EB-2008-0104

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

AND IN THE MATTER OF the review by Board Staff of the regulatory impacts of the transition by the Accounting Standards Board of Canada to International Financial Reporting Standards.

COMMENTS OF THE

SCHOOL ENERGY COALITION

ON THE PROPOSED WORKPLAN

1. On October 7, 2008 Board Staff published a draft document entitled "*Regulatory Accounting Transition to IFRS – Project Work Plan*" (the "Draft Plan"). The Board has asked for comments on that document from interested parties by October 29, 2008. These are the comments of the School Energy Coalition with respect to the Draft Plan.

Overall Concerns

2. For the reasons set out in more detail below, the School Energy Coalition believes that the Draft Plan cannot be approved by the Board in its current form. It is, in our view, wholly inadequate to address an issue – or category of issues – that have the potential to cost ratepayers hundreds of millions of dollars a year commencing in 2011 or earlier, or, conversely to destabilize the financial position of some utilities in a manner that is contrary to the interests of both the utilities and the ratepayers.

3. It is submitted that this Draft Plan is fundamentally flawed. It does not appear to reflect in any cogent way the Board's needs for input and consultation, nor does it have provision for appropriate timelines and resources. Throughout the Draft Plan, the assumption that this is an accounting issue, rather than an important set of changes to ratemaking principles, comes through loud and clear.

4. It appears to us that the reason for the poor quality of the Draft Plan is that the Audit Division of the Board has little experience with public consultations. This manifests itself in two ways. First, the approach taken by Audit in setting out the work to be done suffers from lack of input on the most important issues. Second, in identifying the work to be done the Draft Plan ignores the thoughtful and sophisticated practices and procedures that the Board has developed over the years for situations of this type. Those practices are intended to ensure that the Board gets the benefit of well considered and thorough input from a broad range of stakeholders, resulting in Board policies that are not only better overall, but that gain buy-in from the full spectrum of parties.

5. This flaw is then exacerbated by the fact that Audit generally does not deal with ratepayers directly, but deals regularly with regulated entities, who comprise their "constituency". This, in our view, led them to propose a consultation that initially not only did not invite ratepayer representatives, who would ultimately pay for all of this, but to expressly advise that ratepayer representatives were not welcome. After attempting unsuccessfully to convince Audit that ratepayers should be at the table, SEC had to resort to a formal complaint to even be allowed to attend, but without any costs being available in the consultation.

6. The result of these facts is that the process – both to date and going forward – is and will continue to be flawed in two fundamental ways, both of which need to be addressed on an urgent basis:

   a. The Draft Plan does not contain adequate timelines for real input from all stakeholders. At the highest level, it lacks sufficient periods of notice, time for expert analysis, time for well-thought-out submissions, and the ability to engage the debate on key issues in a meaningful and helpful way. We will go into these points in more detail below.

   b. The non-inclusive approach of Audit has resulted in an unfortunate appearance of bias, something the Board has been successful in avoiding in other consultations over the last few years. This was most telling at the final consultation meeting on October 16th, when, in a room full of perhaps 100 utility representatives, SEC were the only ratepayers in the room. It appeared to us that even many of the utility reps thought this was a bit strange.

7. We understand why this consultation was made the responsibility of Audit Division, and there was good logic behind that. However, it is submitted that the Board and all parties would be better served if Board Staff with more experience handling multi-stakeholder processes were assigned to this one going forward. Both Applications and Regulatory Policy Development have engaged in many successful consultations, processes and proceedings, and are sensitive to the appropriate approaches necessary to produce the best results. Either would be a good choice, but in our view given the relationship between IFRS and future rate proceedings, and the fact that Audit is also part of Market Operations, having this consultation overseen by individuals in Applications would be the best choice by the Board.

8. Obviously Audit Division has to continue to be involved in this process, as they will have a key role in the implementation of any Board decisions, but if this process were to be managed in tandem with Applications, the Board would have a better consultation, stronger input from the parties, a better decision on the issues, and fewer problems implementing the result.

9. The balance of these comments starts with a review of certain background information, followed by an analysis of what the Draft Plan should be seeking to accomplish, and the issues – both substantive and practical - that are necessarily raised in the process. We conclude with a proposed alternative approach for the Board's consideration, including specific steps and detailed timelines.

