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May 25, 2009

VIA MAIL AND EMAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
26th Floor
2300 Yonge Street
Toronto, ON
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Dear Ms. Walli:

Re: Consultation on Transition to International Financial Reporting Standards
Board File Number: EB-2008-0408

Submissions of the Vulnerable Energy Consumers Coalition (VECC)

As Counsel to the Vulnerable Energy Consumers Coalition (VECC), I am writing, per the Board letter of May 14th, 2009 to provide VECC's comments on the issues associated with the transition to International Financial Reporting Standards (IFRS). The comments are organized according to the List of Issues established by the Board and specifically address the Board Staff Proposals as distributed on April 24th, 2009.

A. Scope

VECC agrees with the scope of the consultation – "to examine the effects of the adoption of International Financial Reporting Standards on regulatory accounting and rate making, to identify necessary changes to the Board's filing and reporting requirements and rate setting methodologies". During the consultative process, it was acknowledged that the requirements under IFRS are still evolving[1] and as such it is not possible to definitively state what the final requirements are. Given this context, it is VECC's view that it is premature to consider if/how the adoption of IFRS may affect the financial risk profile of utilities. As a result, VECC concurs with the exclusion of this

[1] May 24th Transcript, page 25

topic from the List of Issues. Indeed, it is likely that the Board's determinations arising out of this process regarding reporting requirements and rate making may need to be reassessed (or at least fine tuned) as the requirements of IFRS become clearer.

B. Principles

Board Staff has set out five principles for guiding the determination of the preferred alternative for each of the issues identified.

1.1 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.

VECC agrees and strongly supports the principle that it is the OEB who has the authority (and the responsibility) for establishing regulatory accounting and reporting requirements. The Board also has and should retain (subject to statutory limitations) the responsibility and authority for establishing rate setting methodologies. Indeed, in VECC's view, the role of regulatory accounting and reporting requirements is to support the Board's rate regulation responsibilities.

Given this context, VECC believes the last sentence in the above principle is misplaced and should be dropped/changed. The primary "driver" of regulatory requirements should be the Board's overall regulatory objectives, particularly as they relate to rate setting. While IFRS accounting requirements are a "consideration", it is VECC's submission that the primary "driver" of regulatory requirements should be just and reasonable rates. As an alternative wording VECC suggests that the last sentence should be replaced by – "While IFRS account requirements are a consideration in determining regulatory requirements, the objective of just and reasonable rates will continue to be the primary driver".

1.2 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.

VECC agrees with this principle. Indeed, as pointed out in the comments on Principle #1 above, this is the key principle that should be used in establishing if and how the Board should adjust its practices as result of financial reporting transitioning to IFRS.

1.3 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.

VECC also agrees with this principle and views it as being entirely consistent with the "fairness" requirement set out in Principle #2. VECC notes that both the electricity and gas distributors[2] expect to be held harmless from the introduction of IFRS, particularly in those circumstances where rates are being set under an incentive-based mechanism during the time-frame when IFRS financial reporting changes are introduced. VECC acknowledges this concern but VECC submits that it is equally important that customers (i.e., the ratepayers) also be held harmless. Any process that the Board puts in place should be symmetric in this regard and not simply rely on distributors to "self-identify" and make applications as they deem required.

1.4 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.

VECC disagrees with this principle as it places the primary emphasis on financial reporting requirements (i.e., IFRS) versus regulatory principles. As discussed earlier, the objective in establishing regulatory reporting requirement is to support the Board's regulatory function as it pertains to ratemaking. As a result the primary focus should be the Board's ratemaking obligations and the associated regulatory ratemaking principles. Indeed, Board Staff acknowledged this point during the Technical Conference[3] in stating:

> "So the statement made in the fourth principle has driven many of the proposals that we, Board Staff, have made under the individual issues. This statement aligns regulatory accounting with IFRS, unless that alignment is inconsistent with a regulatory principle.
> Where inconsistency occurs, we believe the regulatory paradigm should take precedence for regulatory accounting."

Given this concurrence by Board Staff one might ask – where's the disagreement? VECC agrees that there may be little difference provided, under the Board Staff's approach, all potential changes are tested against regulatory principles. Indeed, the approach put forward by John Browne[4] provides a framework for doing just this. The problem arises when this rigour is not applied to proposed changes.

