

International Financial Reporting Standards (IFRS) – posted November 2011

IFRS Project

In 2006, the Canadian Accounting Standards Board (AcSB) published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian generally accepted accounting principles with International Financial Reporting Standards (IFRS) over an expected five year transitional period.

Our changeover date for the conversion to IFRS was originally April 1, 2011. However, the AcSB has amended Part 1 of the CICA Handbook – Accounting to require:

- o Qualifying entities with rate-regulated activities to adopt IFRSs for the first time no later than annual periods beginning on or after January 1, 2012; and
- o Entities electing to defer the first-time adoption of IFRS to disclose that fact.

The Canadian Securities Administrators' regulations have also been amended to incorporate the AcSB's one-year deferral.

We have elected this option which defers our changeover date for conversion to IFRS to April 1, 2012.

Transition to IFRS will require the restatement for comparative purposes of amounts reported by us for the year prior to changeover date. We are monitoring ongoing standards development as issued by the International Accounting Standards Board (IASB) and the AcSB as well as regulatory developments as issued by the Canadian Securities Administrators, which may affect the timing, nature or disclosure relating to our adoption of IFRS.

The transition to IFRS may materially affect our reported financial position and results of operations. As future balances of our regulatory accounts are uncertain, we cannot reasonably estimate and conclude the impact of IFRS on our future financial position and results of operations.

We commenced our IFRS transition project in 2007 and have established a formal project governance structure with regular reporting. We have also engaged a quality assurance advisor to assist in the project.

Our IFRS transition project consists of three phases:

1. Scoping and diagnostic phase, which has been completed, involved project planning and resourcing, high level impact assessment of differences between current Canadian GAAP and IFRS, and priority setting;
2. Analysis and development phase, which has also been completed, involved detailed analysis and evaluation of options and alternative methodologies available under IFRS, and the financial impact of these options; and
3. Implementation and review phase which involves implementing and approving changes to accounting policies, information systems, business processes and training, and developing IFRS-compliant financial statements.

We are currently in the implementation and review phase.

The following table includes elements of our IFRS transition plan and an assessment of progress towards achieving the key milestones which have been amended to reflect our election to defer our changeover to IFRS by one year, to April 1, 2012. We are working through a detailed IFRS transition plan and certain project activities and milestones could change. Further, changes in regulation or timing of standard development throughout the project could result in changes to the transition plan.

Financial statement preparation

Key activities

- Identify differences in Canadian GAAP/IFRS accounting policies
- Select ongoing IFRS policies
- Develop financial statement format
- Select IFRS 1 exemptions for transition
- Quantify effects of change at April 1, 2011 (for fiscal 2012 comparative financial statements)

Milestones

- Senior management review of policy decisions and illustrative IFRS financial statements and disclosures by June 30, 2011
- Audit & Finance Committee approval of policy decisions and IFRS financial statement format, in principle, by September 30, 2011
- IFRS 1 exemptions finalized and quantified by September 30, 2011
- Policies and procedures in place by March 31, 2012

Status

- Scoping and diagnostic phase completed in fiscal 2009, with high-level review of the major differences between Canadian GAAP and IFRS
- Highest areas of impact identified, review prioritized, and in-depth analysis complete
- Accounting policy alternatives analyzed and recommendations made for key accounting policy decisions
- IFRS 1 exemptions reviewed and analyzed
- Senior management review of policy decisions complete
- Preparation of illustrative financial statements and note disclosures complete
- Senior management review of illustrative financial statements complete
- Audit & Finance Committee review of illustrative financial statements complete
- IFRS 1 exemptions finalized and quantified
- Policies complete and procedures nearing completion

Information technology infrastructure

Key activities

- Confirm system upgrades required for IFRS reporting
- Review/revise data gathering processes
- Review/revise budgeting and forecasting processes

Milestones

- System configuration changes complete by March 31, 2010
- System reporting changes required to accommodate both current Canadian GAAP and IFRS complete by August 31, 2010
- Changes to budgeting and forecasting processes complete by June 30, 2011

Status

- Detailed reporting requirements to accommodate the transition to IFRS identified and documented
- Overall system approach selected
- System configuration to accommodate both current Canadian GAAP and IFRS complete
- System changes to accommodate reporting requirements complete
- Review to determine effects on the project of one-year deferral of changeover and absence of standard on rate-regulation complete
- Changes required to budgeting and forecasting processes complete

