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Private and confidential

Mr. Paul Winton,
Assistant General Counsel
KPMG
Bay Adelaide Centre
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Dear Mr. Winton,

We have been engaged by you to report on aspects related to the application of rate regulated accounting under Public Sector Accounting Standards to an “other government organization” based on the specific facts and assumptions described below. This report is being issued to you for assistance in evaluating accounting principles for the described specific facts and assumptions. Our engagement has been conducted in accordance with Canadian generally accepted standards for such engagements.

The scope of our engagement is to provide our opinion on the application of rate regulated accounting to public sector accounting standards. The scope of our engagement does not address whether the change in accounting policy requirements were met under PS 2120 and does not consider whether the Independent Electricity System Operator (“IESO”) qualifies for rate regulated accounting under ASC 980.

Statement of facts and assumptions

The facts, circumstances and assumptions relevant to the specific transaction as provided to us by KPMG are as follows:

- The IESO is classified as an “other government organization” under Public Sector Accounting Standards (“PSAS”)
- IESO has the choice to report under PSAS or under International Financial Reporting Standards (“IFRS”) and has chosen to report under PSAS
- Pursuant to the PSAS Generally Accepted Accounting Principles (“GAAP”) hierarchy as described in PS 1150 Generally Accepted Accounting Principles, IESO has adopted an accounting policy retroactively for its December 31, 2016 Financial Statements that applies the guidance in US GAAP (FASB Accounting Standards Codification 980 *Regulated Operations*) to certain balances and transactions which are subject to the rate setting mechanisms and approvals of the Ontario Energy Board
- Our report addresses certain matters relating to the application of US GAAP by the IESO in the preparation of their financial statements and not to that of the Province of Ontario.

Application of accounting principles

Our report addresses the following questions:

1. Is it appropriate for IESO to consider PS 1150 in selecting accounting policies for dealing with the effects of rate regulation?
2. In applying PS 1150 and considering sources other than the primary source of GAAP, is US GAAP an appropriate source for IESO to consider?
3. In considering sources other than the primary source of GAAP under PS 1150, should IESO give precedence to IFRS over other frameworks?
4. Is ASC 980 an exemption from US GAAP that should not be considered to provide a valid source other than the primary source of GAAP under PS 1150?

5. Do the assets and liabilities that would result from following ASC 980 meet the conceptual definitions under PS 1000?
6. Would rate regulated assets be intangibles under PSAS and therefore be precluded from being recognized?

Conclusions
Our conclusions related to the accounting principles to be applied to the specific facts and assumptions related to IESO described above are as follows:

1. It is appropriate for IESO to consider PS 1150 in selecting accounting policies in dealing with the effects of rate regulation.
2. US GAAP is an appropriate source for IESO to consider in determining an appropriate accounting policy.
3. IESO is not required to give precedence to IFRS over other accounting frameworks when considering other sources of GAAP under PS 1150.
4. ASC 980 is a fundamental component of US GAAP and is not an industry exception to US GAAP and therefore ASC 980 is a valid source to consider in the selection of accounting policies pursuant to PS 1150.
5. The assets and liabilities that result from the application of the principles of ASC 980 meet the respective conceptual definitions under PS 1000.
6. Rate regulated assets are not intangible assets and therefore they are not precluded from being recognized under PSAS.

Based on the above conclusions, a rate-regulated entity reporting under PSAS that qualifies for rate-regulated accounting under ASC 980 is not precluded from following the guidance in that section.

Authoritative Support and Supporting Rationale
Our report is based on the authoritative support and other supporting rationale described below.

Our consideration of this matter addresses the fundamental issue of whether it is appropriate for IESO to follow accounting principles developed with reference to ASC 980 in its general purpose financial statements prepared in accordance with PSAS, on the assumption that IESO would meet the specific scope and recognition criteria for following rate regulated accounting under ASC 980. We address this issue through analysis of a series of questions that would be relevant in reaching a conclusion. It should be noted that our report does not address the details of how the IESO has or should apply the principles of ASC 980 in the recording of specific regulatory assets and liabilities or in the presentation of its results of operations.

