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via electronic mail to: ***IFRSproject@oeb.gov.on.ca***

Mr. Bill Cowan
Chief Regulatory Auditor
Ontario Energy Board
PO Box 2319
2300 Yonge Street, 27th floor
Toronto, ON M4P 1E4

Dear Mr. Cowan:

RE: EB-2008-0104 IFRS Transition Consultation
Toronto Hydro-Electric System Limited Comments on Draft Work Plan

Introduction

Toronto Hydro-Electric System Limited ("THESL") has participated in the Board's "Consultation for the Transition of Regulatory Accounting to International Financial Reporting Standards", and offers the following comments in response to the questions posed in Board Staff's Draft Project Work Plan, dated October 7th, 2008 ("Draft Work Plan").

Responses to Draft Work Plan Questions

1.1 Entities to Which IFRS Reporting Applies

1.1.1 Should the Board require all entities to continue to report information to the Board using Canadian GAAP until December 31, 2010, notwithstanding what may occur with respect to IFRS?

RESPONSE:

On February 13, 2008, the AcSB confirmed that publicly accountable enterprises will be required to adopt IFRS in place of Canadian GAAP for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. Some of the standards will be implemented in Canada during the transition period with the remaining standards adopted at the change over date. Due to the fact that THESL is a public registrant with the OSC, THESL will be required to issue its first set of IFRS financial statements for the period ending March 31, 2011. The transition from Canadian GAAP to IFRS is a major initiative for all utilities. For these reasons, THESL believes that the Board should require all entities to continue to report information to the Board using Canadian GAAP until December 31, 2010, which is also consistent with the AcSB implementation dates.

In the unlikely event that the AcSB defers the implementation of IFRS, the Board should also permit utilities to defer the reporting of information to the Board under IFRS. However, the Board should be aware that it is possible that some utilities would prefer to start reporting for the post-2010 period under IFRS if they had planned to do so.

For clarity, due to the lag between the calendar period in question and the reporting of results for that period, THESL also submits that the Board should require entities to report information to the Board under Canadian GAAP *for the period up until* December 31, 2010.

1.1.2 Should the Board require all such entities to report information to the Board using IFRS beginning January 1, 2011?

RESPONSE:

Utilities will be required to adopt IFRS in place of Canadian GAAP for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. Due to the fact that THESL is a public registrant with the OSC, THESL will be required to issue its first set of IFRS financial statements for the period ending March 31, 2011, whereas non-public utilities will only be required to issue their first set of IFRS financial statement for the period ending December 31, 2011. Thus non-public utilities in essence have an additional year to ensure compliance. Therefore, it may not be realistic for the Board to require all utilities to report information to the Board using IFRS for any fraction of the period beginning January 1, 2011. However, the Board should require entities to report information to the Board using IFRS for the annual period beginning January 1, 2011.

Furthermore, the Board should provide application filing guidelines, specifying the basis of accounting information to be used in a rate application to the Board. The Board should recommend that cost of service applications for years after January 1, 2011 be in accordance with IFRS. Also, the Board should recommend that applications for cost of service review for years prior to December 31, 2011 be in accordance with existing Canadian GAAP. Finally, the Board should recommend that applications involving multi-year incentive regulation provide reconciliation of reported annual performance to the same basis of accounting as that upon which the incentive framework was approved.

1.2 Regulatory Assets and Liabilities

1.2.1 Should the Board continue deferral and variance accounts to achieve regulatory objectives?

RESPONSE:

The regulatory framework including the use of deferral and variance accounts should be maintained for utilities and ratepayers to be kept whole. The fact that utilities need to transition from Canadian GAAP to IFRS should have little or no bearing on the fundamental regulatory framework, to utilities or to ratepayers. The judicious use of deferral and variance accounts is required to avoid undue rate volatility and to avoid the introduction of increased risk levels for utilities and ratepayers.

Currently, IFRS does not permit specialized recognition of rate-regulated accounting under IFRS. Though IFRIC has referred the issue to the IASB for their consideration, there are no changes expected prior to the rollout and implementation dates for revised regulatory instruments under this Draft Work Plan. It is unlikely that IFRIC will make an exception for Canada, due to the fact that IFRS has been implemented in many different countries for which no special exemption was given for specialized recognition of rate-regulated accounting. Therefore, this will result in utilities maintaining two separate sets of books. Special audit opinions may be required by the Board in order to obtain assurance regarding the balances of deferral or variance accounts that are reported to the Board, but which would not be permitted under IFRS.

The fact that some or all utilities will be required, by the various regulators to whom they report, to keep two or more set of books will create both transition and ongoing incremental costs for utilities. It is fundamental that the Board permit prompt recovery of costs prudently incurred to meet these requirements.

1.2.2 If so, should Board staff propose definitions for deferral and variance accounts? This could aid the Board in their usage for regulatory purposes and enhance the ability of proposed accounts to meet the definition criteria of an asset/liability under IFRS. These definitions could be an aid for OEB regulators. They could also include a description of the information that must be included in a Board decision for an approved deferral or variance account considered necessary to meet the recognition criteria of an asset or obligation for financial reporting purposes.