Background

10. The changeover from Canadian GAAP to IFRS did not spring up as a sudden problem this year. The Accounting Standards Board of Canada ("AcSB") started the process with a general proposal, published in May 2004 for public comment, to consider moving to IFRS. After written comments and public forums provided extensive input, AcSB published a Draft Strategic Plan in March 2005, proposing a five year transition to IFRS. Comments were also invited on that proposal, and there was again considerable input. In 2005, many other countries were already moving to IFRS, and it was clear that Canada would likely have to go in that direction. In fact, in May 2005 CA Magazine, read by virtually all accounting professionals in Canada on a regular basis, published an article describing the move to IFRS as inevitable, and treating the five year transition as already decided.

11. It was thus no surprise to anyone in the accounting field that, in January 2006, the AcSB formally approved the Strategic Plan that included a five year transition to IFRS. It was specifically known, then, that the changeover to IFRS for affected Canadian companies (which would include almost all utilities) would take place no later than January 1, 2011.

12. We should add that some utilities responded to this by starting the internal processes necessary to consider the impact. Many utilities, for example, in their 2008 rate applications, filed in 2007, already included budget items for IFRS. In the consultations in this proceeding it has become clear that, at least in 2007, and perhaps in some cases in 2006, many large utilities had already started to work on this. This is true in non-utility companies as well, by the way. The major accounting firms had guides for Audit Committees published before the end of 2006, and the Audit Committees of many companies had, by the beginning of 2007, already started the process of planning for this change.

13. We note that, when we discuss the question of externally imposed deadlines, below, and how they impact the Draft Plan, the urgency of the situation will be considered in the context of how long everyone has known about this.

The Interest of Schools

14. SEC is involved in this process first because IFRS has the potential to have a significant impact on rates. For schools alone, we have estimated that the annual impact of IFRS could be between $5 million and $40 million, depending on the Board's final policies. While we do not anticipate that the latter figure will be the actual result, even at the lower extreme the impact is still significant. (Of course, for all ratepayers you can multiply those figures by about 50, since schools generally pay about 2% of the regulated charges in Ontario.) There is little doubt that, in the first five years, IFRS will cost ratepayers at least $1 billion, and the potential cost is many times that.

15. Conversely, as noted below if the Board determines that rates will not be affected by IFRS in any significant way, the potential destabilizing impact on some utilities could be substantial. Schools consider reliability of electricity and gas supply to be critical to their operations, and so anything that a) destabilizes the operations of these key suppliers, b) makes it more difficult

for them to supply gas or electricity in a safe and reliable manner, or c) is a barrier to financing their capital needs on normal commercial terms, is contrary to schools' interests.

16. It is because of these significant impacts that SEC has sought to be involved in this consultation from the outset, attending the consultative meetings and making submissions, despite the fact that the process ate up a considerable amount of our tightly controlled annual budget. Unfortunately, the limited resourcing meant we were not able to retain outside experts, as we would have preferred, and that has limited our ability to provide more detailed input on certain of the issues raised.

Purpose of the Work Plan

17. This process to date has proceeded from a premise on the part of Board Staff that this is about getting the accounting right, and in the process making things administratively simpler for the Board and the utilities. In our view, this is fundamentally incorrect. While those things are undoubtedly relevant, this process is essentially about rates, and until the Board approaches it from that point of view, it is submitted that the process, whether based on the Draft Plan or otherwise, will not be viable.

18. It is submitted that the Board's involvement in IFRS can have one or more of three goals:

a. ***Changes to Revenue Requirement.*** Determination of the extent to which IFRS will or should affect rates, through changes to how revenue requirement is calculated, or through other impacts on the actual or calculated costs of regulated entities. For example, if IFRS prohibits capitalization of overhead, resulting in higher operating expenses for accounting purposes, to what extent should the Board allow that to increase rates?

b. ***Transition Cost Responsibility.*** Determination of whether, and if so to what extent and when, administrative costs associated with the transition by regulated entities to IFRS should be included in the amounts recoverable from ratepayers. For example, if a utility is in the middle of IRM, should a Z factor be allowed for these costs?

c. ***Minimizing Compliance Costs.*** Assisting (or encouraging, or requiring) regulated entities to work together so that the overall costs of the industry to shift to IFRS, and ongoing costs thereafter to remain compliant, are minimized. This could range from actions to avoid the duplication of efforts we saw in the open market transitional costs (for example by acting as a clearing house for common initiatives), to administrative and filing procedures that minimize the cost of compliance with Board requirements in light of IFRS.

