IESO PSAB Accounting – Speaking Notes

- Prior to January 1, 2011, the IESO followed the Canadian Generally Accepted Accounting Principles (CGAAP) for all of its accounting included the accounting for pension and other post-employment benefits.

- On January 1, 2011, the Canadian Generally Accepted Accounting Principles (CGAAP) ceased to exist and the IESO had to move to a new accounting standard.

- The Province of Ontario classifies the IESO as an "other government organization" (OGO) within its general accounts and in all classifications. OGOs had a choice of adopting either PSAB or IFRS. ~~Only if an OGO considered itself a publicly accountable enterprise could it voluntarily adoption IFRS. Otherwise, an OGO had to adopt PSAB~~In making this choice, an OGO would normally select PSAB unless the PSAB standards did not meet the financial statement users' needs. If this was the case, IFRS would be selected.

- The IESO believed the reporting requirements of PSAB were more suitable to the IESO and the users of its financial statements than IFRS.

- The Ontario Power Authority adopted PSAB, as did the Ontario Energy Board. The Ontario Energy Board applies PSAB as required as it is a Government Component.

- The IESO's external financial statement auditors ~~were also supportive of~~concurred with the IESO's adoption of PSAB in 2011, as evidenced by their audit opinions without modification since 2011.

- The adoption of PSAB in 2011 was not as a result of government or ministry mandate, but required due to the changes in accounting frameworks as prescribed by the Accounting Standards Board of the Canadian Institute of Chartered Accountants at that time.
- The analysis of PSAB identified several areas of impact to the IESO. These areas of impact include: financial statement presentation; retirement and post-employment benefits; financial instruments; and presentation of capital assets and associated note disclosures.

- The largest area of differences between CGAAP and PSAB, for the IESO, was within the calculation of pension and post-employment benefits expenses.

- One of the key differences in this calculation is the calculation of pension and post-employment benefit expenses related to actuarial gains/loss. A process referred to as the corridor method required under CGAAP had the effect of reducing year to year volatility of the expense related to actuarial gains/losses, given the long term nature of these obligations. The IESO would no longer be able to use the corridor method to amortize actuarial gains/losses for pension expense. The corridor method was adopted by the IESO to help smooth actuarial gains/losses and thus the impact on the IESO usage fee.

Commented [LB1]: Is there a simple way to describe accrual accounting :
-Service cost for benefits being earned,
-Interest accrual on the assets and liabilities, and
-To the extent experience is different from expected, or the plan is amended, the amortization in of gains and losses in a systematic manner and the amortization of the impact of plan changes (I think under PSAB this is not amortized but maybe we can put something simple up front)
- While the key principals of accrual accounting are the same under both approaches, there are two important points
-- some of the methodology is different, and
--- the difference between the two methodologies at the transition date has to be dealt with as always the case in an accounting transition.
Then proceed into the differences and transition treatment

Commented [LB2]: I don't know that the corridor elimination is that significant versus the change in discount rate methodology

Commented [m3]: Should we be defining/describing actuarial gains and losses? That could go on for several pages.

- Changes also resulted to the discount rate~~,~~; the discount rate, used to determine the Pension Benefit Obligation, under CGAAP was determined based on high quality corporate bond yields whereas under PSAB the discount rate was based on management's expected long-term experience and short-term forecasts for a return on asset assumption. This change has ~~results~~ resulted in a more stable discount rate assumption (and since the transition date a lower liability than would have been recognized under the prior standard).

- Beginning in 2011 under PSAB, past service costs from plan amendments would be expensed immediately. Past service costs are incurred when additional benefits or enhancements to existing benefit plans are provided to existing employee groups without the need for additional service by the employee. Under CGAAP, past service costs were recognized over a specified period of time.

- Upon first-time adoption, PSAB required retrospective application with restatement of the prior periods with four possible exemptions. Only one exemption applied to the IESO and it related to the retirement and post-employment benefits. Namely, at the date of transition, the IESO could elect to transfer all cumulative actuarial losses directly to an accumulated deficit account ($140 million as of the end of 2009 for pension and other post-employment benefits) instead of recalculating the losses retrospectively from 1999 without a corridor method or changes to discount and asset return rates.

