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

Dear Ms. Walli:

Re: EB-2008-0408 – Comments of the London Property Management Association and the Building Owners and Managers Association of the Greater Toronto Area in the Consultation on Transition to International Financial Reporting Standards and Consequent Amendments to Regulatory Instruments

A. INTRODUCTION

These comments are provided on behalf of the London Property Management Association ("LPMA") and the Building Owners and Managers Association of the Greater Toronto Area ("BOMA") related to the Staff Proposal related to the transition to International Financial Reports Standards ("IFRS") and the consequent amendments to regulatory instruments required for rate making.

BOMA & LPMA has been actively involved in this consultative, including participating with other ratepayer groups as part of the "Group of 8 Ratepayer Groups".

B. PRINCIPLES

BOMA & LPMA are in general agreement with the principles as set out in the Staff Proposal, with one exception as noted below. These principles have been included below and comments on them have been provided following the each of them.

1. The methodologies used by the Board to establish just and reasonable rates have not always been the same as those used for external financial

reporting purposes. The Board has and will retain the authority to establish regulatory accounting and regulatory reporting requirements. IFRS accounting requirements will not be the sole driver of regulatory requirements.

BOMA & LPMA strong support this key principle. The Board needs to distinguish regulatory accounting from financial accounting. Regulatory accounting is required to allow the Board to establish just and reasonable rates. Financial accounting is required for external reporting purposes. As a number of participants indicated throughout the consultative, financial reporting is rarely used to set prices on a going forward basis. Companies that operate in competitive markets do not set their prices based on their past financial accounting results. In fact, the opposite occurs. These companies adapt their costs and operating practices to reflect the revenues that can be obtained at the prices that the market will bear. Financial accounting then reflects the degree of success (or failure) of the company's operation. The return on equity falls out of this financial accounting.

Regulatory account, on the other hand, has been established and has evolved as a key component of setting just and reasonable rates on a forward looking basis. Forecasts of operating costs and practices, including a forecasted return on equity, are used to set rates that can be charged by the regulated company.

The Staff Proposal states, as part of this principle, that *"IFRS accounting requirements will not be the sole driver of regulatory requirements."* BOMA & LPMA submit that it would be more appropriate to state that the determination of just and reasonable rates continues to be the primary driver of regulatory requirements.

2. Future regulatory accounting and regulatory reporting requirements established by the Board will continue to be based on sound regulatory principles. These principles include fairness, minimizing intergenerational inequity and minimizing rate volatility.

BOMA & LPMA agree with this principle. Sound regulatory principles are the foundation to good regulation and should continue regardless of accounting changes.

3. Future regulatory accounting and regulatory reporting requirements established by the Board will, in taking into account IFRS requirements, balance the effects on both customers and shareholders.

BOMA & LPMA strongly support this principle, but believe it does not go far enough. In their submission to the Board in EB-2008-0104 (Consultation for the Transition of Regulatory Accounting to International Financial Reporting Standards) dated October 29, 2008 Enbridge Gas Distribution stated (at page 4) *"EGD highly stresses that any regulatory processes and definition changes approved by the Board must ultimately leave the rate regulated entities* ***unharmed*** *from a financial perspective."*

BOMA & LPMA submit that it is equally important any regulatory processes and definition changes approved by the Board must also ultimately leave the ratepayers unharmed from a financial perspective as well. Changes in accounting practices or rules should not result in changes in rates. As noted above, financial accounting is not used to set future rates. Changes in financial accounting should not, therefore, result in changes to future rates.

4. Future regulatory accounting and regulatory reporting requirements established by the Board will be aligned with IFRS requirements as long as that alignment is not inconsistent with sound regulatory rate making principles.

BOMA & LPMA disagree with this principle as stated. This principle appears to assume that IFRS is the default and that regulatory accounting and reporting requirements would be changed to reflect IFRS requirements as long as they are **not inconsistent** with sound regulatory rate making principles.

It is submitted that the current regulatory accounting policies and reporting requirements should remain the default until it is determined that adoption of the IFRS requirements are **consistent** with sound regulatory rate making principles.

An analysis would be required to demonstrate that adoption of the IFRS requirements were consistent with sound regulatory rate making principles. The Staff Proposal to adopt the IFRS requirements as the default does not appear to do this analysis.