Question 1: Is it appropriate for IESO to consider PS 1150 in selecting accounting policies for dealing with the effects of rate regulation?

Paragraph .05 of PSAS 1150 states, in part, that "*When the primary sources of GAAP do not deal with the accounting and reporting in financial statements of transactions or events encountered by the public sector reporting entity, or additional guidance is needed to apply a primary source to specific circumstances, the selection of an appropriate accounting policy requires the exercise of professional judgment.*"

There is no specific standard in PSAS that addresses accounting for rate regulation, and this topic has never been addressed by the Public Sector Board. PSAB did however recently issue a general standard on recognition and measurement of assets (PS 3210) which became effective on April 1, 2017. While IESO is not required to apply PS 3210 before April 1, 2017, this standard, which has been approved by the Public Sector Accounting Board and is available for early adoption, addresses the general recognition of assets. Under PSAS, PS 3210 is required to be referenced before considering PS 1150. Although PS 3210 does provide further guidance on the concepts and principles in PS 1000, it does not provide any specific guidance which would support or prohibit the recognition of assets or liabilities arising from the effects of rate regulation under PSAS pursuant to PS 1150.

PS 3210 has a definition of an asset which is consistent with the definition of an asset under the conceptual framework PS 1000. PS 3210 does provide further guidance on what is meant by an economic resource, control, future economic benefits and past events and transactions, which are components of PSAS definition of an asset. However, this does not provide any specific guidance or indication that this standard would specifically address rate regulated accounting. Therefore, in considering whether rate regulated assets would meet the definition of an asset, PS 3210 should be looked to for guidance, but does not specifically indicate whether rate regulated assets would be permitted under GAAP. Therefore, our conclusion is that PS 3210 does not provide any additional guidance on principles related to rate regulated accounting that would need to be considered before application of the GAAP hierarchy in PS 1150.

PS 1150.009 indicates that the selection of appropriate accounting policies and disclosures requires the exercise of professional judgment. Using the GAAP hierarchy to select an appropriate accounting policy is a choice, not a requirement, and this decision does require the use of professional judgment.

Given the lack of guidance in PSAS regarding accounting for the impacts of rate regulations, we believe that it is reasonable to refer to PS 1150 to guide the exercise of professional judgment in selecting appropriate accounting policies on this topic.

Question 2: In applying PSAS 1150 and considering sources other than the primary source of GAAP, is US GAAP an appropriate source for IESO to consider?

PSAS 1150 provides the following guidance on consideration of sources other than the primary source of GAAP.

> .08
> A public sector reporting entity consults sources other than primary sources of GAAP to assist in selecting accounting policies and disclosures only when these sources comply with paragraph PS 1150.05. The public sector reporting entity evaluates sources in selecting the appropriate accounting policies and disclosures based on all of the following criteria:
>
> a) The specificity of the source — A source that deals with the specific circumstances is likely to be more relevant than one from which the public sector reporting entity must analogize.
> b) The authority of the issuer or author — A source issued by an accounting standard setter in its own jurisdiction is likely to be more relevant than a source issued by others in the same jurisdiction.
> c) The continued relevance of the source — The passage of time may diminish the relevance of certain sources.
> d) The development process for the source — A source developed after extensive consultation and debate is likely to be more relevant than a source developed without such discipline.

Consideration	***Evaluation of ASC 980 in determining appropriateness of accounting policy***
The specificity of the source — A source that deals with the specific circumstances is likely to be more relevant than one from which the public sector reporting entity must analogize.	ASC 980 deals with the specific circumstances of rate regulated accounting and therefore is considered to be a relevant standard.

