maintain records using CGAAP of the amounts in the PP&E accounts that will be included in rate base, commencing at their last rebasing under CGAAP, and continuing until their first rebasing under MIFRS."*

As was noted under Issue 1 above, most distributors will not be maintaining full sets of financial records at transactional levels under CGAAP after the adoption of IFRS. The maintenance of PP&E records using CGAAP could therefore only reasonably be expected at a high level, not at any level requiring transactional data. Reasonable use of proxies for costs and components such as differences in capitalization overhead rates should be acceptable. These proxies could be developed from data in 2011 (the 'pivot' year) where actual values under both CGAAP and IFRS will be known. Use of proxy, high-level data would be a cost effective and reasonable basis for the maintenance of PP&E accounts under CGAAP and MIFRS.

In paragraph 2 of page 9, under the rationale and need for a PP&E account, potential differences in treatment within Staff's proposal are noted. These are a) application of carrying charges –for which an 'alternative' is specifically identified on page 11 and b) the issue that the amount recorded in the account may be approved by the Board for clearance despite the fact that some portion of the amount is based on a forecast.

Application of Carrying Charges:

The CLD supports the Board staff proposal that carrying charges not be added to the balance accruing in the deferral account. The CLD agrees with Board staff's view that until MIFRS is adopted as the basis for setting rates, no under or over-collection has occurred and neither the utility nor the ratepayer should be compensated for the time value of this amount through the application of carrying charges.

Treatment of Clearance of Deferral account including forecast:

In this section, Board staff appears to be providing information on alternative treatments for clearance of the deferral account.

While there is no clear statement of recommendation, the CLD submits that a recommendation is inferred in the last sentence on page 7 "Staff proposes that disposition of the amounts in the account would be considered by the Board in the next cost of service application, and staff further recommends that the account be closed to further posting of differences at that time."

This statement implies that the bridge year and test year forecasts of the deferral account amounts be accepted in the balance to be cleared and not subject to further true up. The CLD supports the implied treatment on the basis that these forecasts are similar to and should be treated no differently than other of the PP&E components of rate base where a forecast is accepted by the Board to be included in an approved rate base value.

Need for a Pension & Other Post Employment Benefits ("P&OPEB") Account:

Board staff submits that a generic account to capture P&OPEB differences driven by the transition to IFRS is not required. Board staff also submits that only a few large distributors with Post-Employment Benefit Plans will be significantly affected by the adoption of IFRS.

The CLD does not support the Board staff recommendation.

The CLD agrees that only a few large distributors will experience a major change in their P&OPEB balances due to the adoption of IFRS. The impact, however, may be quite large for those distributors that may have unrecognized actuarial gains or losses at the date of transition to IFRS or experience actuarial gains or losses in the future.

A distributor that has unrecognized gains or losses at the date of transition will be required to apply IFRS retrospectively or recognize all cumulative gains and losses at the date of transition. Applying IFRS retrospectively is an unlikely option for most distributors due to the associated information and time requirements. Therefore, distributors will need to recognize all actuarial gains and losses at the date of transition to IFRS as an adjustment to opening retained earnings.

The CLD is concerned that if a generic account is not established, the adjustment to the P&OPEB liability at the date of transition to IFRS may never be reflected in rates. The CLD notes however, that further consideration and analysis is required to determine the appropriate amount to be recorded in each situation, as it cannot be assumed that the entire adjustment represents differences from amounts that have been realized in rates.

The CLD is also concerned that if the proposed IASB amendment to IAS 19 is approved, all entities will be required to recognize actuarial gains and losses immediately in income after the adoption of IFRS. Currently, under IAS 19, using the corridor method, an entity could avoid the immediate recognition of the full amount of actuarial gains and losses into income. There is however, a strongly supported proposed ISAB amendment to remove this option which would require all entities to immediately recognize actuarial gains and losses to other comprehensive income after the adoption of IFRS.

The CLD believes the Board should approve a generic account that would capture the one-time adjustment to the P&OPEB liability at the date of transition to IFRS, as well as establish a variance account for future actuarial gains and losses.