After it has been demonstrated that adoption of the IFRS requirements are consistent with sound regulatory rate making principles then it would be likely that IFRS would be adopted as the regulatory policy. This would be because there would be an administrative burden from having a regulatory policy that differs from IFRS. Minimization of this regulatory burden and the associated costs that are passed on to ratepayers is a sound regulatory objective. If IFRS is consistent with sound rate making principles then there is no reason not to adopt it as the regulatory policy.

On the other hand, if it cannot be demonstrated that the IFRS requirement is consistent with sound regulatory rate making principles, then the administrative burden associated with having a regulatory policy that differs from IFRS may well be justified.

BOMA & LPMA suggest that this principle should be re-worded as follows:

"Future regulatory accounting and regulatory reporting requirements established by the Board will be continued as is and will be aligned with IFRS requirements only when it has been established that such alignment is consistent with sound regulatory rate making principles and do not have a material impact on ratepayers."

BOMA & LPMA note that the Group of 8 Ratepayer Groups has developed an Evaluation Framework that would provide the information needed to evaluate a proposed change in regulatory accounting policy and focus the discussion on the criteria that reflect sound regulatory rate making principles.

5. Future regulatory accounting and regulatory reporting requirements established by the Board will be universal and standardized for all utilities, while recognizing that utility-specific issues can be addressed through a utility's applications.

Assuming that government controlled enterprises will be subject to IFRS, BOMA & LPMA agree with this principle. However, should government controlled enterprises be exempt from IFRS, then BOMA & LPMA submit that the Board should rethink this principle. As the majority of distributors in Ontario are government owned, a change to their IFRS reporting requirement should cause the Board to re-evaluate this principle.

BOMA & LPMA also note that there are some regulated distributors in Ontario that may not be subject to IFRS. If the adoption of IFRS by these distributors for OEB purposes results in an increase in rates to ratepayers, the Board should rethink this requirement as well. In such a case the only driver of a change to IFRS is an artificial requirement of the OEB that results in increased rates. This would not appear to result in just and reasonable rates.

C. MAJOR POINTS OF DEPARTURE BETWEEN EXISTING REGULATORY ACCOUNTING AND RATE MAKING AS COMPARED TO IFRS

BOMA & LPMA are providing comments on each of the issues in section 2 through 10 of the Staff Proposal paper.

2. Regulatory Assets and Liabilities

2.1 Should the Board continue to use deferral and variance accounts in the event that they are not recognized under IFRS?

BOMA & LPMA agree with the Staff Proposal that the Board should continue to use deferral and variance accounts for rate making in appropriate circumstances regardless of whether or not these accounts are recognized for IFRS reporting purposes. Deferral and variance accounts are key regulatory instrument that allows distributors to recover costs over an appropriate period of time to match the benefits provided and also allow variances to be recovered when circumstances beyond the distributors control occur. This approach is an essential component of ensuring that rates for consumers are just and reasonable.

2.2 Should the Board approve definitions for deferral and variance accounts if the Board retains their use for regulatory purposes?

BOMA & LPMA agree with the Staff Proposal that the Board should continue it current practice in the use and establishment of such accounts. When more information is received from the International Accounting Standards Board ("IASB"), the Board should then review its current practices to see if any changes are required or desired.

BOMA & LPMA note that the Staff Proposal indicates that utilities **may** use appropriate financial reporting methods to increase the understanding of the nature of deferral and variance accounts within the financial community, such as increased disclosure in the notes to audited financial statements, increased management discussion and analysis in annual reports and the education of financial professionals.

BOMA & LPMA submit that the word "may" should be changed to "should" in the Staff Proposal. Further, it is submitted that the Board should actively participate in the education of financial professionals with respect to deferral and variance accounts. The Board should also consider the preparation of a generic statement regarding deferral and variance accounts from the Board's perspective that could be included in the notes to audited financial statements and annual reports for the distributors. Inclusion of such a generic statement across distributors may help the understanding of the issue by the financial community.

3. Property, Plant and Equipment

3.1 For the purpose of first-time adoption of IFRS, should the Board require historic cost (NBV) or the IFRS adoption requirements (fair value or retrospective restatement) to be used as the basis for setting opening rate base values and reporting to the Board?

BOMA & LPMA agree with the Staff Proposal that the regulated net book value is to be used as the basis for setting opening rate base values and reporting to the Board at the time of the first report to the Board or rate application for periods subsequent to the adoption of IFRS. The detail provided should include gross capital costs and accumulated depreciation and should continue to be provided at the level of detail required to support regulatory accounting requirements as established by the Board.

