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October 17, 2011

VIA MAIL and E-MAIL

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
P.O. Box 2319
2300 Yonge St.
Toronto, ON
M4P 1E4

Dear Ms. Walli:

Re: Vulnerable Energy Consumers Coalition (VECC)
Final Submissions: EB-2011-0268
Hydro One Networks Inc. – Adoption of USGAAP for Rate Making

Please find enclosed the submissions of the Vulnerable Energy Consumers Coalition (VECC) in the above noted proceeding.

Thank you.

Yours truly,

Michael Buonaguro
Counsel for VECC

cc: Hydro One Networks Inc.

ONTARIO ENERGY BOARD

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c.15 (Schedule B);

AND IN THE MATTER OF an application by Hydro One Networks Inc. for an order or orders approving a transmission revenue requirement and rates and other charges for the transmission of electricity for 2011 and 2012.

AND IN THE MATTER OF a Motion by Hydro One Networks Inc. pursuant to the Ontario Energy Board's *Rules of Practice and Procedure* for a review by the Board of its Decision with Reasons EB-2010-0002 dated December 23, 2010.

FINAL SUBMISSIONS

On Behalf of The

VULNERABLE ENERGY CONSUMERS COALITION (VECC)

October 17, 2011

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Vulnerable Energy Consumers Coalition (VECC)
Final Argument

1 Introduction

- 1.1 In July 2011, Hydro One Networks Inc. (HONI) filed a letter and Notice of Motion with the Ontario Energy Board (the “Board” or the “OEB”) seeking to vary the Board’s Decision (EB-2010-0002) regarding its approved 2012 Transmission Revenue Requirement and the associated 2012 Uniform Transmission Rates. The motion sought to vary the Board’s earlier Decision so as to permit Hydro One to use US GAAP for rate application filings, regulatory accounting and regulatory reporting and to adjust the 2012 revenue requirement and variance accounts as approved in the Decision to reflect the adoption of US GAAP rather than International Financial Reporting Standards (“IFRS”) for regulatory purposes.
- 1.2 In a Decision, Notice of Hearing and Procedural Order dated August 25, 2011 the OEB denied HONI’s motion. However, on its own motion, the Board commenced a hearing under section 78 of the *Ontario Energy Board Act, 1998* to consider adjustments to Hydro One’s 2012 Transmission revenue requirement and other adjustments and variance accounts that may be necessary should Hydro One use US GAAP rather than modified IFRS (“MIFRS”) for regulatory purposes.
- 1.3 Set out below are VECC’s final submissions on these matters.

2 Hydro One Networks' Use of US GAAP for Financial Reporting

- 2.1 HONI's original application for approval of its 2012 revenue requirement (EB-2010-002) was premised on the assumption that the company would be required to adopt MIFRS for financial and regulatory reporting purposes commencing January 1, 2012¹. However, in May 2011 it became known that there was an option for rate regulated entities to apply to their securities regulator for an exemption to permit the use of US GAAP for the preparation of financial statements.
- 2.2 On July 7, 2011 HONI filed an application² with the Ontario Securities Commission ("OSC") seeking approval to utilize US GAAP as the basis for preparing its periodic public securities filings effective January 1, 2012. Approval to do so was granted by the OSC on July 21, 2011³. The OSC approval is effective up to the end of 2014.
- 2.3 On August 17, 2011 Ontario Regulation 395/11 was approved requiring Hydro One Inc. (HONI's parent company) to prepare its financial statements in accordance with U.S. generally accepted accounting principles (US GAAP)⁴. However, unlike the OSC approval, there is no time limitation in the Regulation on the use of US GAAP.
- 2.4 VECC submits that the OSC approval and Ontario Regulation 395/11 place Hydro One Networks Inc. in a unique position relative to other electricity transmitters (and distributors) in the Province as it has both the necessary OSC approval to adopt US GAAP for reporting purposes and, more importantly, is required by statute to adopt US GAAP for financial reporting purposes.

