ONTARIO ENERGY BOARD

CONSULTATION ON TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

Written Submission of Industrial Gas Users Association (IGUA)

Essential Position.

1. Transition by regulated distribution utilities to International Financial Reporting Standards (IFRS) for public reporting purposes should not, *per se*, result in material rate increases.

2. This should be one of the principles that guides the Board in development of its policy regarding how to adapt rate regulation to address the introduction of IFRS for utility public financial reporting.

3. IGUA takes this position based on the premise that a change in how financial information is reported does not change the underlying economics of delivering regulated service.

4. IGUA does, however, recognize that:

   (a) There will likely be one time administrative costs to utilities to switch their public financial reporting to IFRS, and, subject to prudence and reasonableness, these are legitimate costs of operating the utility and should be recovered from ratepayers.

   (b) If there are ongoing administrative costs to address differences between regulatory reporting and public reporting under IFRS, such ongoing administrative costs are also, subject to prudence and reasonableness, legitimate costs of operation of the regulated utility and thus properly recoverable from ratepayers.

5. Further, IGUA recognizes that there may be instances in which;

   (a) alignment of regulatory accounting with IFRS would best serve ratepayers, by minimizing utility administrative and/or overall regulatory costs, minimizing regulatory complexity, and/or minimizing opacity of regulatory reporting versus audited public financial reporting under IFRS; and

(b) such alignment may, as a result of timing differences between IFRS based regulatory reporting and current regulatory reporting, resulting in near term increases in revenue requirement.

6. In IGUA's view, all or any of the one time switchover costs, ongoing administrative costs, or revenue requirement impacts of timing differences associated with justified adoption of IFRS conventions to enhance regulatory reporting, should be subject to mitigation measures such that;

(a) aggregate near term IFRS related rate impacts, when combined with any other rate increases for a particular utility in the subject year, do not exceed the appropriate materiality threshold; and

(b) such IFRS related costs and revenue requirement impacts are spread over a sufficient time period such that ratepayers impacted by such regulatory changes over time bear their proportionate share of such costs.

7. A simplified example may assist to illustrate the way in which IGUA would approach application of these principles.

(a) The example assumes $5 million in annual system training costs. Under current regulatory accounting these costs are capitalized and recovered through depreciation expenses and return on equity. Under IFRS treatment these costs would be expensed in the year in which they are incurred.

(b) Assuming a five year depreciation period for each year's capitalized training costs, there is $5 million dollars of training costs recovered from ratepayers each year under current regulatory accounting ($1 million for each of the current year and the last 4 years). There would also be a return recovered in each year on the portion of training costs in rate base in such year (say $400,000 on $5 million in rate base, assuming an 8.5% return on rate base), for a total annual ratepayer cost of $5.4 million.

(c) If the Board were to direct IFRS treatment of training costs, IGUA understands that the entire $5 million incurred in the transition year, and each year thereafter, would be expensed to ratepayers as incurred. In the year of transition, the current year's $5 million of training expense would be added to the $4 million of depreciation for training capitalized in each of the preceding 4 years, plus a return on the previously capitalized training costs; say $340,000 (assuming $4 million in accumulated rate base times an 8.5% return).

(d) The in year impact in the transition year would thus be a total of $9.34 million expensed to ratepayers.

8. In this scenario, IGUA would submit that:

(a) The Board would first have to evaluate whether adoption of IFRS capitalization policies for regulatory purposes resulted in; i) appropriate matching of costs and benefits to current and future ratepayers; and ii) sufficient regulatory cost savings, regulatory simplification and/or financial clarity to warrant adoption of the IFRS convention at the expense of the resulting near term $3.94 million rate impact.

(b) In the event that the foregoing analysis indicated that it was in the ratepayers' long term interests for the Board to adopt IFRS capitalization policies for the purposes of regulatory reporting, then the Board should direct a mitigation approach that would smooth the rate impact of $3.94 million (the difference between the unmitigated in year impact of $9.34 million and the comparable in year impact of $5.4 million under the historical regulatory approach). The mitigation approach adopted should also consider other rate changes expected to occur over the same period of time.

(c) The period properly adopted by the Board for the purposes of smoothing such incremental transitional rate impact and spreading it over ratepayer "generations" that benefit from transitioning of regulatory accounting to incorporate IFRS capitalization policies would be circumstance specific, and properly determined in the context of the particular rate application.

9. The foregoing numerical example is intended to be illustrative, and not mathematically precise.

10. It appears to IGUA that its position is consonant with (if not identical to) that expounded by the School Energy Coalition at the Stakeholder Conference.[1]

11. In summary of its essential position, IGUA submits the Board should only adopt IFRS responsive regulatory accounting which materially increases rates where doing so is found to be in the best long term interests of rate payers (for reasons such as those identified above). In such event, rate mitigation should be employed to minimize near term rate increases and equitably spread incremental near term costs among ratepayers who will benefit over the years from the mandated regulatory accounting changes.

[1] Transcript May 5, 2009, pages 103 *et seq.*

Issue Regarding Potential for Effect on Utility Risk Profile.

12. The presentation made by Enbridge Gas Distribution (EGD) during the stakeholder conference cited, several times, the potential for impact on perceived utility risk profiles of the adoption of IFRS for public financial reporting and, potentially in some respects, for regulatory reporting.[2]

13. At one point during their presentation, EGD's representatives indicated that this issue had been discussed during the informal stakeholder meetings with Board Staff.[3]

14. EGD further proposed that that the Board's policy should acknowledge that there would be certain financial risk profile-related outcomes from the adoption, for public reporting purposes, of IFRS, that need to be considered.[4]

15. IGUA attended all of the stakeholder meetings and, to its recollection, no discussion of this issue took place, save to note that public financial reporting could include discussion and/or notes regarding regulatory assets not recognized by IFRS standards.

16. Further, the Board has expressly <u>excluded</u> consideration of the issue from the scope of this consultation in setting the issues list for the consultation[5].

17. It is noteworthy that only EGD has raised the issue. The other regulated participants have respected the scope determined by the Board for these discussions.

18. In these circumstances, IGUA <u>strongly</u> opposes any consideration of the issue, even if only by way of acknowledgement, by the Board at this time.

19. IGUA submits that any comment on the issue by the Board as an outcome of this process would be premature and without the necessary foundation.

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[2] Transcript May 5, 2009, page 69, lines 11-13 and line 27 to the top of page 70; page 70 lines 15 to 22; page 71, lines 22 to 25; page 72, lines 4 to 25; page 82, lines 15 to 17.
[3] Transcript May 5, 2009, page 76, lines 1 to 13.
[4] Transcript May 5, 2009, page 83, lines 4 to 15.
[5] Board Approved Issues List, page 1 under "Scope" heading.

Conclusion.

20. IGUA submits that it has participated responsibly in this process, and has focussed its contribution on the interests of its constituents as ratepayers. IGUA has offered brief submissions related to principles regarding ratepayer interests, leaving the details related to regulatory adaptation to the adoption of IFRS for public reporting to others. IGUA nonetheless hopes that its brief submissions are of some assistance to the Board in its consideration of the matter. IGUA requests recovery of 100% of its reasonably incurred costs of participation.

ALL OF WHICH IS RESPECTFULLY SUBMITTED:
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Per:

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