If a distributor chooses to use something other than historic cost (net book value) such as fair value or retrospective restatement that is not equal to net book value upon first-time adoption of IFRS, then the Board should ensure that any one-time costs and any on-going administration costs related to this difference are borne solely by the shareholder. A corporation may have valid reasons for adopting something other than net book value for the purpose of first time adoption of IFRS. However, it would be unfair, in the view of BOMA & LPMA, to impose additional costs on ratepayers as the result of a decision made for corporate purposes. These costs should be to the account of the shareholder.

3.2 After adoption, what should be the basis for reporting PP&E for regulatory purposes (e.g. historical acquisition cost, fair value)?

BOMA & LPMA support the use of historical acquisition cost as the basis for report property, plant and equipment for regulatory purposes on a going forward basis. As noted above, it is further submitted that if a distributor adopts a different approach (for example, fair value), then any and all administration costs should be borne by the shareholder and not the ratepayers. A corporation may have valid reasons for adopting an approach that differs from historical acquisition costs. However, since this decision is driven by corporate objectives, the costs should be borne exclusively by the shareholder.

3.3 Should the Board require PP&E to conform to IFRS capitalization requirements (e.g. capitalize less indirect overhead and administration cost)?

The Staff Proposal is that distributors would be required to adhere to IFRS capitalization accounting requirements for rate making and regulatory reporting purposes after the date of adoption of IFRS.

BOMA & LPMA believe it is premature for the Board to decide on this issue at this time. The Staff Proposal may well be appropriate, however, at this time, it is the submission of BOMA & LPMA that the Board does not have sufficient information to make an informed decision on this matter.

Capitalization involves a broad spectrum of issues and interpretations. The issues include the amount, if any, of overhead costs that should be capitalized to whether or not training costs associated with new systems should be capitalized. As the Board is aware, current capitalization policies of the distributors vary widely across the province.

Whatever capitalization policy the Board ultimately requires, it is submitted that the Board should provide all distributors with more direction on the amounts that should and should not be capitalized. Greater consistency across distributors of whatever policy is adopted should be encouraged.

At this point, the Board does not have any evidence of what the rate impact may be of adoption of the IFRS capitalization policies. All that parties to this consultation have been told is that rates would likely increase in the short term as more costs are expensed than have been in the past. This would be offset over time, through lower depreciation costs and cost of capital associated with a lower rate base decreasing rates over the long term. However, there is no indication of the magnitude of the short term increase in rates that may result from adoption of IFRS capitalization for rate making purposes. In addition, since most utility assets are long lived, with useful lives of 40 years or more, it may be that the decrease in rates in the longer term may not occur until 20 years from now, which is approximately half the expected lives of the utility assets.

BOMA & LPMA submit that the Board should direct a representative cross section of the distributors to provide a detailed estimate of the impact on their revenue requirement of changing to IFRS capitalization. This information should be provided to all interested parties. The Board should then deal with this change through the Evaluation Framework as proposed by the Group of 8 Ratepayer Groups.

3.4 What changes to existing regulatory or rate making treatments should the Board require for other PP&E related items as a result of the adoption of IFRS?

- **Borrowing costs applied to PP&E (as opposed to deemed interest or AFUDC)**

BOMA & LPMA believe that the actual interest cost incurred for construction work in progress is the appropriate amount to be capitalized. The current situation involves the use of a deemed interest rate. As a result, a distributor could incur costs that were in fact, not incurred. On a going forward basis, regardless of the IFRS requirements, BOMA & LPMA submit that any interest cost capitalized must be costs that were actually incurred for the construction work in progress. Distributors should not be able to "allocate" interest costs associated with their long term or short term debt used to finance rate base. This would be double counting of interest and result in higher rates for ratepayers. If a distributor does not borrow to finance the construction work in progress then no interest cost should be capitalized since there was no cost.

In addition, if affiliate debt is used to finance construction work in progress, the interest rate used should match a market rate, such as that available from a bank or Infrastructure Ontario. The Board should disallow any capitalized interest from an affiliate that is in excess of the rate which could have been obtained through a third party.

- **Customer contributions received for PP&E**

BOMA & LPMA support the intent of the Staff Proposal that customer contributions for regulatory reporting and rate making purposes be treated as deferred revenue to be included as an offset to rate base and amortized to income over the life of the facility to which the contributions relate.

