May 25, 2009

Ontario Energy Board
P.O. Box 2319
2300 Yonge Street 27th Floor
Toronto, ON
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Attention: Ms. Kirsten Walli, Board Secretary

Re: **EB-2008-0408 Consultation on Transition to International Financial Reporting Standards and Consequent Amendments to Regulatory Instruments**

The Coalition of Large Distributors ("CLD") respectfully submits its written comments on the Ontario Energy Board Staff ("Board" and "Board staff", respectively) Proposal for the Transition to International Financial Reporting Standards ("IFRS"). The CLD comprises Enersource Hydro Mississauga, Horizon Utilities, Hydro Ottawa, PowerStream, Toronto Hydro-Electric System Limited, and Veridian Connections. Certain members of the CLD will also file separate comments to highlight particular issues or concerns related to their circumstances.

A Scope

The CLD acknowledges that the IFRS consultation does 'not include a discussion of the financial risk profile of utilities, and how the adoption of IFRS may affect that risk profile'. However, any change in the financial risk profile of a utility may result in future financial implications to that utility, which will need to be addressed at that time.

B Principles

The CLD supports the five principles put forth by the Board staff, with additional comment pertaining to principle 4. Principle 4 states;

> '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'

The CLD understands that the Board is required to make sound regulatory rate making decisions consistent with the objects of the *Ontario Energy Board Act*. However, we submit that the global transition towards IFRS is in recognition that such standards purport to report financial information in a manner that reflects the economic reality of underlying transactions. In many respects, IFRS represents a contemporary refinement of existing jurisdictional financial reporting standards. Generally speaking, the Board has adopted ratemaking policies on a "cost of service" basis. We submit that IFRS is quickly becoming the authoritative global standard for the determination of costs from an external financial reporting perspective and, as such, it would be ideal if IFRS was adopted as much as possible by the Board for the purposes of ratemaking.

Misalignments between cost of service for regulatory purposes versus IFRS will ultimately result in misalignments between regulated electricity distribution cashflows and costs for IFRS purposes, possibly with negative or unintended consequences. For instance, constraints on cash flow could affect the ability of electricity distributors to finance their capital and operating programs.

The starting position of whether IFRS aligns with sound regulatory rate making principles should not be a comparison of Canadian Generally Accepted Accounting Principles ("CGAAP") and IFRS. Instead, the Board should only determine if IFRS follows sound regulatory rate making principles. If it does then IFRS should be followed and, if required, rate mitigation can be used.

The CLD observes that CGAAP will no longer exist for publically accountable enterprises after the transition to IFRS. Unlike other countries that kept their local GAAP, Canada has decided not to do so. If the Board doesn't substantially switch from CGAAP to IFRS for regulatory purposes, the Board will be required to continue to update their accounting standards as necessary. In the future, both the Board and utilities and will have to train new staff on accounting standards that are no longer based on Canadian accounting principles.

C Major points of departure between existing regulatory accounting and rate making as compared to IFRS

2 Regulatory Assets and Liabilities

The CLD supports Board staff's proposals for the continuation of the use of deferral and variance accounts (Proposal Nos. 2.1 and 2.2). Furthermore, the CLD anticipates the approval of a regulatory asset to record incremental costs associated with the transition to IFRS. Deferral accounts could also be a mechanism with which to deal with any material changes as a result of the transition to IFRS, evaluated on a utility by utility basis. Another method includes the use of a funding adder, as discussed in more detail in Section 8 below.

The CLD recommends that enhanced definitions of regulatory deferral and variance accounts be set by the Board once the International Accounting Standards Board ("IASB") has ruled on rate regulated accounting. The revised definitions will likely need to formalize the process that rate regulated entities must follow in order to have their variances approved by the Board. It is essential that utilities, their auditors, and investors have confidence that deferral and variance accounts will be recovered in a timely and effective manner when the correct process is followed. It is anticipated that this process will be outlined in the Board staff Discussion Paper on an Electricity Distributors' Deferral and Variance Account Review Initiative, (EB-2008-0046).

Enhanced definitions may provide enough certainty to allow regulatory assets and liabilities to fall under the IFRS framework definition of an asset and a liability. This would provide the above noted stakeholders with confidence of recovery. Enhanced definitions will also assist the users of financial statements to understand the impact of regulatory assets and liabilities and any associated risk with them.