The authority of the issuer or author — A source issued by an accounting standard setter in its own jurisdiction is likely to be more relevant than a source issued by others in the same jurisdiction.	ASC 980 was issued by the Financial Accounting Standards Board that establishes Generally Accepted Accounting Principles for the United States of America. While this is a different jurisdiction then Canada, there are Canadian companies that follow rate regulated accounting under US GAAP, ASPE and IFRS. Accounting for the impacts of rate regulation in Canada by referring to ASC 980 is a long-standing practice for entities subject to rate setting by regulatory bodies in various industries including Utilities, Oil & Gas and Telecommunications. While we observe that industry practice in and of itself is not a sufficient basis for developing accounting policies, we note that this industry practice has continued to be acknowledged and sanctioned by Canadian standard setters. This can be observed through the disclosure and other requirements addressing rate regulated accounting in ASPE and through the Canadian Accounting Standards Board's (AcSB) deferral of the adoption of IFRS in Canada for eligible rate regulated entities to allow time for the issuance of an interim standard by the IASB specific to entities subject to rate regulation. We also note that the AcSB has continued to be an active participant in the continued development efforts of the International Accounting Standards Board in this area. For example, in September 2016, the AcSB issued a research paper for discussion at the Accounting Standards Advisory Forum ("ASAF") titled *Results of research on the decision-usefulness of financial information that reflects the economics of rate-regulated activities*
The continued relevance of the source — The passage of time may diminish the relevance of certain sources.	ASC 980 continues to be relevant as demonstrated through the continuance of the standard through the codification of US GAAP, which occurred in 2009. ASC 980 is a continuance of SFAS 71 which was effective in 1982. While it is an older standard, ASC 980 continues to be maintained and updated as needed, as the body of US GAAP evolves.
The development process for the source — A source developed after extensive consultation and debate is likely to be more relevant than a source developed without such discipline.	FASB uses an extensive consultative due process which allows for feedback to be provided on draft standards and for a variety of stakeholders to share their views.

Additionally PS 1150 provides examples of sources that could be consulted when developing an accounting policy.

PS 1150.19

> Pronouncements issued by other bodies authorized to issue accounting standards may be useful sources to consult. For example, accounting pronouncements published with the authority of the Canadian Accounting Standards Board (AcSB), International Accounting Standards Board (IASB), US Federal Accounting Standards Advisory Board (FASAB), US Governmental Accounting Standards Board (GASB), or International Public Sector Accounting Standards Board (IPSASB) are often important sources to consult on matters not covered by primary sources of GAAP or for assistance in applying a primary source of GAAP to specific circumstances.

In looking at PS 1150.19, it is important to note that the sources provided are examples of sources to consult and that this is not an exhaustive list of sources that should be considered when developing an accounting policy. The frameworks referenced in paragraph 19 include frameworks from other jurisdictions, include frameworks for profit oriented enterprises, and frameworks specifically developed for public sector entities, which indicates that PS 1150 does not restrict entities from consulting certain types of frameworks, such as those primarily designed for profit oriented enterprises.

In consulting other sources of GAAP, PS 1150.05 and .10 indicate that the selection of an appropriate accounting involves the determination of whether that policy is consistent with the primary sources of GAAP and the conceptual framework in PSAS, as descript in Financial Statement Concepts PS 1000

PS 1150.05

> When the primary sources of GAAP do not deal with the accounting and reporting in financial statements of transactions or events encountered by the public sector reporting entity, or additional guidance is needed to apply a primary source to specific circumstances, the selection of an appropriate accounting policy requires the exercise of professional judgment. In these circumstances, a public sector reporting entity should adopt accounting policies and disclosures that are consistent with:
>
> (a) the primary sources of GAAP; and
>
> (b) the application of the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000. [APRIL 2005 *]

PS 1150.10

> A public sector reporting entity considers all sources of GAAP that it consults in the context of the concepts described in paragraph PS 1150.05(b), which describes the concepts underlying the development and use of accounting principles in financial statements. A public sector reporting entity adopts accounting policies that are consistent with these concepts. The Public Sector Accounting Board (the Board) considers a source to be consistent with the concepts in paragraph PS 1150.05(b) when the guidance in that source is compatible with the qualitative characteristics of financial information, the elements of financial statements, and the recognition and measurement criteria in paragraph PS 1150.05(b).