However, it is unclear to BOMA & LPMA that the Staff Proposal results in no difference in rates as compared to the current treatment where the contributions are a direct reduction in rate base and are amortized over the life of the asset. BOMA & LPMA have two concerns related to the proposal.

First, assuming that the amount amortized to income each year over the life of the facility to which the contribution relates equals the depreciation expense associated with the facility there would be no net change in the revenue requirement. However, as noted under the Depreciation category of the Staff Proposal, depreciation rates can and may change on a yearly basis. It is not clear to BOMA & LPMA that the amount amortized to income each year would or could also change on a yearly basis to match the amount of depreciation. If it can, then the amount amortized to income and the depreciation expense should offset one another. If not, then there would be a rate impact that could vary from year to year.

Since the depreciation expense may change on a frequent basis for the assets that have attracted capital contributions, this would change the net book value from that where the depreciation expense did not change. In order for this approach to remain rate neutral, the deferred revenue may have to be adjusted to reflect a changing depreciation expense (and a changing amount amortized to income each year).

Second, as long as the remaining deferred revenue is netted off of the net book value to determine rate base then there should be no impact on the cost of capital associated with the rate base. However if the cost of capital is determined based on net book value before the reduction associated with the deferred revenue amount there would be a negative rate impact to customers. This is because the net book value attracts a cost of capital equal to the weighted average cost of capital for the company (short term debt, long term debt & equity) whereas the deferred revenue would only attract interest at a short term debt rate. Over time this difference would become significant, given the significant levels of customer contributions received by some distributors.

- **Asset reclassifications from PPE to intangible assets (e.g., computer software and land rights).**

BOMA & LPMA agree that any assets that are reclassified from PP&E to intangible assets should be included in rate base and the amortization expense should be included in the depreciation expense for calculating the revenue requirement. This reclassification will preserve the continuity of rate base. Unlike the situation for capital additions noted above, there does not appear to be any impact on rates of this change.

- **Asset retirement obligations**

BOMA & LPMA support the Staff Proposal that for rate setting and reporting requirements the distributors shall identify separately the depreciation expense associated with the amortizing the asset retirement cost and the accretion expense associated with the amortization of the asst retirement obligation.

- **Gains and losses on disposition of assets**

BOMA & LPMA support the Staff Proposal with respect to the gains and losses on the disposition of assets. The Staff Proposal appear to continue to the existing methodology used by many distributors.

However, it appears that this proposal may result in a rate base that would deviate over time from the net book value of the assets on the financial statements of a distributor. For regulatory purposes, the gain or loss is accounted for in depreciation expense which would impact on accumulated depreciation and net book value for rate base purposes. For accounting purposes it would appear that there would be no depreciation expense change, but rather the gain or loss would be accounted for as a charge or credit to income.

The Board should review this issue to see if the cumulative impact over time is significant or not.

- **Treatment of asset impairment**

BOMA & LPMA support the Staff Proposal.

<u>4. Depreciation</u>

4.1 Should the Board set parameters for depreciation accounting for regulatory purposes (e.g. depreciation methods, the level at which sub-componentization should be applied to specified asset classes)?

BOMA & LPOMA support the Staff Proposal that distributors should continue to use the straight line method of depreciation.

However, it is not clear to BOMA & LPMA that a joint depreciation study would result in depreciation methodologies and rates which would be consistent with IFRS requirements. This is discussed further under 4.2 below.

4.2 Should the Board set the parameters for electricity distributors to establish their own depreciation rates rather than continue to use depreciation rates historically provided by the Board (co-ordination of depreciation studies may be possible)?

BOMA & LPMA are concerned with the intent to use a joint depreciation study for the electrical distribution utilities as recommended by Staff. While such a study could be used to determine the methodologies that would be applied by all electrical distribution utilities, it is not clear that a set of rates can or should be calculated to apply to all utilities. It is also unclear that such a process would result in depreciation rates that would be consistent with IFRS requirements.

It is highly unlikely that the same depreciation rates for any set of assets would be the same across electrical distributors. Depreciation rates are based on a number of factors including the total service life of the assets, the weighted average age of the assets, the resulting estimated remaining life of the assets, the salvage value or salvage costs and the net book value of the assets (which reflect past depreciation rates). These factors will all be unique to a utility. Therefore, depreciation rates will be different for utilities. It is doubtful that under IFRS reporting requirements, depreciation rates that are based on the Ontario-wide sector rather than on the specific utility would be acceptable. The balance sheet of the utility should reflect its unique circumstances. Using depreciation rates that are not based on the circumstances of the utility could not result in accurate balance sheets for these distributors.