3 Property, Plant and Equipment

The CLD supports Board staff's proposals related to property, plant and equipment (Proposal Nos. 3.1-3.4). In particular, the CLD supports Board staff's proposal that will 'require utilities to adhere to IFRS capitalization accounting requirements for rate making and regulatory reporting purposes after the date of adoption of IFRS'. If utilities were required to track two separate asset ledgers, it would create substantial work on the utilities in terms of information system upgrades, increased staffing and administrative efforts that would translate into increased costs to the rate payer. These costs would not be alleviated until it was no longer required to have dual accounting books.

It is also noted that the IFRS capitalization rules fall within the guidelines of the current Accounting Procedures Handbook ("APH"). It would therefore be inappropriate to disallow the use of IFRS capitalizations rules at the adoption of IFRS. Utilities might be forced to apply for a new capitalization policy, through a rate application, prior to the adoption of IFRS if they wanted to avoid two asset ledgers.

With respect to borrowing costs, the CLD supports the Board staff proposal that 'requires utilities to capitalize carrying charges associated with Construction Work in Progress ("CWIP") using actual interest cost incurred as opposed to amounts calculated at rates prescribed by the regulator.' This will allow utilities to keep the same values for both regulatory and financial statement purposes.

4 Depreciation

The CLD generally believes that an industry depreciation and componentization study would be a valuable tool in establishing a common starting point for LDCs (Proposal Nos. 4.1-4.2). However, each LDC must set their own depreciation and componentization levels as they apply to their organization, taking into account both unique useful lives and materiality levels.

The CLD is very concerned about the timing of such a study, should it proceed. Depreciation and componentization are significant pieces of LDC IFRS transition projects. Most large distributors are well into their IFRS projects with many decisions already made, or soon to be made. Utilities must be ready to record according to IFRS by January 1, 2010 for comparison purposes. The CLD believes that while it might be too late to proceed with an industry wide depreciation and componentization study with the expectation that it would be able to eliminate the need for utilities to perform their own studies, a common study could be of use for some LDCs if it was completed by January 1, 2010. However, utilities should have the option to conduct a separate depreciation and/or componentization study should they so choose.

The intention should be to align depreciation and componentization with IFRS unless it can be successfully argued that there is a justified reason why the two cannot be aligned. An increase in rates should not be considered a justifiable reason for nonalignment, as it can be handled through rate mitigation.

As suggested with capitalization, IFRS depreciation rules fall within the guidelines of the current APH. Disallowing IFRS depreciation and componentization rules upon the adoption of IFRS would be inappropriate and could lead to utilities applying for a new depreciation policy, through a rate application, prior to the adoption of IFRS in order to avoid two asset ledgers.

5 Other Issues

The CLD supports the Board staff proposal for inventory valuation, payments in lieu ("PILs") and pensions and employee future benefits (Proposal No. 5.1).

D External Uncertainties

6 Decisions of Accounting Standard-Setting Bodies

The CLD agrees with Board staff's decision to proceed in the absence of decisions from the IASB (Proposal No. 6.1). However, Board staff should continue to monitor the progress of outstanding issues with the IASB and address any necessary changes in a timely manner.

E Impacts

7 Rate Impact

The CLD agrees that there are three kinds of potential costs related to the transition to IFRS based reporting: two of which are administrative type costs and one which is a possible change in revenue requirement due to changes in rate base and operating cost determinants. The magnitude of the changes and the resulting impact on rates will vary from utility to utility and can be managed using existing mechanisms of the Board, such as the 10% threshold on total bill triggering mitigation and deferral accounts used as smoothing mechanisms (Proposal Nos. 7.1-7.3).

8 Utility and Shareholder Impact

The CLD supports Board staff's Proposal Nos. 8.1 and 8.2 for prudently incurred administrative incremental costs directly related to the transition to IFRS and prudently incurred administrative incremental costs directly related to the compliance with IFRS, with the following addition to Proposal No. 8.1, as suggested by Toronto Hydro at the May 5th, 2009 stakeholder session: "Cost incurred prior to January 1, 2009, will be considered on a case-by-case basis and the Board, in determining the disposition of the account, will consider the criteria of causation, materiality and prudence".