19. In each of these cases, the Board's involvement is based on its mandate to set just and reasonable rates. We believe that all three of these goals should be addressed in this process, and the Board should establish guidelines or procedures in the end that deal with each.

20. It is submitted that, once the Board accepts that this is an exercise in establishing ratemaking policies, the structure of this consultative process becomes clearer. Certain things are necessary. For example, ratemaking policies are not established without the involvement of

the ratepayers. Sufficient time and resources must be available so that all key issues are properly engaged and decided. And, it follows, the Board before making its decision on this policy must have an opportunity to hear all sides on each material issue.

Issues of Principle

21. We are not in a position, at this stage, to identify all of the critical issues that arise in the context of this consultation, but we feel it may be of assistance to the Board to identify some of the more important ones, so that the context of the Draft Plan and the work to be done is clear.

22. ***Overall Principle.*** In our submission, the most important issue of principle is the potential impact on rates and/or utility financial positions of IFRS, which is in essence a tension between two problems:

   a. ***Rate Impacts.*** On the one hand, IFRS will change the accounting income of regulated entities, generally by recognizing expenses earlier and thus increasing costs and reducing income for accounting purposes. If this is allowed to carry forward to the calculation of revenue requirement, the result would be a substantial rate increase for ratepayers, while the actual cost of the regulated service is not changing. Ratepayers have already been through this with market opening, and bore substantial additional costs without any additional services. They have also borne, in some cases, specific changes in accounting costs (e.g. for stock based compensation and capitalization policies) that provided no benefits. It is difficult to imagine the Board and utilities explaining to ratepayers that, after the government added significantly to rates at market opening, and the utilities then started to spend more to upgrade their systems, now the Board will authorize an additional level of cost – 10% to 20% is the likely range – without any real world change in what the ratepayers are getting. Not only would this be opposed strenuously by many ratepayers, but even utilities are likely to be uncomfortable with this result.

   b. ***Financial Statement Impacts.*** On the other hand, if regulatory income does not change, IFRS will result in financial statements being increasingly disconnected from regulatory statements. In effect, the current situation, in which regulatory accounting and financial accounting have some – manageable – differences, would be changed to one in which the two sets of records would be largely unrelated. This would have the effect of reducing financial earnings of utilities, and increasing earnings volatility, destabilizing those regulated entities. This could affect market values of their shares, and, more importantly, their ability to access the credit markets at reasonable cost. In the most extreme cases, some utilities might well show losses from a financial perspective, even though they are, from a regulatory point of view, earning their allowed rate of return.

23. At the final consultation session, a number of utilities spoke in favour of having the debate on this principle, and how it should be addressed, at the outset of the process, before getting down to the details. As the Board will see from our comments below, this is not simply a question of choosing between unpalatable results. It may also be a question of whether, if one or the other result is inevitable or more likely, the Board's choice is thus more limited than it

first appears. In either case, it will also be a decision balancing short term against long term, and potentially involving transitional rules.

24. As will already be clear, this is also about resisting IFRS, or accepting it. At one extreme, if IFRS is fully accepted (scenario a above), the rate impacts are unacceptable. At the other extreme, if IFRS is resisted to the point of complete rejection (scenario b above), the financial impacts on utilities are unacceptable, and eventually the rate impacts of that result are also unacceptable.

25. ***Simplicity and Regulatory Costs.*** One of the goals the Board has been trying to accomplish over the last several years is to streamline the regulatory process and reduce the (nominally unproductive, but necessary) costs of regulation. IFRS will undoubtedly increase the complexity of regulatory accounting, and one of the Board's tasks in this process is to minimize that impact.

26. This is, indeed, much of the focus of the Draft Plan. However, each decision to simplify and reduce administrative cost has the potential to either a) limit the Board's flexibility in exercising its mandate to set just and reasonable rates, or b) add amounts to revenue requirement. Reducing administrative cost is likely, in most cases, simply a function of increased acceptance of (or reduced resistance to) IFRS, and comes at a price.