Paragraph .10 deals with consistency and compatibility of the frameworks on a number of fronts, including qualitative characteristics. Since PSAS is designed as a framework for financial reporting by governments, its framework will necessarily address some qualitative characteristics that are different than those of US GAAP as promulgated by the FASB. However, we believe that the most relevant considerations relate to consistency and comparability of the elements of financial statements, most notably assets and liabilities. The following compares the definition of an asset under US GAAP to PSAS:

US GAAP	PSAS
Assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.	Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.
Liabilities are probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.	Liabilities are present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits.

Both frameworks have three main components to the definition of an asset which are compared below:

	US GAAP Asset	PSAS Asset
1	Probable future economic benefits	An economic resource from which future economic benefits are expected to be obtained
2	Benefit must be obtained or controlled	The economic resource must be controlled
3	As a result of a past event or transaction	As a result of a past event or transaction

US GAAP requires the existence of probable future economic benefits while PSAS requires the expectation that future economic benefits be obtained. In our view the establishment of an expectation that future economic benefits will be obtain does equate to the requirement in US GAAP that there is probability that future economic benefits be obtained.

US GAAP does indicate that a benefit must be obtained or controlled, whereas PSAS indicates that the economic resource must be controlled. In our view both frameworks require control of an asset which is conceptually similar.

Both frameworks do require the economic benefit to arise as a result of a past event or transaction and therefor are aligned in this component of the definition of an asset.

Similarly, both frameworks have three main components to the definition of a liability which are compared below:

	US GAAP Liability	PSAS Liability
1	Probable sacrifices of economic benefits arising from present obligations	Present obligations of a government to others
2	Transfer assets or provide services	Settlement is expected to result in the future sacrifice of economic benefits
3	As a result of a past event or transaction	From past transaction and events

Both definitions require there to be a present obligation to third parties, which will result in the transfer of assets, provision of services, or sacrifice of economic benefits. US GAAP identifies that the sacrifice of economic benefits to be probable whereas PSAS uses the term expected, which we believe is conceptually similar.

Therefore based on the analysis above, US GAAP is an appropriate framework for IESO to consider in the development of an accounting policy. This conclusion is based on the fact that the criteria in PS 1150.08 indicate that US GAAP is an appropriate source, as well as the fact that the definitions of an asset under both frameworks are compatible. This conclusion has been reached while acknowledging that US GAAP is not mentioned specifically in PS 1150 as a secondary source of GAAP to consider, but based on the fact that the examples cited in PS 1150.19 are not an exhaustive list and that US GAAP meets the criteria in PSAS 1150 to be considered a valid source to refer to.

Question 3: In considering sources other than the primary source of GAAP under PSAS 1150, is IESO required to give precedence to IFRS over other frameworks?

Because IESO is an “other government organization” (OGO) as described in the CPA Canada Handbook, it has a choice between following PSAS or IFRS. IESO has chosen PSAS as the framework it will follow in preparing its financial statements. Since IFRS is designated as an alternative to PSAS for OGOs, we considered whether IFRS needs to be given precedence when considering sources other than the primary source of GAAP, or PSAS in this case.

As noted above, there are a number of criteria and attributes provided in PSAS 1150 which are to be used in considering sources other than the primary source of GAAP. However, there is no hierarchy or ordering of sources set out in PSAS 1150. Instead, PSAS 1150 sets a framework for the exercise of professional judgment. As long as the chosen source meets the criteria in PSAS 1150, we believe that it is a valid alternative source. As such, it is possible that different entities may reasonably choose different paths under PSAS 1150 when dealing with transactions or events that are not dealt with in the primary source.