Issue #3 – Are there special implications associated with IFRS-related corporations tax or PILs impact during an IRM period for which additional IFRS transition related guidance is required from the Board?

The CLD provides no comment on this issue or the recommendation.

Issue #4 – Should the Board permit rate applications or RRR reporting using USGAAP?

The CLD provides no comment on this issue or the recommendation.

Issues Arising after Adoption of Modified IFRS

Issue #5 – Should the Board grant a generic deferral account, for utilities that have rebased under modified IFRS, for the impacts of changes resulting from new IFRS standards or changes in existing IFRS standards arising during an IRM regime?

Staff Recommendation

Board staff recommends that the Board not grant a generic deferral account for the impacts of changes resulting from new IFRS standards or changes in existing IFRS standards at this time. The CLD supports this recommendation.

The CLD notes that there is no reasonable way to anticipate the nature of new standards or changes in existing IFRS standards. There is also no reasonable way to anticipate the required nature or workings of a deferral account designed to manage these impacts.

The CLD does, however, encourage the Board to closely monitor activity related to IFRS standards and be proactive and timely in its efforts to engage stakeholders in consultation to address the impacts of such changes.

Issue #6 – Should the Board grant a generic variance account, for utilities that have rebased under modified IFRS, to mitigate volatility in certain expenses that may arise from the application of IFRS rules? In particular, differences in depreciation or amortization expense caused by changes in estimated useful life of in-service PP&E or intangible assets included in rate base, gains and losses arising from early retirement of in-service assets and differences in pension and post-employment benefit expenses should be considered.

Staff Recommendation

Board staff recommends that no generic variance account be established to mitigate the volatility that may be created by the application of IFRS rules. Further, that, utilities that do experience, or can demonstrate a likelihood of, significant ongoing volatility can apply to the Board for utility-specific relief.

CLD does not support the Board staff recommendation.

The issue is worded as a mechanism to mitigate volatility in certain expenses that may arise from the application of IFRS rules but CLD submits that the particular examples cited may have added complexities.

There are 3 specific examples provided. Two relate to volatility in amortization expense and the other relates to differences in pension and post-employment benefit expenses.

1. Differences in depreciation or amortization expenses caused by changes in estimated useful life of in-service PP&E or intangible assets

Depreciation of approved rate base investments (deemed prudently incurred by the Board), included within a distributor's revenue requirement, is the mechanism for distributors to recover the cost of those distribution asset investments. The recovery of approved investments through depreciation has not been considered a cost for which the distributor is 'at risk' during an IRM period. If the historic investment was deemed prudent and approved by the Board, sound regulatory rate making principles support recovery of this investment and a regulated rate of return on the utility's investment.

If the new accounting regime requires that the recovery of the investment (through depreciation) is increased during the IRM period to an amount above what is funded within the current revenue requirement AND there is no mechanism for adjusting for that additional depreciation at rebasing, the distributor will be unable to recover its investment and the associated return.

Under Board staff proposal for Issue #2, rate base at rebasing is calculated on an MIFRS basis (Point 3 of the recommendation - "*For that rebasing year, and every subsequent year, rate base will be calculated on a MIFRS basis.* ").

Without an adjustment to account for the accelerated depreciation within the IRM period, the MIFRS rate base will be lower and both depreciation and return in the future would be set on this lower value. On this basis, the distributor would never be able to recover that portion of the capital costs or return on capital expenditures deemed prudently incurred and previously approved in rate base.

The CLD submits that without such an adjustment mechanism, namely a variance or deferral account, distributors would be unfairly experience loss of capital due simply to the change in accounting regime.

2. Gains and losses arising from early retirement of in-service assets

Currently under CGAAP and the 'pooled asset' basis of accounting, early retirements of in-service assets do not trigger a removal of the associated net book value from the distributor's PP&E accounts. Rather, the asset's value remains in rate base until fully recovered through depreciation.

Under IFRS, the value of the retired assets is reported for financial purposes as a loss on disposition. Under MIFRS, the loss is reclassified as depreciation expense.