27. For this reason, it is our view that the administrative responses to IFRS should <u>flow from</u> the Board's consideration of the overall principles, rather than driving them.

28. ***Deferral and Variance Accounts.*** A particularly difficult issue for some regulators, including the Board, is the limited ability under IFRS to treat amounts in regulatory deferral and variance accounts (regulatory assets) as assets for financial accounting purposes. IFRS effectively deals with these items in an asymmetrical way. Regulatory assets are not considered to be assets in most cases, since they would lack certainty as to amount collectible. Regulatory liabilities, on the other hand, would be considered actual liabilities, and so would show as such on the balance sheet.

29. There are a number of options for dealing with this problem, all of them containing problems from a regulatory perspective, including but not limited to the following:

   a. Cease using deferral and variance accounts. This likely means that the rule against retroactive ratemaking would have to be altered, since some types of expenditures can only be calculated fairly after the fact. It would also result in the acceleration of some costs into revenue requirement, increasing rates.

   b. Change the process so that the disposition of a deferral or variance account is determined when the account is established, and the amounts are identified with certainty. This would increase the regulatory burden when accounts are established, and would severely limit the Board's ability to supervise the prudence of these expenditures.

c. Change the timing of clearance of deferral and variance accounts, so that utilities never have a regulatory assets of any substantial size on their year end financial statements. Not only does this have the potential to create a multiplicity of proceedings, but it would require that some accounts be cleared before sufficient evidence is available to make a reasoned decision.

d. Make no changes. This would likely result in significant differences between the regulatory and financial balance sheets and income statements of the utilities.

30. The above only deals with the discretionary deferral and variance accounts. Some deferral and variance accounts are either expressly, or by implication, required by statute. This adds a further layer of problems in how to deal with them.

31. The Board could, and perhaps should, embark on a more fundamental review of what it regularly accomplishes using deferral and variance accounts, and how the same things could be accomplished in different ways that are more compatible with IFRS. This is not a trivial exercise, and is unlikely to be done in the time frames set out in the Draft Plan.

32. ***Fair value of assets***. IFRS requires, in some cases, assets to be revalued to fair market value for financial reporting purposes. This is much more extensive than the limited category of revaluations allowed under Canadian GAAP. This creates a fundamental difficulty for the regulator, because rate setting relating to capital spending has to date been based on recovering from ratepayers the original actual cost of an asset, over its useful life (based on traditional accounting principles). Recoveries from ratepayers based on market value would be a fundamental change to the regulatory compact.

33. The valuation problem may be alleviated somewhat by the fact that, even today, rate base and fixed assets, while related concepts, are not identical. IFRS would make the differences larger, but that impact is quantitative, not qualitative.

34. There are other impacts to this, though. For example, revaluations affect the income statement, and thus could exacerbate the differences between financial and regulatory income. At a more mundane level, regular revaluations may come at a cost, and some ratepayers may question whether that cost has anything to do with them (since it doesn't affect the regulatory statements).

35. ***Pooled Depreciation.*** IFRS does not use the pooling concept of depreciation that is common in Canadian financial and tax accounting. It is not yet known how, if at all, this change would affect regulatory costs and income, or whether it has implications for depreciation in general. Board Staff correctly points out in the Draft Plan that the question of whether common depreciation methods and rates should be mandated by the Board to be used by regulated entities is collateral to the issue of changing the depreciation rule to comply with IFRS.

36. In our view, the Board should seek expert advice as to the on-the-ground implications of changing the depreciation method for rate base, publish the expert report, and then invite comment from utilities and other stakeholders.

37. ***Capitalization of Overheads***. Much discussion in the consultation centred around the IFRS prohibition against capitalizing indirect overheads. Direct costs associated with capital projects are still capitalized, but anything that is not directly associated with capital projects must be expensed. Often utilities have substantial capitalized amounts, with a loading factor that ranges from 10% to 40% depending on the methodology.