¹ Exhibit A, Tab 3, Schedule 1, page 1

² Exhibit B, Tab 1, Schedule 2

³ Exhibit B, Tab 1, Schedule 1

⁴ OEB Staff Interrogatory #6

3 Hydro One Networks' Request with Regard to Regulatory Rate Applications, Accounting and Reporting

3.1 In the additional materials⁵ filed with the Board on September 6, 2011 HONI indicated that it was seeking the following with respect to revenue requirement determination:

- Approval allowing Hydro One Networks to utilize US GAAP as its approved framework for rate setting, regulatory accounting and regulatory reporting commencing January 1, 2012 in a manner appropriate for a rate regulated entity.
- Acknowledgement and approval that if US GAAP is adopted to establish the revenue requirement and rates for Hydro One Transmission, it is appropriate for Hydro One Networks to do so for Hydro One Distribution.
- A reduction to the base revenue requirement from \$1,657.6 million to \$1,462.3 million for 2012 as set out in Exhibit C2, Tab 1, Schedules 1 to 11.
- Approval of an increase in the 2012 capital expenditures from \$781.3 million to \$981.3 million as set out in Exhibit C2, Tab 1, Schedule 4.
- Approval of an increase in the 2012 rate base from \$8,726.3 million to \$8,774.4 million as set out in Exhibit C2, Tab 1, Schedule 3.

3.2 With respect to the deferral/variance accounts related to the implementation of MIFRS, HONI is seeking approval⁶ to:

- Discontinue the Impact for Changes in IFRS Account (2012 only),
- Discontinue the IFRS – Gains and Losses Account (2012 only),
- Discontinue the IFRS Capitalization Policy Variance Account (2012 only),

⁵ Exhibit A, Tab 3, Schedule 1, page 3

⁶ Exhibit D1, Tab 1, Schedule 1, page 1

- Continue, with a revised scope, the IFRS Incremental Transition Costs Account, and
- Establish a new Impact for US GAAP Account (2012 only).

Adoption of US GAAP for Rate Setting, Regulatory Accounting and Regulatory Reporting

3.3 In its June 2011 Addendum Report⁷ the Board indicated that if a utility wished to use US GAAP for regulatory purposes it must file the following information in its cost of service application:

- The eligibility of the utility under the relevant securities legislation to report financial information using that standard,
- A copy of the authorization to use the standard from the appropriate Canadian securities regulator (if applicable) showing any conditions or limitations, and
- Set out the benefits and potential disadvantages to the utility and its ratepayers of using the alternate accounting standard for rate regulation.

3.4 As noted in the preceding section of VECC's submissions, Hydro One Inc. has received authorization from the OSC to use US GAAP for preparing its periodic public securities filings effective January 1, 2012. Furthermore, VECC notes that Hydro One Inc. is required, by Ontario Regulations, to prepare its financial statements in accordance with US GAAP. As a result, VECC submits that HONI has the Board's first two requirements.

3.5 In terms of benefits and disadvantages to the utility and its stakeholders, VECC agrees with HONI's view that "its adoption of US GAAP for both financial accounting and regulatory accounting and reporting purposes is in the best interests of all stakeholders"⁸. For rate payers, the benefits include:

- Continued rate stability, as US GAAP is very similar to CGAAP⁹,
- Lower transmission (and distribution rates) in the near term¹⁰,

⁷ Page 19

⁸ Exhibit C, Tab 1, Schedule 1, page 4

⁹ VECC #3 and OEB Staff #25

- Reduced compliance and reporting costs for HONI as compared to using MFRIS for regulatory purposes and US GAAP for financial reporting, which would otherwise have to be passed on to customers¹¹, and
- Lower revenue requirement and rates over the long term due to differences between group accounting under US GAAP and item accounting under IFRS regarding the treatment of gains and losses upon retirement¹².