There is no requirement for IESO to consider IFRS as the only, or the preferred, source other than the primary source of GAAP in its application of PSAS 1150.

Question 4: Is ASC 980 an exemption from US GAAP that should not be considered to provide a valid source other than the primary source of GAAP under PSAS 1150?

ASC 105-05-1 states the following, in part:

This Topic establishes the *Financial Accounting Standards Board (FASB) Accounting Standards Codification®* (Codification) as the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB….

Although, it is tagged under the heading "Industry" in the Codification, ASC 980 is part of the codification. It was developed following the full due process accorded by the FASB to other standards included in the codification.

Despite the seemingly clear indications that ASC 980 is an integral part of US GAAP, we went back to the basis for conclusions to FAS 71 (which is the predecessor standard that was incorporated into the codification as ASC 980) to determine its genesis and whether the FASB seemed to be considering FAS 71 as an exception to US GAAP. The basis for conclusions described what they considered to be a threshold issue, which was essentially whether accounting prescribed by regulatory authorities should be considered in and of itself generally accepted for financial reporting by rate regulated entities?

The FASB concluded as follows:

> 54. The Board concluded that regulatory-prescribed accounting should not be considered generally accepted per se, but rather that the Board should specify how generally accepted accounting principles apply in the regulatory environment.

Nowhere in the literature is rate regulated accounting referred to as an exception to US GAAP. Instead the intent was to develop guidance on how GAAP would be applied in the regulatory environment.

Further, the FASB considered the following question:

> 56. The second threshold issue in the Discussion Memorandum was: "Does rate regulation introduce an economic dimension in some circumstances that should affect the application of generally accepted accounting principles to rate-regulated enterprises?"

The conclusion regarding this question provides further relevant insights, including the FASB's application of the conceptual definition of an asset in the context of rate regulation.

> 58. The economic effect cited by most respondents is the ability of a regulatory action to create a future economic benefit – the essence of an asset. For example, consider a regulated enterprise that incurs costs to repair damage caused by a major storm. If the regulator approves recovery of the costs through rates over some future period or is expected to do so, the rate action of the regulator creates a new asset that offsets the reduction in the damaged asset. The enterprise has probable future economic benefits – the additional revenue that will result from including the cost in allowable costs for rate-making purposes. The future benefits are obtained or controlled by the enterprise as a result of a past event – incurring the cost that results in the rate order. Thus, the criteria of Concepts Statement 3 for an asset are met.

(Note that, although Concepts Statement 3 was replaced by 6, the definition of an asset was carried forward from Concepts Statement 3 to Concepts Statement 6, which sets out the current framework considerations.)

ASC 980 itself provides this explanation of the integration of the principles of rate regulation with the rest of the Codification.

15-5

[Guidance in other Codification Topics that applies to entities in general also applies to regulated entities. However, entities subject to this Topic shall apply it instead of any conflicting provisions of other parts of the Codification. FAS 071, paragraph 7] [For example, a regulator might authorize a regulated entity to incur a major research and development cost because the cost is expected to benefit future customers. The regulator might also direct that cost to be capitalized and amortized as an allowable cost over the period of expected benefit. If the criteria of paragraph 980-340-25-1 are met, the entity shall **capitalize** that cost even though Subtopic 730-10 requires such costs to be charged to income currently. That Subtopic shall still apply to accounting for other research and development costs of the regulated entity, as shall the disclosure requirements of that Subtopic. FAS 071, paragraph 7]

ASC 980 is an integral part of US GAAP, and not an exemption. It sets out the authoritative guidance as to how US GAAP is to be applied to entities subject to rate regulation meeting the established criteria. We can see this from the way the standard itself is worded and also from the basis for conclusions document, which provides the explanations of the rationale behind the standard. We would also note the FASB's stated conclusion that the impact of regulation can create assets that meet the criteria for assets as set out in the conceptual framework. The FASB would have no reason to position ASC 980 as an exemption from US GAAP, since it was considered to be consistent with the conceptual framework.