Consider, for example, the depreciation rates of the gas utilities. None of the depreciation rates for Union and Enbridge are the same. Even where the total service life of an asset category is the same between the two gas utilities, the average age of those assets differ between them. Salvage costs can also be significantly different. Removing a gas pipeline from under Yonge Street in downtown Toronto is likely to be more expensive than removing the exact same pipeline from under Main Street in downtown Dutton. All of these factors, and more, result in different depreciation rates for Union and Enbridge. It is doubtful that under IFRS either utility could use depreciation rates that reflect both their own situation and the situation of the other utility. In this example, one utility would have a lower depreciation rate and the other would have a higher depreciation rate than they would have if they used their own specific rate. The balance sheets of both companies would be inaccurate be definition.

BOMA & LPMA note that the Staff Proposal related to depreciation studies for the gas utilities should include proposals related to the treatment of items unique to the gas industry. Cushion gas is provided as an example of these unique assets. It should be pointed out that cushion gas is a non-depreciable asset and would not be included in a depreciation study.

5. Other Issues

5.1 What changes to existing regulatory accounting and rate treatments should the Board require for other items?

- **Inventory valuation (based on lower of cost and net realizable value)**

BOMA & LPMA agree with the recommendation that for gas utilities the Board should continue to current practice of recording the difference between the actual purchase price of gas inventory and the weighted average cost of gas in a variance account for future disposition to customers when approved by the Board.

- **Payments in lieu of corporate income taxes**

BOMA & LPMA support the continuation of the current practice of using estimated taxes (or PILS) for inclusion in the revenue requirement for rate setting purposes. BOMA & LPMA also support the recovery of future income taxes (or PILS) when they become payable, as determined and approved in a future rates proceedings.

- **Pensions and employee future benefit costs**

BOMA & LPMA support the continuation of the current practice of reviewing pension and employee future benefits costs in rate applications.

6. Decisions of Accounting Standard-Setting Bodies

6.1 What are the potential implications on the Board's decisions of the questions now before accounting standard-setting bodies? These uncertainties include:

- **Potential exemption from the requirement for retrospective or fair value restatement of PP&E (International Accounting Standards Board)**

BOMA & LPMA support the proposed policy choice as outlined on issue 3.1 of the Staff Proposal paper, regardless of the decision from the IASB.

- **Recognition of regulatory assets and liabilities, e.g., deferral and variance accounts (International Accounting Standards Board)**

BOMA & LPMA support the proposed policy choice as outlined on issue 2.1 of the Staff Proposal paper, regardless of the decision from the IASB.

- **Whether accounting standards will require municipal and provincial government-owned distributors (government business enterprises) to adopt IFRS (Public Sector Accounting Board – Canada)**

As noted above in the Principles section, BOMA & LPMA submit that the Board should remain open to changes in its requirements related to government owned distributors should IFRS not become the default accounting requirements for these entities.

- **Other developments from accounting standard-setting bodies.**

BOMA & LPMA submit that as other developments occur, they should be evaluated using the Evaluation Framework as described by the Group of 8 Ratepayer Groups to determine if they represent sound regulatory rate making principles.

7. Rate Impact

7.1 Compared to rates established under current regulatory accounting, what are the direction and estimated magnitude of rate impacts created by establishing rates on the basis of various IFRS accounting options?

BOMA & LPMA agree with Staff that the potential rate impacts of adopting IFRS will vary from utility to utility. At this point in time, the potential rate impacts are not known and cannot be reasonably estimated with any degree of certainty.

It is therefore reasonable to expect that utilities will specifically identify any differences in the revenue requirement that relates to adoption of IFRS requirements in their first cost of service rate filing after IFRS adoption. This will be the only opportunity for all parties – the Board, intervenors and the utilities – to quantify the impact of IFRS on the revenue requirement.

7.2 Should a mechanism be developed to phase-in or otherwise mitigate the rate impacts, if any, of adopting IFRS?

The Board has extensive knowledge of rate mitigation techniques used in the past such as deferral accounts and amortization of amounts over a number of years. It is expected that these same techniques can be used to reduce rate impacts if required.