Should early retirements occur under IRM, a situation similar to 1. above occurs, in that the PP&E values of rate base are reduced at the next rebasing. With no mechanism for recovering that additional "depreciation" at rebasing, the utility would again unfairly experience loss of capital.

Distributors currently have limited or no historical information on the dollar value of early retirements as recognition for regulatory accounting purposes was not required.. It is unlikely, then that distributors would be able to accurately forecast these values for inclusion in cost of service applications. The Board and intervenors are equally unlikely to accept a forecast based on such poor data.

Even with a forecast in place there could still be considerable variance of actual results relative to the forecast, and that would create unjustified, windfall losses and corresponding gains for utilities and ratepayers, due simply to the change in accounting regime.

The CLD submits that the rate base impacts arising from examples 1 and 2 above are no different in nature than those arising from first time adoption of IFRS that Board staff propose be addressed through a deferral account in their recommendation under Issue 2. While the magnitude and frequency may be unknown, the same principles should be applied.

3. Differences in pension and post-employment benefit expenses (P&OPEB)
   Upon adoption of IFRS, any unamortized actuarial gains or losses related to pension and post-employment benefit expenses must be recognized by distributors. After adoption, in future cost of service applications, a distributor would presumably forecast the actual expense for pension costs and post-employment benefit expenses.

   CLD employees are members of the OMERS pension plan which is a multi-employer plan and as such, is treated as a defined contribution plan. These costs tend to be predictable, although changes in rates do occur and can be significant.

   The liability and expense related to other post-retirement benefits are determined based on actuarial studies. Currently, these expenses include the costs of benefits accruing in the current year (current service cost), interest expense plus the amortization of some unrecognized past service costs and actuarial gains or losses. As discussed under issue 2 on page 4, under IFRS, past service costs and actuarial gains or losses likely will be recognized immediately in income. These increases or reductions in costs, which can be material, may never be reflected in rates if not captured in a variance account. The CLD supports the establishment of a variance account to record significant changes in post retirement benefit costs relative to the costs in rates.

Alternative

Based on the reasons provided above in examples 1 and 2, the CLD does support the proposed alternative of the establishment of a variance account to record the discrepancy between costs recorded in the PP&E accounts and costs built into rates for these assets that arise due to the early retirement of assets.

The CLD further suggests that the scope of this variance account be expanded to include the discrepancy in depreciation expense on approved rate base during the IRM, due to changes in estimated useful life of in-service PP&E or intangible assets, and the value of depreciation expense that was built into rates for those assets during the IRM period.

The CLD does not agree with the proposed sunset date of 2016 for recording entries into the variance account. Board staff has provided no strong rationale in support of this arbitrary end date. The CLD submits that, in fact, the establishment of a sunset date to

such an account would invariably result in the circumstances outlined above where distributors would be at risk of not recovering investments that have been deemed prudently incurred and for the loss of the associated return.

Issue #7 The Board Report in issue 10.4 states "Utilities under incentive regulation are required to include in their annual RRR filing a reconciliation of reported annual performance to the same basis of accounting as that upon which the incentive framework was approved". Does this mean that a reconciliation from modified IFRS, as reported under RRR, to CGAAP must be performed and filed each year of an IRM period? Or is a reconciliation for the first year of RRR reporting under modified IFRS sufficient? What level of audit assurance should the Board require for this reconciliation?"

Staff Recommendation

Board staff outlines 4 specific recommendations related to reconciliation requirements.

1. One time reconciliation between the 2011 CGAAP audited financial statements figures and the 2011 IFRS audited financial statement figures – to be submitted with the RRR reporting for 2012 – Audit assurance provided by an external auditor to the "review level of assurance" specified in the CICA Handbook.

   The CLD supports the Board staff recommendation.

2. A one-time mapping and reconciliation between the 2011 uniform system of account (USoA) balances and the 2011 IFRS audited financial statements comparative figures (reported as part of the 2012 IFRS audited financial statements) – to be submitted with the RRR reporting for 2012 – Audit assurance provided by an external auditor to the "review level of assurance" specified in the CICA Handbook.