The current proposals by Board Staff provide an excellent example of this. Board Staff claims[5] that they have "attempted to identify those places where IFRS principles and regulatory principles could clash". However, the approach taken does not appear to have been systematic, as there is no formal discussion or documentation of this presented in conjunction with each of their individual proposals. As the Board will see in the comments that follow, VECC generally agrees with the Staff's proposals. However, principles establish how problems are approached and issues addressed. It is VECC's

[2] May 5th Transcript, pages 13 & 89
[3] May 4th Transcript, page 6
[4] May 4th Presentation, Appendix 3
[5] May 4th Transcript, page 7

concern that adopting the principle as espoused by Board Staff will result in decisions defaulting too quickly to IFRS without a fulsome consideration of regulatory principles and the appreciation that regulatory principles take precedence.

Indeed, if regulatory principles take precedence (as Board Staff have agreed), then they should be “front and centre”. In this context, VECC submits that it would be more constructive and healthy from a regulatory perspective, if the principles did not offer or suggest a “default”. This would lead to an approach whereby all alternatives (including full adoption of IFRS for regulatory purposes, adoption of modified versions of IFRS and maintaining the status quo) would be considered and evaluated based on regulatory principles. Since minimization of administrative burden[6] and the associated costs are valid regulatory considerations in this context, it is likely IFRS (or some modification thereof) would be adopted unless there was some fundamental problem identified. However, such an approach would ensure that the appropriate evaluation was performed.

1.5 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.

VECC generally agrees with this principle as it facilitates the application of standard rate making methodologies to all utilities. However, if some distributors are not required to adopt IFRS for financial reporting then the adoption of modified-IFRS regulatory accounting and reporting requirements could lead to additional administrative burden and costs. In such circumstances, the Board will need to carefully consider merits of applying modified-IFRS regulatory reporting requirements to the entities concerned. Again, the guiding principles should be the Board’s overall regulatory objectives.

C. Major Points of Departure Between Existing Regulatory Accounting and Rate Making as Compared to IFRS

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?

VECC agrees with the Staff Proposal that the Board should continue to use deferral and variance accounts for rate making in appropriate circumstances, whether or not these accounts are recognized under IFRS.

[6] This would also include regulatory audit burden and a utility’s financial statements are subject to third party audit.

VECC agrees with Board Staff's comments[7] that these accounts are very useful in rate making. Indeed, this question of whether or not to continue to use deferral and variance accounts points out the fundamental difference between financial accounting/reporting versus regulatory accounting and rate making. Financial accounting and reporting deals almost exclusively with historical costs (one exception being ARO). In contrast, rate making must deal with uncertainty and circumstances that are difficult to forecast and/or are beyond a distributor's control. In these circumstances, deferral/variance accounts are a critical regulatory instrument that serves to hold both utilities and rate payers harmless and also reduce overall costs[8].

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

VECC agrees with Board Staff's proposal that the Board continue to apply the existing approach in the use and establishment of such accounts. VECC acknowledges that the approach to deferral/variance accounts may need to be reviewed when more definitive rulings are received from the IASB regarding the use of deferral/variance accounts in financial reporting. However, in VECC's view, this review must again be done within the context of the Board's overall regulatory objectives. In this context, VECC submits that it would be inappropriate for the Board to provide full assurance that deferral/variance account balances are "recoverable" as recorded without some form of review for reasonableness and prudency.

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?

VECC agrees that regulated net book value should be used as the basis for setting opening rate base 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. Net book value represents the costs incurred by the utility which it has not yet had the opportunity to recover and therefore is a reasonable and fair basis on which to set future rates. VECC notes that all parties participating in the consultation supported this approach.

VECC notes that the Board cannot dictate a utility's financial reporting practices[9]. However, VECC submits that as long as the use of net book value is acceptable under IFRS then any additional transitional or ongoing costs incurred by utilities that choose an alternative approach permitted under IFRS should <u>not</u> be recoverable from ratepayers.

[7] May 4th Transcript, page 10
[8] May 4th Transcript, page 99
[9] May 4th Transcript, page 4

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

VECC also supports the use of historical acquisition costs as the basis for reporting PP&E for regulatory purposes. Again, the use of acquisition costs ensures that utilities recover from ratepayers the cost incurred to serve them – no more / no less.