3.6 In both its initial submission¹³ and in response to interrogatories¹⁴, HONI has set out the ways in which its other major stakeholders (the OEB, the financial community, its shareholder, and the Corporation itself) benefit from the adoption of US GAAP for regulatory purposes. The only potential disadvantage is that HONI's transition to US GAAP will not facilitate the benchmarking of its results with those of other local (Ontario) utilities. However, the adoption of US GAAP will facilitated HONI's ability to benchmark its results with those of other large North American utilities, which it commonly does¹⁵. Also, Hydro One has indicated that with reasonable normalization adjustments benchmarking with Ontario utilities can still take place¹⁶.

3.7 In its June 2011 Addendum Report¹⁷ the Board stated that the "adoption of US GAAP as a short term solution may be counter-productive". While Hydro One's request to the OSC regarding the use of US GAAP for filing its financial statements was only for the period before January 1, 2015, the Company has explained the choice of a three year exemption period was based on the Enbridge Income Fund precedent and the fact that such a term was likely to be approved¹⁸. However, Hydro One has also indicated that if the issues surrounding rate-regulated accounting under IFRS are not resolved by the time the exemption

¹⁰ OEB Staff #2

¹¹ OEB Staff #12 and Exhibit C, Tab 1, Schedule 1, page 2

¹² OEB Staff #14

¹³ Exhibit C, Tab 1, Schedule 1, pages 2-4

¹⁴ OEB Staff #5

¹⁵ VECC #1

¹⁶ OEB Staff #17

¹⁷ Pages 19-20

¹⁸ OEB Staff #8

granted by the OSC expires then it would likely apply for a further extension¹⁹ or even a permanent exemption²⁰. As a result, in HONI's case, the use of US GAAP does not represent a short-term delay in the implementation of IFRS (as it is currently formulated).

- 3.8 In VECC's view the benefits of HONI adopting US GAAP for regulatory purposes far outweigh any potential disadvantages and the use of US GAAP by HONI should be approved by the Board for both its Transmission and Distribution businesses.

Capital Spending, Rate Base and Revenue Requirement 2012 Adjustments

- 3.9 The supporting schedules²¹ filed by HONI with its EB-2010-0002 Draft Rate Order the Company documented the impact of adopting MFRIS as opposed to CGAAP for 2012:

- Revenue Requirement increased by \$195.3 M,
- Capital Expenditures decreased by \$200 M, and
- Rate Base decreased by \$48.1 M.

- 3.10 Given HONI's assertion that the differences between CGAAP and USGAAP are not expect to have any impact on either its 2012 expense statement or balance sheet²² or revenue requirement²³, VECC submits that HONI's proposal to account for its adoption of USGAAP by adjusting the 2012 approved (MIFRS-based) revenue requirement, capital expenditures and rate base by equivalent amounts is reasonable and should be accepted by the OEB.

¹⁹ OEB Staff #10 iii)

²⁰ VECC #2

²¹ See Exhibit C1, Tab 2, Schedule 2 - DRO Exhibit 1.9

²² VECC #3

²³ LPMA #3

Proposed Changes to Deferral and Variance Accounts

- 3.11 With the adoption of US GAAP HONI will not require the deferral/variance accounts associated with the implementation of IFRS and VECC submits it is reasonable that they be discontinued.
- 3.12 The only exception is the IFRS Incremental Transition Cost Account which HONI is proposing to maintain in order to capture any differences between actual incremental IFRS and US GAAP transition costs incurred and the estimated incremental IFRS costs approved by the Board as part of the 2011 and 2012 Transmission Rates. VECC agrees with HONI's proposal to maintain this account, appropriately renamed.
- 3.13 Finally, HONI is proposing to establish a new US GAAP Account to capture any differences between Canadian and US GAAP that would impact its revenue requirement. To date, HONI has not identified any such differences and appears to be requesting the account as a "precautionary" measure. In principle, VECC has no objection to the approval of such an account. However, VECC would be concerned if ultimately there were material variances recorded in the account since the main justification for adopting US GAAP is its similarity to current Canadian accounting practices.

4 Recovery of Reasonably Incurred Costs

- 4.1 VECC submits that its participation in this proceeding has been focused and responsible. Accordingly, VECC requests an award of costs in the amount of 100% of its reasonably-incurred fees and disbursements.

All of which is respectfully submitted this 17th day of October 2011