RESPONSE:

Currently, the AP Handbook lists some deferral and variance accounts. The term "variance accounts" is used in Article 490 of the AP Handbook with specific reference to the definition of RSVA and RCVA Accounts. Under Article 330, page 2 discusses the Board's authority to establish "regulatory assets and liabilities" through rate making actions. In this Article, the AP handbook does provide a definition for "Regulatory debits" and "Regulatory credits", as noted on page 3. In addition, the AP Handbook lists and defines a number of specific balance sheet accounts to be used to record regulatory debits and credits, as provided for in the USoA, which include: smart meter "variance" accounts, OEB cost assessment, pension contribution "deferral" account, Regulatory

Asset Recovery Account ("RARA"), etc. However, there does not appear to be a generic definition for deferral and variance accounts provided in the AP Handbook.

Therefore, assuming that the Board continues deferral and variance accounts to achieve regulatory objectives, Board staff should propose expanded and generalized definitions for deferral and variance accounts, to enable acceptance under IFRS where possible and facilitate the transition from Canadian GAAP to IFRS. The definitions would aid the Board in their usage for regulatory purposes and enhance the prospects of proposed accounts meeting the definition criteria of assets and liabilities under IFRS. The definitions should be "open-ended" or general enough to allow for any unforeseen IFRS/regulatory adjustments.

Finally, the Board should look to the IFRS accounting framework in order to refine the current definitions of deferral and variance accounts, which would assist in recognition of assets and liabilities under both the regulatory framework and IFRS.

1.3 Accounting for Property, Plant and Equipment ("PP&E") on Initial Adoption of IFRS

1.3.1 Should the Board require historic cost/NBV to be used at the date of adoption for regulatory purposes?

RESPONSE:

In order to avoid disturbing the underlying economics of utility regulation to the detriment of utilities or ratepayers, the Board should require that the historic cost/NBV approach continue to be used, at least for the near foreseeable future. It would be impractical and imprudent to fundamentally alter the basis of regulation from historical to replacement cost at this time. However, after adequate investigation and study it may be possible in the future to depart from the historic cost basis.

1.4 Accounting for PP&E on an Ongoing Basis

1.4.1 Should the Board require historic cost/NBV values to continue to be used for regulatory purposes on an on going basis?

RESPONSE:

For the same reasons set out above, until the merits of changing the system can be clearly established, the Board should continue to use the historic cost approach to regulation.

However, while it appears clear that utilities will have to maintain two sets of books, every reasonable effort should be made to minimize that cost and the level of divergence between those books.

1.5 Application of Depreciation Accounting Under IFRS

1.5.1 Should the Board provide further guidance on depreciation policies and principles (e.g., the level of sub-componentization to be applied to specified asset classes to ensure that depreciation expenses represent a reasonable matching of recoverable costs in rates and the benefits derived by ratepayers from the consumption of the service value of the assets)?

RESPONSE:

The Board should provide “recommended” guidance on depreciation policies and principles. Depreciation expenses may change due to the required application of componentization accounting and the uncertainty of the group depreciation method continuing under IFRS. There are upward pressures on annual depreciation expense and major accounting system changes for utilities. A uniform regulatory approach would be helpful for utilities, but the Board should allow utilities to deviate from the “recommended” guidance on depreciation policies and principles, if the utility can demonstrate with appropriate rationale and support the basis for their choice.

Finally, the Board should provide guidance and recommendations with respect to the extent of componentization.

1.5.2 Should the Board encourage sector-wide depreciation studies by utilities (based on defined policies and principles)? This is especially important for electricity distributors since their current generic depreciation rates have been in effect at least as far back as 1992. There may be benefit in determining asset service lives in common for like assets. This needs to be done recognizing that asset service life is determined by an assessment of physical reality (wear and tear in use, erosion due to the action of the elements, obsolescence, etc), not by the regulator.

RESPONSE:

Sector-wide depreciation studies (based on defined policies and principles) could be beneficial since for some electricity distributors current generic depreciation rates have been in effect at least as far back as 1992. There would be a benefit in determining asset service lives in common for like assets. However, it is unreasonable to expect or require utilities, across the province or in sub-groups, to orchestrate and fund multiple and possibly overlapping depreciation studies. Instead, the Board itself or another centralized body should undertake a generic depreciation study in consultation with utilities. The costs of the study would be minimized and could then be assessed to utilities on an equitable basis.

Nevertheless, local conditions and specialized assets of some utilities would not be reflected in a generic study, so the Board should also allow and encourage utilities to undertake their own depreciation studies for specialized assets, in the event these assets are not properly reflected in the Board’s sector-wide depreciation studies.

OTHER ISSUES

With respect to Section 2.3 - Amendments to the Electricity and Gas Reporting and Record-Keeping Requirements (“RRR”) arising from changes to the APH, Electricity Distributor and Gas USoAs, THESL submits that although the Board has stated in the Draft Work Plan that “reconciliations between IFRS and regulatory accounting information may be required”, it is important for the Board to understand that utilities will face substantial challenges in preparing such reconciliations. While some utilities are exploring significant system changes and enhancements in order to be able to provide such reconciliations, there is no guarantee at this time that all amounts will be able to be reconciled and reported between IFRS and regulatory accounting, unless significant changes are made to utilities’ systems and processes, which will result in additional and unforeseen costs being incurred by utilities.

THESL hopes that its responses to these questions will be helpful in the finalization of the Draft Work Plan and thanks the Board for its efforts to engage utilities in the process. THESL looks forward to participation in the ensuing OEB consultations on this topic.

Yours truly,

[Original signed by]

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