- Considering the cost to undertake the recalculation and the fact that the IESO has historically had rates approved based on accounting expenses, the IESO elected to use this ~~exception~~exemption.

- The changes in accounting standards were expected to have implications on the 2011 and future rate cases and these were discussed at the IESO's 2011 rate case with the Ontario Energy Board.

- It was noted that the Ontario Energy Board (OEB) report issued by the Board in July 2009, discussed the types of changes mentioned above for the adoption of IFRS and the Board provided explicit principles to rate regulated entities. More specifically the stated principles for setting regulatory accounting, reporting and filing include fairness, minimizing intergenerational inequity and minimizing rate volatility.

- The Board confirmed its expected continuation with the current approach of establishing and clearing of deferral and variance accounts, which the IESO used to account for the transfer of cumulative actuarial losses and past service costs into a deficit account.

- Actuarial gains/losses occur when the actual experience differs from the assumptions that were used in the calculations that derived the pension expense and the expense for other post-employment benefits. This amount fluctuates each year, sometimes as a loss and sometimes as a gain. The most common sources of gains and losses are investment returns different from expected as well as changes in liability resulting from changes (most recently reductions) in the discount rate used to measure the obligation.

- At the transition date of January 1, 2010 [being the beginning of the comparative period for the 2011 financial statements] the unrecognized actuarial loss for pension benefits was $72 million

Commented [LB4]: Note that under CICA 3461 the unrecognized losses and prior service cost were combined $167 million at dec 31 2010. The change in discount rate in particular reduced the amount of loss that needed to be recognized on transition.

Commented [m5]: Move up in the document? Agreed – LB – move up in the document

IESO-N-0039927

and the unrecognized actuarial loss for OPEB was $5 million. These amounts were recognized in accumulated deficit.

- Under CGAAP, the amount of actuarial gain/loss was amortized (i.e., recognized as an expense for financial statement purposes) over the estimated average remaining service life of employees (EARSL) and the amortized portion was included in ~~the~~ expenses.

- With the adoption of PSAB, this principle was held constant, with the amount transferred into the accumulated deficit account also amortized over EARSL and included in the expense.

Commented [m6]: I don't follow this comment.

- Past service costs relating to pension and other post-employment benefits occur when plan amendments are made and the expenses are based on the total service of the employee instead of a go-forward benefit.

Commented [m7]: Move up and put this in place of the definition that I had suggested?

- At the transition date of January 1, 2010, the IESO had $2 million and $172 thousand in unrecognized past service costs relating to pension and OPEB, respectively. These amounts were recognized in accumulated deficit.

- Under CGAAP, the amount of past service costs were amortized on a straight-line basis over the estimated average remaining service life of employees (EARSL) and the amortized portion was included in the expense.

- With the adoption of PSAB, this principle was held constant, with the amount transferred into the accumulated deficit account also amortized over the remaining EARSL and included in the expense.

Commented [m8]: Similar to above, not sure I follow this.

- This total unrecognized actuarial loss and past service costs restated to accumulated deficit as a result of the transition to PSAB was $80 million, which as a matter of fact is much lower than the accumulated loss and past service cost that was being amortized into expense under CGAAP.

- The approach of amortizing the actuarial loss and past service costs constant when calculating the annual pension expense and other-post employment benefit expense was consistent with the stated principles expressed by the Ontario Energy Board.

- These amortized costs are recorded and publicly disclosed in the annual report of the IESO.

- To the end of 2015, $33 million of the $80 million has been amortized into the expense.

I think what you are trying to get at towards the end is that the unamortized losses that were transferred to the accumulated deficit at the date of transition are being "transferred" over EARSL from a special accumulated deficit account to the general accumulated deficit account. At the same time, IESO is including in its annual revenue requirement the amount of the annual transfer. By doing so, the IESO is recovering the costs on a systematic basis over the same time period that it was recovering under CGAAP, prior to the switch to PSAB.

As the actuary I think it is worth mentioning that none of this changes the ultimate and actual cost of the pension and OPEB plans or the benefits earned by members. The ultimate cost is the benefits paid to members and at the end of the plan' s existence the accounting cost will equal the actual plan cost.