Question 5: Do the assets and liabilities that would result from following ASC 980 meet the conceptual definitions under PSAS 1000?

In determining whether it is appropriate to select an accounting policy that is based on the principles and guidance outlined in ASC 980, PS 1150 requires an assessment of the principles of the standard to determine whether it would result in a policy that is conceptually consistent with the Public Sector Accounting Standards Framework.

PS 1000. 35-.37

Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained

Assets have three essential characteristics:

(a) they embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows;

(b) the public sector entity can control the economic resource and access to the future economic benefits; and

(c) the transaction or event giving rise to the public sector entity's control has already occurred.

An item is not an asset of a government if it lacks one or more of the essential characteristics listed in the preceding paragraph. Thus, for example, an item does not qualify as an asset of a government if the item involves:

(a) no future economic benefit;

(b) future economic benefit, but the government cannot obtain it; or

(c) future economic benefit that the government may obtain, but the events or circumstances that give the government control of the benefit have not yet occurred.

Future Economic Benefit

Rate regulated assets involve a future economic benefit because they represent the amount of cost that can be recovered through future rate setting. The right to collect the incurred costs from ratepayers is a future cash inflow and therefore a future economic benefit. This is supported by PS 3210 which indicates that the future economic benefits embodied in an asset may be in the form of generation of future cash inflows. Cash inflows benefit the public sector entity because cash can be used to purchase or to provide goods and services, redistribute wealth or settle liabilities. Benefits in the form of cash inflows relate to resources, such as loans receivable, inventory for resale and portfolio investments. Also, some public sector resources generate cash inflows because they have user fees associated with them. In the case of rate regulated assets, the resource collected from rate payers is the future economic benefit, which is in accordance with PS 1000 and PS 3210.

Control of the Economic Resource

Control of an economic resource is further interpreted in PS 3210 as the ability to benefit from the economic resource, and deny or regulate access to the resource. In the regulatory environment, incurring costs creates an enforceable right to set rates at a level that permits IESO to recover those costs. Regulatory assets are generated because costs are incurred which are permitted to be recovered through future rates. Therefore, IESO controls the economic benefit as the incurrence of the cost is what gives them the right to recover the funding for the assets through rates.

Transaction or event has already occurred

The recognition of a rate regulated asset is based on the fact that the related expenditure has been incurred and that the authority to recover the cost of the expenditure from the ratepayer is in place. The electricity act of 1998 provided IESO with the right to recover costs from distributors, which indicates that once an eligible cost has been incurred, that the right to recover the cost will be met.

Based on the above analysis, we have determined that rate regulated assets would meet the definition of an asset under PSAS.

Nevertheless, since IFRS also includes similar conceptual definitions of assets and liabilities, we believe that it is also worth considering historical and recent developments around rate regulated accounting internationally. Until recently, it was a commonly held view that accounting for rate regulated assets and liabilities was not generally appropriate under IFRS. Since IFRS has similar definitions of assets and liabilities as both PSAS and US GAAP, we considered whether the absence of rate regulated accounting under IFRS in other jurisdictions casts doubt on whether rate regulated assets and liabilities do in fact meet the conceptual definitions.

Accounting for the effects of rate regulation is actively being considered by the IASB. We would observe that in recent years the situation has evolved significantly. In the June 2017 paper presented to the Accounting Standards Advisory Forum (ASAF), current IASB considerations are described in some detail, including the following discussion of rate regulated assets in the context of the conceptual definition of an asset:

“A right arises from the rate-adjustment mechanism if the entity has already partially or fully fulfilled a regulatory requirement (past event) but the current regulated rate does not yet reflect the compensation that the entity is entitled to in exchange. Even though the entity cannot compel its customers to buy the regulated goods or services, the entity's right to charge an increased future regulated rate has the potential to produce for the entity an inflow of economic benefits that are not available to other parties. That right will be consumed as the entity includes the rate increase in future regulated rates and will lead to an inflow of economic benefits if customers pay the increased future regulated rate for the future delivery of goods or services."