This addition is proposed as some distributors incurred costs prior to January 1, 2009 in preparing to implement IFRS in 2010; Toronto Hydro, Enersource Hydro Mississauga and Hydro Ottawa applied for a deferral account in 2008 for IFRS related costs as part of their 2009 rate applications. To disallow costs prior to January 1, 2009 appears to unduly penalize those utilities that tried to be proactive in their transition to IFRS.

The CLD recommends that the following be added under Proposal No. 8.4:

> "Changes in revenue requirement that arise from changes in accounting for rate base and operating costs prompted by the adoption of modified IFRS will be recovered from ratepayers on the same basis as other costs. This applies to utilities filing for rates on a cost of service basis and to utilities on an incentive rate mechanism."

For a cost of service application, the utility would prepare the revenue requirement based on the modified IFRS rules and bring forward the normally required evidence. The impact of the modified IFRS rules may increase or decrease the revenue requirement compared to regulatory accounting based on CGAAP. Any rate impact would be handled as discussed in Section 7.

For an incentive rate mechanism application, there are two possible methods for a utility to adjust the revenue required from customers due to the change to modified IFRS. One is the EDA's proposal to establish a deferral account for transitional differences which would be cleared at the time of the next rebasing.

The CLD proposes a second method which would ensure that the utility is not adversely affected during an IRM year after the transition to IFRS but before a rebasing. The utility would request a funding adder for the IRM year based on the difference between the forecasted revenue requirement under existing CGAAP regulatory accounting and the forecasted revenue requirement under modified IFRS. After actuals for the year have been audited, the actual difference due to the implementation of IFRS would be reconciled and the difference between the funding adder and actuals would be trued up. This is a similar process to that which is working well for Smart Meter funding.

Any adjustment to the revenue requirement resulting from IFRS would include the impact to the PILs. Therefore, under the EDA's proposed approach, the affect on PILs would be recorded in a deferral account. Under the alternative approach, the IFRS affect on PILs would be reflected in the funding adder.

In the absence of viable options within the IRM framework to adjust for changes resulting from IFRS, most utilities will have no other option but to file cost of service rate applications. This could lead to a flood of applications for 2011, severely constraining the resources of the Board.

F Filing and Reporting Requirements

9 Filing Guidelines for Rate Applications

The Board staff proposal would result in the following requirements for a distributor that rebased in 2008:

	Rebasing in 2011	Rebasing in 2012
Approved historic year	2008 (actual) - CGAAP	2008 (actual) – CGAAP
Bridge years	2009 (actual) & 2010 (part actual/part forecast) - CGAAP	2009 (actual) – CGAAP 2010(actual) – CGAAP & Modified IFRS 2011 (part actual/part forecast) – Modified IFRS
Test year	2011 Forecast in CGAAP and Modified IFRS	2012 Forecast in Modified IFRS

For utilities that rebase in 2011 it is required to maintain information in two formats for an additional year, 2011. It would appear that Board staff is recommending this as the 2010 information would consist of actual and forecast information. If it was acceptable to use 2010 as the 'cross over' year in both cases, it would reduce the additional work and expense for the distributors filing in 2011. This would also reduce the likelihood of a utility rebasing earlier than initially intended simply in order to avoid preparing two forecasts for the test year.

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

The CLD agrees with Board staff's Proposal Nos. 10.2 to 10.4. However, the CLD does not agree with the requirement for a full audit of regulatory account values by a third party auditor (Proposal No. 10.5). This is a departure from past practice and will result in significant additional costs to distributors. Optionally, a lower level of assurance can be addressed if regulatory accounting is aligned to IFRS as much as possible; as long as IFRS does not deviate from regulatory rate making purposes.

In the CLD's view, provided that a distributor can reconcile the audited IFRS statements for financial reporting and modified IFRS for regulatory purposes, no external audit should be required. The CLD is concerned that this requirement for an external audit will lengthen the timelines for rate applications and unnecessarily increase costs.

Proposal No. 10.6 requires that during an IRM period, after implementation of IFRS but before a rebasing, the utility will be required to reconcile the financial results (which will be in IFRS) to the CGAAP based IRM. Note that this is the same reconciliation that the CLD is proposing under the second way of handling the impact of IFRS during an IRM year.

Thank you for this opportunity to provide input on the Board staff's Proposal for the Transition to IFRS. Two paper copies, along with an electronic version accompany this submission.

Yours truly,

Original Signed By

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(On behalf of the Coalition of Large Distributors)