7.3 Should rate increase thresholds be set?

As noted by Staff, an aggregate of all the changes in a total bill of more than 10% may trigger rate mitigation. The IFRS-related costs would be considered part of the aggregate of these changes. BOMA & LPMA believe this approach is reasonable.

8. Utility and Shareholder Impact

8.1 Should the administrative costs (e.g. new systems, special audits, consulting) to transition to IFRS be recovered from ratepayers? On what basis?

BOMA & LPMA agree that all prudently incurred incremental costs directly related to the transition to IFRS should be recovered from ratepayers on the same basis as other costs.

When a utility is under an incentive rate mechanism, these costs should be recorded in a deferral account for review when the utility comes in for a cost of service rebasing application, or as part of their annual clearance of deferral and variance account balances. However, recording of these amounts in the accounts should not be construed as recovery of the balances will be approved.

A prudence review should be held to ensure that all the costs posted in the account were directly caused by the transition to IFRS, that they were prudently incurred and that they are material. With respect to materiality, BOMA & LPMA submit that the need to transition to IFRS is a clear example of a Z factor event. If the balance in the deferral account exceeds the materiality threshold then the account is eligible for clearance. If it does not meet the materiality threshold, then it should not be recoverable under IRM.

It should also be noted that the Board has already approved IFRS related costs for some utilities as part of the revenue requirement in 2009. In such instances BOMA & LPMA believe that the Board should establish variance accounts in which to record the difference between the actual costs incurred and those recovered in rates.

Staff has suggested that only incremental administrative costs incurred after January 1, 2009 should be eligible for recovery. BOMA & LPMA note that some distributors applied to the Board prior to January 1, 2009 requesting deferral accounts for incremental IFRS relate costs. The Board deferred these requests to this proceeding. BOMA & LPMA submit that to the extent that requests for deferral accounts were received by the Board, those distributors should be permitted to establish deferral accounts to record the costs incurred prior to January 1, 2009, starting at the date of the deferral account request.

8.2 Should incremental on-going compliance costs be recovered from ratepayers? On what basis (z-factor treatment? threshold amounts?)?

BOMA & LPMA agree that all prudently incurred incremental administrative costs directly related to the compliance with IFRS should be recovered from ratepayers on the same basis as other costs.

8.3 How can the Board encourage minimization of IFRS implementation costs?

As noted earlier, BOMA & LPMA do not support the concept of a joint depreciation study, but would support the concept of the development of a depreciation methodology to be used by distributors.

Without an analysis of the rate impacts of the differences between IFRS requirements and regulatory requirements, BOMA & LPMA cannot support the Staff Proposal that differences between the two should be minimized in order to minimize IFRS implementation costs. The added costs may be justifiable on the basis that they are less than the increase in costs resulting from harmonization.

BOMA & LPMA submit that a review of transition costs should be done on an industry wide basis. Such a review would highlight any distributors that are significantly above their peers. These distributors would be required to justify the difference in costs if they requested recovery from ratepayers.

The Board should actively participate with the distributors to ensure that information about what is being done and at what cost is circulated among the distributors while they are transitioning to IFRS. This would help ensure that all parties keep costs to a minimum.

8.4 Should any proposed increases in revenue requirement that may arise from changes in accounting for rate base and operating costs prompted by the adoption of modified IFRS be recovered from ratepayers? If yes, on what basis?

As noted above under the third Principle, BOMA & LPMA submit that any regulatory processes and definition changes approved by the Board should ultimately leave ratepayers unharmed from a financial perspective.

The more important question is whether this should occur on a year to year basis, or over a longer period of time. As discussed under the capitalization issue, some increase in rates over the immediate term could be offset by decreases in the longer term.

Until the rate impacts of the transition to the modified IFRS are known with a greater level of certainty than is now available to all parties, BOMA & LPMA submit that it is premature to deal with this issue. When all the facts are available and the impacts are known, then the Board should determine how the costs should be recovered, and from whom.

9. Filing Guidelines for Rate Applications

9.1 What are the filing requirements for rate applications for entities regulated by the Board during and after the transition to IFRS?

See comments under issue 9.4 below.

9.2 What financial filings should the Board require for use in cost of service rate applications for historical and test years subsequent to 2009?

See comments under issue 9.4 below

9.3 Should the Board prescribe any specific rate making measures in its incentive regulation mechanisms to take account of the adoption of IFRS?