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

In VECC's view there are two related issues involved here. Currently there is a wide variation in practice across gas and electricity with regards to capitalization. As VECC understands it, one of the reasons for this is that current accounting standards are open to interpretation regarding the types of costs that may be capitalized. In contrast, IFRS provides much clearer guidance. VECC agrees there is a need for greater consistency across utilities in terms of their capitalization policies[10].

The second issue is whether the degree of capitalization that will occur under IFRS is consistent with the Board's regulatory principles. In VECC's view there has not been adequate attention given to this question to date. For example, VECC notes that the Board's current regulatory policies for pricing services provided to affiliates calls for the use of fully allocated costs. In contrast, VECC understands IFRS only permits directly related costs to be capitalized. VECC submits that this is one area where a more fulsome evaluation is needed based on regulatory principles.

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)

The Staff Proposal is that for regulatory rate making and reporting the Board will use the values calculated in accordance with IFRS (i.e., actual interest costs incurred) to determine capitalized carry charges on CWIP and discontinue publication of market based rates for applying carrying costs to CWIP.

VECC generally agrees with the Staff Proposal. Consistent with the regulatory principles of fairness and cost recovery, capitalization should be based on actual interest costs. However, VECC notes that there are a number of related issues that require clarification/direction in order to ensure consistency in regulatory accounting. First, there appears to be some uncertainty and the potential for variation in practice in terms of what assets will qualify for capitalization[11]. In VECC's view the Board should

[10] May 4th Transcript, page 12
[11] May 4th Transcript, pages 193-194

establish the construction period that would typically qualify for “interest capitalization”. Utilities would be able to request an alternative period but would have to show cause as to why the alternative is more applicable in their circumstances.

Also, in VECC’s view there is some question as to exactly how “actual interest costs” would be established. For example, do the interest costs for notes issued in previous years qualify as “actual interest costs” for capital spending in the current year? Again, in VECC’s view, the Board – as regulator – has a role in establishing a standard practice for regulatory purposes.

Finally, just as the Board currently has policies that limit the cost of affiliate debt that can be expensed and included in rates, similar policies will be required to ensure that the cost of affiliate debt used to determine interest capitalization does not exceed the rate that could have been obtained through a third party.

• Customer contributions received for PP&E

VECC agrees with the Staff Proposal that customer contributions will 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 it relates. As the intent of capital contributions is to hold (other) customers harmless for the incremental costs of the facility, the treatment should be such that the costs charged to customers in each year closely match those that would arise if the added capital costs that the contribution is designed to offset had not been incurred. Staff Proposal goes some way to achieving this objective but there are a couple of issues the Board needs to still address.

First, under IFRS there is likely to be less grouping and more componentization of asset records – particularly if the individual assets in a facility have different service lives. This may lead to the need for multiple deferred revenue accounts being required for a single capital contribution.

Second, IFRS requires regular review (and updating) of asset deprecation rates. If the amortization of the deferred revenue is to truly offset the impact of the higher capital costs then the amortization period would need to be adjusted accordingly.

Finally, VECC notes that Staff Proposal also calls for the remaining deferred revenue to be used as an offset to rate base. VECC submits that this is critical if customers are go be held harmless from the increased recorded assets costs the contributions are meant to offset.

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

VECC agrees that the simple reclassification of assets for financial reporting purposes should not change their treatment from a regulatory perspective.

• Asset retirement obligations

VECC agrees with the Staff Proposal that the depreciation and accretion expenses associated with asset retirement obligations should be reported separately. Given the unique nature of these costs it is important that they be separated out for regulatory purposes in the event a different revenue requirement treatment is warranted.

• Gains and losses on disposition of assets

VECC agrees that a gain or loss on disposition of assets should be identified separately so as to permit a different treatment if required.

• Treatment of asset impairment

Similarly, VECC agrees with the proposed treatment of asset impairment losses.

4. Depreciation

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)?

IFRS does not appear to require a utility to change its depreciation methodology (e.g., straight line versus sinking fund). As a result, VECC concurs with the Staff Proposal that utilities continue to use the straight line method.