   The CLD supports the Board staff recommendation in part. The CLD agrees that a one-time mapping and reconciliation of the 2011 USoA balances to the 2011 IFRS audited financial statements should be completed and submitted.
   The CLD does not support the requirement for audit assurance to the "review level of assurance".
   For financial statement purposes, many distributors do not use the prescribed USoA, but rather another set of ledger accounts. For regulatory reporting requirements, amounts are mapped or allocated to the prescribed USoA as per guidance provided in the Accounting Procedures Handbook (APH). The CLD believes that currently, external auditors do not include a review of a distributor's allocations to the prescribed USoA, nor of RRR filing information. Currently, the distributors' provision of a reconciliation and mapping of RRR information to audited financial statements is considered sufficient assurance by the Board.
   The CLD submits that Board staff has not provided sufficient rationale to support the value to the Board of an external audit review of a distributor's mapping and reconciliation.
   For external auditors to review the mapping and reconciliation would require them to gain a level of expertise in the application of the APH and the use of the

USoA. This would be a new requirement that would unnecessarily increase audit costs for distributors.

3. Where an electricity distributor has not rebased under modified IFRS, a reconciliation be provided each year during an IRM period for Group 1 deferral and variance accounts between amounts recorded under CGAAP and modified IFRS – to be submitted with the RRR reporting for each year beginning with the year of adoption of IFRS – Audit assurance provided by an external auditor to the "review level of assurance" specified in the CICA Handbook.

   The CLD supports the recommendation that a reconciliation be submitted, but not the requirement for audit assurance to the "review level of assurance". The value to the Board of the audit assurance noted above is unclear compared to the added complexity and costs of audit services.

4. For all distributors, a reconciliation be required for the balance reported in the RRR, in the deferral account created to record differences in PP&E arising from the transition from CGAAP to MIFRS (proposed in Issue 2). The reconciliation would be required up to and including the year of first rebasing under MIFRS.

   The CLD supports the Board staff recommendation in part. The CLD agrees to the requirement of the reconciliation, but submits that the reconciliation would be required up to and including the last historic year prior to a distributor's rebasing under MIFRS, but not for the bridge and test years.
   As recommended by CLD in the discussion of Issue 2, the bridge and test year entries to the deferral account should be forecast values (as filed in evidence in a utility's rebasing application) and not subject to true up. On that basis, no reconciliation would be required for the deferral account for the bridge and test years.

Should the Board determine that audit assurance provided by an external auditor to the "review level of assurance" specified in the CICA Handbook is required for any or all of the above reconciliation items, the CLD submits that any additional costs arising from these requirements be considered as "Administrative one-time transition" costs and be eligible for inclusion within the Board established deferral account for such costs.

Alternative

The CLD does not support the proposed alternative that distributors are to file RRR information in both CGAAP and MIFRS format for several years, to support the Board's ability to benchmark utility performance over the transitional period. The CLD submits that it is generally understood that all of the subject distributors will be adopting IFRS in 2012. Therefore, the change in OM&A costs due to IFRS, and hence, RRR reporting, will occur at the same time for all distributors. While it is true that the magnitude and impacts of those changes will vary across distributors, it is also true that application of CGAAP principles currently varies across utilities and has various resulting impacts on OM&A levels. These variations currently hinder comparability across distributors. With all distributors reporting RRR information on a consistent basis (MIFRS) at the same time, comparability will improve. The CLD further submits, as Board staff did in the

rationale for their recommendation, that the use of a three year average for OM&A costs will provide some smoothing of the magnitude of impacts.
CLD submits that the added cost of maintaining high level CGAAP values for all RRR information for multiple years for benchmarking purposes would be significant and not of sufficient benefit to stakeholders.

Issue #8 – Should the Board in some forum consider potential adjustments to the IRM methodology related to the transition to IFRS in the upcoming work of the Board? For example, the basis for the types of relief listed in Issue 1 in the paper may have to be reconsidered (X and & factors, ICM, off-ramps, ROE deadbands and thresholds for disposition of deferral and variance accounts).

The CLD provides no comment on this issue or the recommendation.

Yours truly,

(Original signed on behalf of the CLD by)

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