While this paper is not authoritative, we believe it demonstrates that current thinking around this topic is evolving such that the lack of rate regulated accounting by entities following IFRS around the world does not negate our conclusion that rate regulated assets and liabilities can be said to meet the conceptual definitions under PSAS.

Question 6: Would rate regulated assets be intangibles under PSAS and therefore be precluded from being recognized?

PS 1000.58 states that all intangible assets, including those that have been purchased, developed, constructed, or inherited are not given recognition as assets in government financial statements. Therefore we have considered whether rate regulated assets could be considered to be intangible assets and therefore precluded from recognition on IESO's financial statements.

PSAS identifies that assets can be either financial assets or non-financial assets.

PS 1000.39-42

> Financial assets are assets that could be used to discharge existing liabilities or finance future operations and are not for consumption in the normal course of operations.
>
> A financial asset is any asset that is:
>
> (a) cash;
> (b) a realizable asset that is convertible to cash;
> (c) a contractual right to receive cash or another financial asset from another party;
> (d) a contractual right to exchange financial instruments with another party under conditions that are potentially favourable to the government;
> (e) an equity instrument of another entity;
> (f) an investment in a government business enterprise or government business partnership;
> (g) a financial claim on an outside organization or individual; or
> (h) an inventory or item for sale that meets the criteria in FINANCIAL STATEMENT PRESENTATION, paragraph PS 1201.055.
>
> Non-financial assets include tangible capital assets, and other assets such as prepaid expenses and inventories of supplies.
>
> Non-financial assets are acquired, constructed or developed assets that do not normally provide resources to discharge existing liabilities, but instead:
> (a) are normally employed to deliver government services;
> (b) may be consumed in the normal course of operations; and
> (c) are not for sale in the normal course of operations.

Rate regulated assets cannot be consumed in the normal course of operations, and will be able to be used to discharge existing liabilities or finance future operations. A rate regulated asset is essentially a financial claim on an outside organization or individual that has arisen due to the fact that the regulator requires the amount to be collected in a future period. Therefore, in our view rate regulated assets would meet the definition of a financial asset under PSAS.

Intangible assets are often assets that have been purchased or created that are to be consumed by the organization and would often be considered non-financial in nature.

Additionally, under US GAAP, there is no indication that these assets are currently considered to be intangible assets. ASC 980 is not a subset or interpretation of the intangible asset standard under US GAAP.

Therefore based on the analysis, we have concluded that rate regulated assets are not considered to be intangible assets under PSAS and are therefore not precluded from being recognized under PSAS.

The ultimate responsibility for the decision on the appropriate application of regulated rate accounting under Public Sector Accounting Standards by IESO for the specific transaction described above rests with IESO management as preparers of the financial statements, who should consult with KPMG in their capacity as auditors. Our judgment on the appropriate application of Canadian generally accepted accounting principles for the specific transaction described above is based on the facts, circumstances and assumptions provided to me. Should the facts, circumstances or assumptions differ, our conclusion may change.

This report is intended solely for the information and use of KPMG, and KPMG's Office of General Counsel in order to provide KPMG with legal advice, and is not intended to be and should not be used by anyone other than these specified parties or for any other purpose except as otherwise provided for in the applicable engagement agreement.

Please contact Kerry Danyluk, National Director of Accounting Services, regarding any questions about the content of this report (416 775-7183 or kdanyluk@deloitte.ca).

Yours truly,

Deloitte LLP.

Chartered Professional Accountants
Licensed Public Accountants