What IFRS does appear to require is more frequent (formal) review of depreciation rates and a more rigorous application of the component approach[12]. In VECC's view greater granularity in asset recording and depreciation determination would improve the matching of costs to the appropriate time periods and customers and is therefore consistent with regulatory principles. However, various utilities during the consultation expressed concerns about their ability to implement such a detailed approach given their current record keeping practices. VECC submits that there is no need for the Board to insert itself in this debate by either:

- Requiring filings at a level of detail less than that needed to satisfy IFRS requirements – as use of such aggregated data would be inconsistent with regulatory principles.
- Requiring filings at a greater level of detail than utilities auditors have agreed is sufficient to meet IFRS requirements – provided it meets or exceeds the detail provided under current practices. In such circumstances utilities would have to incur additional costs when proposed level of detail already meets current regulatory accounting requirements.

[12] KPMG Report to the OEB, March 4, 2009 – page 50

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)?

In VECC's view deprecation is an area that has been overlooked and needs to be addressed by the OEB. The electric utility depreciation rates currently set out by the Board were established in 2000 and have not been reviewed since. Advent of IFRS provides the impetus for a more standard and rigorous approach to setting depreciation rates for regulatory accounting purposes.

VECC agrees that a joint study to establish depreciation methodologies for electric distributors would be useful. However, it is not clear to VECC that a common rate can be established for all electric distributors. Indeed, this would appear to be an extreme application of "group depreciation" and totally at odds with the requirements of IFRS. Ultimately, the results would not match the circumstances of individual utilities leading to poor cost/benefit matching and increasing the need for adjustments when assets are retired.

Also, unless the "joint study" was repeated regularly determining depreciation rates on this basis would not likely meet IFRS requirements for regular review of useful lives, depreciation methods and residual values.

Finally, the Board will need to address the issue of the timing of any change in depreciation rates for regulatory accounting purposes. Currently, depreciation rates are generally reviewed and adjusted as part of a utility's cost of service (rebasing) proceeding and then the same rate is used during the ensuing IRM period. Under IFRS, the situation could arise where depreciation rates for financial reporting purposes change during the IRM period. This issue will be discussed further under item 8.4. However, it is VECC's view that depreciation rates (and other regulatory accounting parameters) should not be adjusted until reviewed and approved by the Board.

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)**

VECC agrees that the current practice for gas utilities 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 should continue. Again, the use a variance account is critical to ensuring rate stability and that all parties (ratepayers and utilities) are held financially harmless.

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

VECC agrees with the Staff Proposal of including in rates estimated taxes (or payments in lieu of) and the recovery of future taxes in future rates.

- **Pensions and employee future benefit costs**

VECC supports the Staff Proposal to continue the current practice regarding pensions and employee benefits unless specific approval is obtained to do otherwise.

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)**

VECC agrees that the Staff Proposal regarding Item #3.1 should be adopted regardless of the final determination on the subject by the IASB.

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

Similarly, VECC agrees that the Staff Proposal regarding Item #2.1 should be adopted regardless of the final determination on the subject by the IASB.

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

VECC notes that the Staff Proposal in this regard deals specifically with distributors. As discussed earlier, while VECC is generally supportive of a standardized regulatory approach the Board should be open to hearing requests from distributors for separate treatment if circumstances warrant.

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

It is clear that the conversion to IFRS in 2011 will not be the end of financial accounting changes in the foreseeable future. It would be impractical for the Board to wait until all such changes were known. However, the fact future changes <u>will</u> occur highlights the need for a set of guiding principles that focus on the Board's regulatory obligations and objectives.

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?

VECC agrees that the rate impact of IFRS adoption will vary from utility to utility both in magnitude and, potentially, even direction. Furthermore, at this point in time there is insufficient information to estimate such impacts. VECC agrees that the financial differences and revenue requirement impact that arise from the adoption of IFRS should be identified in the utility's first cost of service rate filing after IFRS adoption.

To be clear, such differences and impacts should include not only the impact on the various elements of annual revenue requirement (e.g. depreciation, OM&A, etc.) from the changes due to adopting the new regulatory accounting practices associated with IFRS but also any differences that have accumulated during the IRM period since IFRS was adopted for financial reporting purposes (see Item #8.4).

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

See Item #7.3.

7.3 Should rate increase thresholds be set?

VECC agrees with the Staff Proposal that would see the impact of IFRS being included along with the impact of all other changes in determining whether rate impact mitigation was required and, if so, what mitigation techniques should be employed.