BOMA & LPMA do not believe that any specific rate making measures are needed in the incentive regulation mechanisms to take account of the adoption of IFRS. Deferral accounts (or variance accounts) will be established to account for the costs related to the implementation costs incurred. These deferral accounts should be treated as Z factors under the IRM mechanism. If they meet the materiality threshold, the prudently incurred cost should be recovered from ratepayers. If they do not meet the materiality threshold, they would not be eligible for recovery.

9.4 Should rate applications under an incentive regulation mechanism be required to include a reconciliation of reported annual performance to the same financial reporting standard as that upon which the incentive framework was approved?

BOMA & LPMA have reviewed the filing guidelines as proposed by Staff. With respect to the electricity distribution rate application filings, BOMA & LPMA agrees with the Staff proposals, with the exception of the requirements for rebasing for 2011 rates. Staff proposes that distributors rebasing for 2001 rates should file forecasts under both the current regulatory framework and on the basis of modified IFRS. It is submitted that this approach is problematic. The 2011 rebasing applications will be filed in August of 2010 and most of the forecasts that make up the filing will be done in early to mid 2010. It may not be realistic to expect distributors to be able to file on the basis of a modified IFRS when the rules may still be evolving, the financial reporting systems may not be in place or verified and staff will be unfamiliar with the concepts. BOMA & LPMA submit it may be more practical to allow the distributors making applications for rebasing for 2001 rates to use only the current regulatory framework. Any utility wishing to provide the filing both ways should be allowed to do so.

BOMA & LPMA note that the final group of distributors that will be rebasing as part of the first cycle of the third generation IRM will be filing in 2010 for rebasing of 2011 rates. These distributors should be allowed to file based on the current regulatory framework, the same as those that filed for 2008 and 2009 rates rebasing and as those who will file for 2010 rates rebasing. This would allow all distributors to rebase once using the current regulatory framework. Then, starting with the 2012 filings (in the summer of 2011), distributors would file forecasts under both the current regulatory framework and on the basis of modified IFRS.

BOMA & LPMA agree with the Staff proposal for those distributors making applications for rebasing for 2012 and subsequent year rates. In particular, the filing of 2010 actual historical results would be based on both the current framework and the modified IFRS framework.

It should be pointed out however, that the Staff approach does provide somewhat of a discontinuity between 2011 rate year filers and 2012 and subsequent year rate filers. In particular, the 2011 rate year filers will be filing a test year forecast that will be used to identify any financial differences and any resulting revenue requirement impacts that may arise from the adoption of the modified IFRS requirements. 2012 and subsequent year rate filers would be providing this comparison on the basis on a historical year and not on the basis of the forecast test year. The Board may want to consider whether this is appropriate.

Turning to the gas distributors, for those with earnings sharing mechanisms in place (i.e. Union Gas and Enbridge Gas Distribution), Staff is recommending for the rebasing test year the distributors would file forecasts under both the current regulatory framework and on the basis of modified IFRS. The distributors would also identify financial differences and any resulting revenue requirement impacts that arise from the adoption of modified IFRS requirements. BOMA & LPMA support this proposal. It will ensure a comprehensive comparison of the existing regulatory framework and modified IFRS on a test year basis. This is preferable to a comparison on a historical or bridge year basis.

Of equal importance to BOMA & LPMA is the Staff Proposal that these distributors continue to present all required IRM application filings materials using the current regulatory framework while the current IRM is in place. This is important because of the earnings sharing mechanisms that are in place for both Union and Enbridge. The calculations underlying the earnings sharing are based on the current regulatory accounting principles and practices. It would not be possible, in the view of BOMA & LPMA, to change regulatory frameworks part way through the IRM period without there being some impact on the earnings sharing mechanism. A comparison of both methods in one year would not be adequate to make the jump to the modified IFRS approach, as the modified IFRS approach is likely to diverge from the current regulatory framework more and more from one year to the next due to the impacts of accumulated differences.

The Board may want to consider requiring Union and Enbridge to file their 2010, 2011 and 2012 results using both the current regulatory framework and the modified IFRS framework. Both of these utilities will have modified IFRS results available for these years under the IRM mechanism. These three historical years, combined with the test year of 2013 for the next rebasing applications would provide the Board with an invaluable look at the difference in the revenue requirements of the two frameworks over an extended period. The Board and other parties would be able to see if the difference between the two methodologies is constant on a year to year basis, whether the difference fluctuates randomly, or whether the difference grows over time.