38. On the one hand, capitalization is a zero-sum game. Anything that is expensed is not included in rate base, and so reduces future depreciation and return. Some ratepayers, for example, prefer reduced capitalization, so that they reduce future rate base and therefore overall cost of capital. Others prefer increased capitalization, reducing short term rates. Utilities also fall on both sides of this question, some preferring higher budgets now, and some preferring higher rate base on which their net profit is calculated.

39. What is true, however, is that even if it all works out the same, the time it takes to get to equilibrium, given the long lives of utility assets, is measured in decades, and for a growing utility that point is never achieved. Thus, added to the issue of the initial rate impact of this change is the question of intergenerational equity. If expenses are being incurred today that, from a common sense point of view, are being incurred to benefit future ratepayers, to what extent should it be future rates that recover these costs?

40. A related question is whether different business structures will produce different results on this issue (and others, for that matter). For example, a utility can outsource its capital project work (even to an affiliate) on a time and materials basis. That cost would typically be a fully loaded cost, and, because it is directly attributable to capital projects, it would be 100% capitalized (included the built-in overheads). If this is indeed the case, should the Board a) mandate, b) allow, c) restrict, d) prohibit, or e) ignore these planning techniques in setting just and reasonable rates?

41. ***ROE Impact and ROE***. The obvious impact of IFRS on ROE is the likely reduction in realized ROE at current rates, and the potential requests from regulated entities to increase revenue requirement to adjust for this change.

42. A more subtle and potentially more difficult ROE impact is the actual setting of the Board-approved level of ROE. ROE has in recent years been established using a model that compares utility returns to market returns to determine a "fair return" as revealed by the marketplace. All of those comparables in North America have to date been based on returns using traditional GAAP. With the shift to IFRS across Canada, the response of the marketplace could be to a) increase product prices to retain comparable financial returns, b) accept a lower level of financial returns as the market standard for like companies, c) increasingly decouple investment returns from underlying financial returns of investee companies, or d) some combination of the above.

43. Without a proper study of market impacts (perhaps using Europe or other places as a model), the Board may have difficulty determining whether its current Board-approved ROE continues to be a "fair return" in an IFRS world.

44. The ROE issue could be affected in two other ways. First, many utilities feel that their ROE should be set with reference to market returns in the U.S. With it now being clear that the U.S., if it moves to IFRS at all, will do so long after Canada does, it is now less likely that U.S. returns can be considered comparables for Canadian regulated entities.

45. Second, it is difficult to speculate on whether short term impacts of IFRS on market returns will be sustainable over the long term. There is a body of economic theory that says market returns are driven by investor requirements, not financial returns, and ultimately must return to those absolute levels. If that concept is correct, then market returns could show a reaction to IFRS, and then, as the market adjusts, returns will go back to their previous level.

46. ***Tax Impacts***. It almost goes without saying that changes to the accounting methodology have the potential to change the tax liabilities of taxable entities. From the Board's point of view, this could be material in a couple of ways.

47. At the most obvious level, changes to how utilities must account for tax liabilities, present and future, will affect accounting income and have all the impacts set forth above. This is a problem that the Board already deals with, but would be more serious under IFRS.

48. At a less obvious level, corporate income tax itself is based at its starting point (section 9 of the Income Tax Act) on profit as calculated under GAAP. There are a number of adjustments from GAAP to income for tax purposes, but GAAP remains the foundation. If GAAP changes from Canadian GAAP to IFRS, then unless new tax adjustments are introduced, tax liabilities of regulated entities will change.

49. On this latter point, it is submitted that Board Staff should establish communications with Canada Revenue Agency and the Department of Finance, and keep on top of the changes those government bodies will be making over the next two years to react to IFRS. This will have three beneficial effects:

   a. The Board will be able to keep on top of the tax rules, and prepare for changes required to utility tax calculations.

   b. CRA and Finance will be dealing with some of the same issues that the Board is dealing with (in terms of whether and how to make adjustments from accounting income), and may create solutions that are usable by the Board, directly or with modifications. Sharing information may thus produce better regulatory results, at a lower cost.

   c. If one of the results of the overall process is that there is a separate set of books required for regulatory purposes and for financial accounting purposes, it may reduce regulatory burden if the regulatory books are modeled as much as possible on tax accounting, if such a relationship is reasonably achievable after CRA reacts to IFRS.