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?

VECC agrees that prudently incurred incremental administrative costs directly related to the transition to IFRS should be recoverable from customers. VECC also agrees that a variance/deferral account should be established to record such costs and disposition considered after the transition has been completed. VECC notes that some distributors had an allowance for IFRS transition costs included when their rates were rebased in 2008/2009 while others do not. As a result, the use of a deferral vs. variance account will vary by distributor.

As a matter of practice, the Board should adopt a standard approach for those distributors rebasing in 2010 and either allow all of them to include some provision in their 2010 rates or direct all of them to record these costs in a deferral account. In VECC's view including some nominal provision in the 2010 rates is the preferred alternative as it will reduce the costs customers will have to bear in the future and provide distributors (through rates) with some of the necessary funding.

VECC also supports the Staff Proposal that the Board, in determining the eventual disposition of these accounts, will need to consider the criteria of causation, materiality and prudence.

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

VECC also agrees that all prudently incurred on-going compliance costs should be recovered from customers. The extent and nature of such costs (including any deferred costs) should be matter for discovery and determination in the first cost of service rate proceeding following the transition to IFRS.

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

The Staff Paper contains "some suggestions" as to how IFRS implementation costs can be minimized. VECC has already commented on the merits of a joint depreciation study and on the use of minimizing the differences between IFRS requirements and regulatory requirements as an "objective".

VECC submits that the Board's approach to the recovery of IFRS implementation costs should be similar to that used for market transitions costs:

- There should be an industry-wide review with standard filing requirements.
- While all IFRS implementation costs should be subject to review, those utilities with costs above a certain threshold should be subject to a "detailed" review.
- The threshold should be established post-2011 based on a comparison of the costs incurred by all utilities and a detailed assessment of a small sub-set.

VECC also believes that IFRS implementation costs can be minimized if utilities:

- Work co-operatively so as to share expenses and learn from each other.
- Adopt an organized and structured approach to implementation – i.e., establish a work plan.

Utilities should be advised that the Board will be looking for these two elements when reviewing the reasonableness and prudence of IFRS implementation costs.

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?

This is a new "issue" that was not included on the approved issues list for the consultation. At the Technical Conference Board Staff indicated that its preliminary view was that "both increases and decreases to revenue requirement, as a result of changes in account rules, should be passed to rate payers" and that "any undue rate impacts could be mitigated"[13].

In general VECC agrees that changes in accounting for rate base and operating costs that are approved by the Board as result of the adoption of IFRS should be flowed through to the revenue requirement and the revised revenue requirement recovered from customers – subject to rate impact mitigation requirements. In this regard,

[13] May 4th Transcript, page 21

changes in regulatory accounting triggered by IFRS should be viewed no differently than changes triggered by other events/considerations.

However, VECC submits that such changes in regulatory accounting should not be reflected in the revenue requirement and customer rates for any utility until they have been reviewed by the Board as part of the rate application proceeding. This will ensure that the changes have been implemented correctly and also allow the Board to deal proactively with the potential issue of rate impact mitigation.

This approach will result in utilities that are on IRM-based rates at the time of IFRS implementation, adopting IFRS for financial reporting purposes prior to the adoption of rates based on IFRS-modified regulatory accounting practices. Furthermore, the Staff Proposal under item 10.2 will require these utilities to adopt IFRS-modified regulatory accounting practices for regulatory reporting to the OEB as of 2011. As a result, there will be discrepancy (in the post-2010 period) between the costs reported for regulatory purposes and those that the utility was given an opportunity to recover through rates – until rebasing occurs.

For example, if OM&A capitalization practices are changed in 2011 to conform with IFRS, then the OM&A expense reported (under the modified-IFRS regulatory accounting practices) will be higher/lower. If more OM&A is capitalized then OM&A expense will be lower during the balance of the IRM period resulting in an over-collection from customers. Also, the recorded capital cost of any new assets will be higher leading to a higher rate base at the time of rebasing and, effectively, a double charging of ratepayers. If less OM&A costs are capitalized the effects will be reversed and there will costs incurred by the utility that it has no opportunity to recover. A similar issue can arise with depreciation charges as indicated in VECC's comments under Item #4.2.