10. Electricity Distributor and Gas Utility Reporting and Record-Keeping Requirements (RRR)

10.1 What changes are required to financial reporting requirements for entities regulated by the Board during and after the transition to IFRS?

See comments below.

10.2 Should the Board require all rate-regulated entities to report information to the Board using IFRS beginning January 1, 2011, regardless of whether they are otherwise required to use IFRS?

BOMA & LPMA believe that consistent reporting should be encouraged. However, should some distributors not be required to use IFRS, the Board may want to consider whether it is appropriate to impose additional costs that are purely OEB driven on the ratepayers of those distributors.

10.3 Should the Board require all rate-regulated entities to continue to report information to the OEB using Canadian GAAP until December 31, 2010 (regardless of early adoption by the utility)?

Yes. This will provide a consistent set of distributor data through 2010.

10.4 Should the RRR include requirements for reconciliations between financial reporting under IFRS and regulatory accounting information?

Yes. Reconciliations should be required as proposed by Staff. This would add to the level of comfort of the data provided.

10.5 Should the RRR include a requirement for supplementary audit assurance regarding regulatory accounting values where they differ from IFRS reported values and that are not otherwise audited?

Supplementary audit assurance regarding the regulatory accounting values that involves a full audit of regulatory accounting values by a third party should be required. This would add to the level of comfort of parties that the data is accurate.

10.6 Should the periodic reporting to the Board by utilities under incentive regulation include a reconciliation of reported annual performance to the same basis of accounting as that upon which the incentive framework was approved?

As noted in issue 9.4 above, BOMA & LPMA believe that reporting should be reconciled to the same basis of accounting as that upon which the incentive framework was approved. This is especially true for the gas utilities while their current IRM is in place.

D. OTHER ISSUES

BOMA & LPMA believe there is one other issue that the Board needs to review. This issue relates to differences between modified IFRS requirement and financial IFRS requirements that may occur on a year to year basis while a distributor is under IRM. As an example, base rates would be set using a number of Board approved parameters such as depreciation rates. While these Board approved depreciation rates would continue to be utilized by the distributor during the subsequent IRM years for regulatory accounting and reporting purposes, it may well be that the depreciation rates could change for financial reporting purposes, based on IFRS requirements. This would lead to a divergence in the annual depreciation expense and to an accumulated divergence in net book value.

It is the submission of BOMA & LPMA that the Board cannot ignore this potential difference. Consider the following as an illustrative example of the impact of a change in the depreciation rate during an IRM period. Rates are set based on a 4% depreciation rate for a specific class of assets during a rebasing year application. As a result rates in each of the following IRM years are based on this 4% depreciation rate and the impact it is on rate base through the accumulated depreciation impact on net book value. If the depreciation rate is subsequently lowered for IFRS purposes during the IRM period, the distributor is now over collecting from ratepayers since the depreciation rate has fallen from 4% to, say, 3.5%. If rate base is subsequently re-aligned with the IFRS value (which will be higher under the 3.5% depreciation rate scenario that it would have been under the 4% scenario), ratepayers will have paid higher rates during the IRM period and then will be paying higher rates in the rebasing and subsequent years because of the higher rate base. In fact, ratepayers would be paying for the difference in the depreciation expense twice. Similarly, if the depreciation rate were to be increased from the Board approved 4% level during an IRM period, the distributor would be under collecting from ratepayers relative to the depreciation expense being incurred for financial reporting purposes. Again, if rate base is subsequently re-aligned with the IFRS value upon rebasing, the rate base would be lower than what it would otherwise be. In this scenario, the distributor loses the depreciation expense difference and can never recover this difference.

In both scenarios provided above, the assumption is made that rate base would be re-aligned with net book value for IFRS reporting purposes. If this does not occur, then there would be no double paying by ratepayers or unrecoverable loss by distributors. However, it would mean the continued difference between net book values for modified IFRS regulatory reporting purposes and financial IFRS reporting purposes. In essence there will be a permanent regulatory asset created. The Board may wish to consider how it would deal with this specific issue as it relates to changes in depreciation rates during an IRM plan term. This is just one example of other issues that the Board should be prepared to deal with.

Please contact me if the Board requires any further information related to these comments.

Sincerely,

Randy Aiken

Randy Aiken
Aiken & Associates