50. As noted above, there are many other substantive issues, but these give the Board a flavour of the complexity of the issues that arise, and the impossibility of finding simple answers to them.

Specific Practical/Administrative Issues

51. The Draft Plan does not spend a lot of time dealing with the issues of principle we have noted above, but it does identify and discuss some of the following key administrative and practical issues that IFRS raises:

    a. ***Standardized filing rules for Publicly Accountable Entities and others***, i.e. should all regulated entities be required to convert to IFRS, even if some have applicable exceptions, and/or should the regulatory filing requirements be the same for entities to which IFRS applies, and any to which it does not apply?

    b. ***Standardized reconciliation rules - financial to regulatory,*** i.e. should the Board establish a standardized format for the conversion of financial accounting information to regulatory accounting information, and if so what should the rules be? If not, what parameters should be imposed on financial to regulatory reconciliations?

    c. ***Audit opinions on regulatory statements***, i.e. can the Board continue to rely on the audit opinions on financial statements and, if those are now less valuable, should the Board require the auditors of regulated entities to opine on the regulatory statements? If they do, there are two related questions: what is the wording and legal responsibility of the opinion (since clearly the "present fairly" opinion would not apply), and should the ratepayers bear the additional audit cost associated with this additional opinion?

    d. ***Cost responsibility – conversion and ongoing***. Utilities will incur additional capital and operating costs, first in the conversion to IFRS, and then in the ongoing compliance (e.g. valuations). Who should bear these costs, and how should they be accounted for in the regulatory statements?

    e. ***Assistance to smaller utilities – role of OEB in assisting utilities in acting in concert***. To what extent, if any, should the Board be a facilitator in the transition of utilities to IFRS? What other bodies (such as the EDA) may be better suited to that role, and how can the Board work with other bodies to make the transition smooth and keep the cost down?

52. While these questions are all less important than the issues of principle set forth above, they are not trivial, and it is submitted that dealing with these issues in an orderly manner should be an integral part of the process.

Application to Rate Proceedings

53. It is self-evident that the Draft Plan presented by Board Staff does not include either sufficient time or sufficient resources for the parties to engage the questions set out above, or for the Board to give those questions the serious consideration they require.

54. The problem with this is that, sooner or later, the policies and procedures established in this process will be reflected in rates. The Board, as is often the case, therefore has a choice

between considering these issues fully on a generic basis, and taking the time to do it right, or to consider them in the context of real cases, and allowing the solutions to evolve.

55. It is submitted that the Draft Plan implicitly adopts the latter approach. Because it lacks any provision for a thorough consultation, and never gives any stakeholder (including the utilities) the opportunity to engage the issues and have the debate on principle, the first utility that makes a rates application that covers the IFRS period will have to raise the issues, and all stakeholders will have to participate in that rate case. The principles will be considered in the context of the facts of that specific case, and that individual Board panel will have to develop appropriate principles on its own.

56. This is the "common law" approach to the establishment of Board policy, an approach the Board has been trying to get away from over the past few years. It has its advantages, but also many disadvantages, including cost, complexity, lack of thoroughness, and duplication. Lacking a principle of binding precedent from rate cases, the Board has found in the past that considering generic issues in individual rate cases normally results in future cases going over the same ground, as applicants consider their facts to be slightly different from the case in which the principles were set. Inconsistent decisions sometimes arise, since prior decisions are not binding.

57. In our view, development of a policy along these lines is contrary to good regulatory policymaking and should be avoided by the Board.

<u>SEC's Proposed Alternate Approach</u>

58. The Draft Plan proceeds from the premise that there is a certain amount of time available, and the Board should do what it can in that time to deal with IFRS.

59. With respect, this is the wrong approach to development of ratemaking policies. It is submitted that the better approach is to assess what the proper steps are to deal with the problem at hand, then compare that to the time available and find solutions to any mismatch between work and plan. Our proposal, below, takes that approach.