As noted in discussion under Item #1.3, utilities have indicated that they wish to be held harmless if such changes occur during the IRM period. VECC generally agrees but submits that the principle must be applied to both ratepayers and utilities. This suggests that there must be established procedures for tracking such differences and reporting them to the Board at the time of rebasing, rather than simply leaving it to the utilities to self-identify if an issue exists. At that time the Board can determine if the differences are material and warrant refund/recovery. In this regard, it may be reasonable to treat such differences as a Z-factor.

During the course of the Technical Conference VECC's representative sought clarification as to how the utilities saw such "differences" being determined[14]. However, VECC submits that more work is required in this area. In particular, it is not clear to VECC that the need to track these differences won't result in utilities needing to report to the Board using both the current regulatory accounting practices and the modified-IFRS regulatory accounting practices – at least until the first rebasing. VECC notes that

[14] May 5th Transcript, pages 21 & 89

under the Board Staff Proposals, the two major gas distributors will be required to do so (to satisfy the ESM requirements of their IRM plans) and the issue is therefore primarily one that impacts the electricity distributors. VECC submits that the Board should establish a process (e.g., Staff-lead industry working group) to work through this issue and identify what is needed in order to address these differences at the time of rebasing.

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 Item #9.2

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?

VECC agrees with the Staff Proposals as they apply to gas distributors.

VECC generally agrees with Staff Proposals as they apply to electricity distributors. However, the Board may need to exercise some flexibility as regards to requiring 2011 rebasing Applications to be based on IFRS-modified regulatory reporting. VECC notes that these utilities will have a strong incentive to file on a modified-IFRS basis as it will align their rates more closely with their financial reporting practices and simplify their regulatory reporting requirements in subsequent years. However, the timing requirements for the 2011 filings (e.g., August 2010) may be such that estimates of revenue requirement based on IFRS-modified reporting are not available in all cases. This may require the filing of updates to the Application early in 2011 or, as a last resort, the filing of an Application based on current regulatory reporting practices.

VECC notes that, pending the resolution of Item #8.4, electric distributors filing for rebasing in 2012 and subsequent years may well have bridge year data based on both current regulatory accounting practices and the modified-IFRS regulatory accounting practices. In VECC's view such information will provide a much better picture of the impact of IFRS than relying on 2010 comparables. VECC also notes that if IFRS continues to evolve after 2011 then the 2010 comparison will not provide a complete picture and information would also have to be provided showing the impact of any post-2011 changes on the test year's revenue requirement.

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

VECC agrees with the Staff Proposal and does not see the need for the Board to prescribe any specific rate making measures in the IRM mechanism to accommodate

IFRS apart from the establishment of a deferral/variance account to recorded incremental transition costs.

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?

As discussed under Item #8.4, such reporting may be required in order to hold rate payers/utilities harmless during the IRM period and to identify financial differences at the time of rebasing. VECC submits that such reporting will need to mandatory in those instances where Earnings Sharing Mechanism forms part of the utility's approved IRM plan.

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 the following comments.

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?

VECC generally supports the Staff Proposal that all distributors be required to report using IFRS-modified regulatory account practices starting in 2011. In VECC's view the only potential exception could be if there are utilities who will not be required to (and do not plan to) adopt IFRS for financial reporting purposes as discussed under Item #1.5.

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)?

VECC supports the Staff Proposal that all utilities be required to continue to report their information to the OEB using Canadian GAAP until December 31, 2010. This is consistent with the general premise that it is the Board who approves changes in regulatory accounting and reporting.

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

VECC supports the requirement for ongoing reconciliations between the IFRS results generated for financial reporting and regulatory accounting results reported to the Board based on modified-IFRS. The fact that the information used for regulatory reporting is audited by the third party for financial reporting purposes provides an added level of quality assurance to both the OEB and other stakeholders. However, this quality assurance is only meaningful if the audited financial statements reported under IFRS are reconciled with the regulatory accounting information.

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?

VECC agrees with the Staff Proposal that such supplementary audit assurance is required for the same reasons as set out in response to Item #10.4.

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 discussed under Items #8.4 and #9.4, it is likely that reporting will be required during the IRM period on the same basis upon which the incentive framework was approved. As a result, VECC agrees with the Staff Proposal.

Thank you for the opportunity to comment.

Yours truly,

Original signed

Michael Buonaguro
Counsel for VECC