60. ***What Has to be Done?*** In our view, proper consideration of these issues involves the following steps:

    a. Develop a base of publicly available information on which issues can be addressed. This will help the Board and all stakeholders get a better understanding of the scope of the problem in Ontario. This should include information on the problems and impacts of IFRS transition for regulated entities and regulators in other countries, and compilation of research carried out by accounting bodies and academics on the impact of IFRS on regulated entities. While this should be started first, it can continue throughout some of the subsequent steps, adding further information to the body of knowledge already created. (It may be possible for the Board to build on its existing relationships and co-operation with other Canadian regulators to build this set of background information in a co-ordinated way, saving both time and money.)

b. Prepare an issues list creating a framework for the resulting proceeding or process. This should have three phases: a) the initial issue of principle arising out of the balancing between rate impacts and financial impacts, b) the subsequent analysis of the specific issues in the context of the Board's overall policy direction, and c) the implementation of the decisions on the specific issues.

c. Engage stakeholders in the initial issue of principle – balancing rate impacts vs. financial statement impacts - and make a decision. This would normally be a situation for written submissions, but it may be better in this case to have an oral component as well, to enhance the dialogue. Some stakeholders may also wish to bring in experts to assist in this phase. In dealing with this issue, it is submitted that there are a number of key steps in the analysis:

   i. In the long term, how much difference between IFRS and regulatory accounting is sustainable? The Board may determine that, while IFRS is new today, twenty years from now it will be just normal accounting, and the different regulatory rules will be archaic, a barrier to understanding utility operations, and an unwarranted cost. If the Board were to determine that a close tie between IFRS and regulatory accounting is inevitable, that would change the nature of the debate. It would become about <u>how</u> to get to IFRS-based rates in the most reasonable way, not <u>whether</u> it is a good idea.

   ii. Whether or not IFRS-based regulatory accounting is inevitable, the Board still has to address how to deal with the rate impacts, if any, including both how much rate impact is OK, what other changes can be made to mitigate the impact, and how long a transition period is appropriate given the level of rate impacts accepted.

   iii. If the Board determines that close ties between IFRS and regulatory accounting are appropriate, the Board must develop a process for considering how to handle matters that are currently dealt with by deferral and variance accounts. While the details can wait until the next phase, the initial stage has to include the decision whether to jettison these accounts altogether. If that is to happen, legislation may be required to change some of the Board's mandate.

   iv. To the extent that IFRS and regulatory accounting diverge, the Board has to assess the impact on the financial condition of the utilities, and decide the extent to which it is the Board's responsibility to fashion ways of mitigating that impact.

d. We believe that the end of the first phase of this process would be a decision of the Board, after a full debate, setting out the basic principles the Board will follow in setting rules for the IFRS transition.

e. Once that decision is promulgated, the next phase would include expert analysis by various stakeholders on the individual issues, all with the basic principles as a given. This would include consultation on those issues, perhaps a technical conference or oral hearing so that experts and parties can ask each other questions, and submissions or final argument with a formal Board decision.

f. Once the Board decides on the specific substantive issues (what are the new rules on capitalization, for example), the third phase could be a more simple consultation, likely without experts, on how those decisions should be implemented. This could be driven more by Board Staff working internally, although as is the common practice their proposals should still be published and comments invited.

61. We estimate that the above process would take, if it starts before the end of 2008, until at least the end of 2009, and likely into the spring of 2010. We have set out some proposed dates, below. Regulated entities will rightly point out that this is too late for them. They are making decisions in the winter and spring of 2009 on new systems, hiring new staff, and their overall approach to IFRS, and they need Board guidance in order to avoid wasting money and getting it wrong.

62. The utilities are correct. They need an answer in the next few months. Some of them say even that is too late, but the Draft Plan at least seeks to achieve that target. The problem is, the Board cannot give them a proper answer in that time frame. Hindsight being 20/20, it is now clear that this process needed to start a year earlier than it did, but, sadly, we can't go back in time.

63. The Board is thus faced with a Hobson's Choice: a) get it right, but in the meantime risk some of the utilities making mistakes in their implementation; or b) rush to a solution, and risk the Board making those mistakes for everyone.

64. It is our submission that there is no substitute for getting it right. This Board, and the sector it regulates, will suffer more harm by building its new ratemaking policies on a poor foundation, than it could possibly suffer by getting to an answer in an untimely fashion. Both are bad, but the former is much worse than the latter.

65. ***Transitional vs. Permanent.*** We believe that the solution is to realize that there will be a set of long-term policies for IFRS, and some short-term transitional arrangements to get the sector "from here to there". This would happen in any case, but normally the transitional arrangements would be established after the end-state is already known. In this situation, that is not possible, but it is still possible to identify some transitional arrangements that will minimize disruption while the Board is taking the appropriate amount of time to make the right policy decisions.

66. ***SEC Proposal.*** We therefore propose that the Board implement two parallel tracks, one for the long-term policy decisions, and one for transitional arrangements.

67. With respect to the long-term policy decisions, we believe the steps set forth in para. 60 above are the correct approach, and we would propose the following specific dates (which we believe to be a very tight schedule):

Steps	***Dates***
Initial Notice to Stakeholders and PO/Direction;	December 15, 2008
Engagement of external Board consultants;	January 15, 2009
Intervenors and Stakeholders state participation, cost eligibility, etc.	January 15, 2009
Submissions on Phase One Issues List	February 28, 2009
Phase One Issues List Hearing/Decision	March 5/7, 2009
Submissions (including expert reports) on threshold issue of principle	April 15, 2009
Oral Hearing/Conference on threshold issue of principle	April 25-27, 2009
Board Decision with Reasons on threshold issue of principle	May 31, 2009
PO/Direction for Phase Two (including draft Issues List)	June 15, 2009
Phase Two Issues list Hearing	June 25, 2009
Expert Reports and Initial Submissions	August 15, 2009
Technical Conference/Oral Hearing (questions by September 1/2009)	September 6-9, 2009
Final Submissions	October 1, 2009
Board Decision with Reasons on Phase Two issues	November 15, 2009
PO/Direction for Phase Three (including draft Issues List)	November 30, 2009
Board Staff files proposed new accounting model & code amendments	January 15, 2010
Submissions on implementation, accounting model, code amendments	February 15, 2010
Technical Conference on implementation and related issues	February 28, 2010
Board Decision on Phase Three issues	March 31, 2010

68. In parallel, we propose that the Board establish transitional guidelines to assist regulated entities that are making accounting and system decisions in the meantime. To establish these guidelines, it is proposed that Board Staff prepare a set of draft guidelines, and publish them for comment by January 15, 2009. After receiving comments, the Board should modify and publish the guidelines in letter form by March 31, 2009. They would not be binding, and would not deal with any of the substantive issues addressed above. We believe that the transitional guidelines would include things like:

a. In making system decisions, utilities should assume that there will be at least some material differences between financial accounting and regulatory accounting, but the extent of those differences is not yet known.

b. New systems should be selected with maximum flexibility in mind, as it will be well into 2010 before final decisions on regulatory accounting are made. Particular care should be taken to make sure that flexibility is available for dealing with regulatory assets and liabilities accounts, i.e. deferral and variance accounts.

c. No IFRS-driven changes will be made to regulatory accounting rules until the Board's consultation and policy-making process is completed. Interim changes should not be sought by utilities in rate cases, nor will they be imposed by the Board generally.

d. Similar practical advice.

The purpose of the consultation on the guidelines is to allow parties, and particularly the utilities, to identify areas in which short-term input is most desperately required, and what kinds of guidelines would be most useful.

69. It is submitted that the combination of a proper process to deal with the long-term issues arising out of IFRS, coupled with a short process to establish transitional guidelines, is the best approach the Board can take at this late date. While it is not perfect, it achieves the best possible balance, in our view, between short-term requirements and the importance of getting the policy decisions right.

Conclusion and Costs

70. We hope these submissions are of assistance to the Board in dealing with the difficult issue of how to tackle the change to IFRS. SEC would like to continue to be involved in this process, in whatever form it takes, going forward.

71. It is submitted that the School Energy Coalition has participated reasonably in this process with a view to assisting the Board in developing new policies. This process did not have provision for cost awards, and we understand and accept that no cost award is likely to be forthcoming. However, we believe that our involvement may be of material value to the Board's understanding of how best to handle this process. If the Board agrees with that assessment, we request that the Board make an exception in this case, and make an order for the payment of our reasonably incurred costs of participating in this phase of the consultation.

All of which is respectfully submitted on behalf of the School Energy Coalition on the 29th day of October, 2008.

SHIBLEY RIGHTON LLP

Per: ______________________
Jay Shepherd