Training, Education & Communication
<p>Key activities</p> <ul style="list-style-type: none"> • Determine required level of IFRS expertise within all areas of the company • Ensure appropriate training of key members within Finance • Provide appropriate education and communication to affected departments • Provide department specific training on revised policies and procedures • Provide timely communication to both internal and external stakeholders on impacts of the transition to IFRS
<p>Milestones</p> <ul style="list-style-type: none"> • Topic-specific training for IFRS working committee complete prior to March 31, 2010 • Department-specific training completed by March 31, 2012 • Impacts of transition to IFRS communicated to external stakeholders by March 31, 2012
<p>Status</p> <ul style="list-style-type: none"> • Core IFRS project team members completed topic-specific training, and successfully completed the "IFRS Award Program, Certificate Level" through the Institute of Chartered Accountants in England and Wales • Interdepartmental workshops provided on specific topics, including property, plant and equipment; IFRS 1; and the IFRS Framework • Training requirements identified and training plan developed for stakeholders • Ongoing communications with key stakeholders, including direct communication with the Commissioner, our Agent Bank, rating agencies, our Board of Directors, and with investors indirectly through our website • Interdepartmental training on specific topics underway
Control environment
<p>Key activities</p> <ul style="list-style-type: none"> • Accounting policy determination, documentation and implementation • MD&A ongoing communications
<p>Milestones</p> <ul style="list-style-type: none"> • All internal control process descriptions updated by March 31, 2012 • Publish quantitative effects of conversion on April 1, 2011 opening balance sheet in December 31, 2011 MD&A
<p>Status</p> <ul style="list-style-type: none"> • Analysis of control issues in progress as part of the detailed implementation plan • Review and update of process descriptions in progress • Policies complete and procedures nearing completion
Business policy assessment
<p>Key activities</p> <ul style="list-style-type: none"> • Financial covenants assessment • Compensation arrangements assessment • Customer and supplier contract evaluation
<p>Milestones</p> <ul style="list-style-type: none"> • Potential impact on compensation arrangements determined by December 31, 2011 • Impact on customer/supplier contracts determined by December 31, 2011 • Impact on financial covenants quantified by March 31, 2012
<p>Status</p> <ul style="list-style-type: none"> • All relevant GAAP-dependent covenants and contracts have been identified • Analysis to determine effects of IFRS on existing covenants and contracts is substantially complete

A summary of progress in the review of areas identified to have the highest potential to impact us is as follows:

- Rate-regulated operations: IFRS does not currently provide specific guidance with respect to accounting for rate-regulated activities. In December 2008, the IASB initiated a project on accounting for rate-regulated activities that had an objective to develop a standard on rate-regulated activities that would clarify whether regulated entities could or should recognize assets or liabilities as a result of rate-regulation imposed by a regulatory body.

In September 2010, the IASB staff released Agenda Paper 12 on rate-regulated activities. In their opinion, while the impact of regulators may have an economic impact on entities subject to rate-regulation:

- Regulatory assets do not meet the definition of a financial asset nor the definition of an intangible asset as specified in IAS 38; and
- Regulatory liabilities do not meet the definition of a financial liability nor the definition of a provision as specified in IAS 37.

The IASB closed its project on rate-regulated activities. However, the IASB has commenced consulting constituents to seek input on their strategic direction and preparation in setting work plans over the next three years. It has also provided constituents with suggestions for items to add to their agenda, including rate-regulated activities. We have provided a response in support of reinstating a project on rate-regulated activities.

It is our expectation that issues regarding rate-regulated activities will remain unresolved for some time and that we will not be reporting our regulatory assets or liabilities on the IFRS Statement of Financial Position. Accordingly, balances at March 31, 2011 of \$3.7 million of current regulatory assets and \$1.6 million of long-term regulatory liabilities will be derecognized on our transition date of April 1, 2011 with a net reduction in retained earnings of \$2.1 million.

As future balances of our regulatory accounts are uncertain, we cannot reasonably estimate and conclude the impact on our future financial position and results of operations with respect to accounting for rate-regulated activities.

- Property, plant and equipment:
 - *Inspections and major overhauls:* The capitalization of inspections and major overhauls of our vessels is a significant change affecting us. A process to track these items has been finalized and necessary system configuration changes have been completed. We have defined, identified, and quantified inspection and major overhaul items for each class of vessel for reclassification at transition date and internal reporting solutions are nearing completion. This change has the potential to cause significant fluctuations in earnings over the reporting periods due to the level of inspections and major overhauls in any one period and the number of periods over which each will be amortized.
 - *Valuation subsequent to transition:* We have a choice under IFRS to value our property, plant and equipment using either a historical cost model or a revaluation model. We have decided to use a historical cost model for all property, plant and equipment with the exception of land. We will use a revaluation model for our land.

- IFRS 1 *First-Time Adoption of IFRS*: All elections and exemptions under IFRS 1 have been reviewed and the choices we have made will result in a net increase of \$8.6 million in retained earnings on transition. The elections and exemptions that apply to us upon adoption are summarized as follows:
 - *Employee Benefits*: There is a choice to either recognize all cumulative actuarial gains and losses of defined benefit plans through opening retained earnings or recalculate the actuarial gains and losses under IFRS from the inception of the defined benefit plans. We have elected to recognize all cumulative actuarial gains and losses through opening retained earnings at April 1, 2011. The actuarial loss to be recognized in opening retained earnings is \$3.6 million.
 - *Property, plant and equipment and Intangible assets*: There is a choice of valuation of property, plant and equipment and intangible assets at April 1, 2011, either to:
 - ▶ retrospectively apply IFRS to the valuation of the assets; or
 - ▶ to revalue items, on an asset by asset basis, at fair value and use that fair value as deemed cost; or
 - ▶ use previous GAAP carrying amounts at transition as the deemed cost for assets used in rate-regulated operations as detailed in the amendment to IFRS 1 published May 6, 2010.

We have elected to use previous GAAP carrying amounts at transition as the deemed cost for all intangible assets and the majority of our property, plant and equipment with the exception of land. We have elected to revalue land at fair value at April 1, 2011. This revaluation will result in an increase in land value of \$12.2 million.

- Intangible assets: There is substantially no change in IFRS from Section 3064, *Goodwill and Intangible Assets*, which we adopted April 1, 2009. The adoption of this guidance is not expected to have any significant effect on our consolidated financial statements.
- Asset impairment: Policies and processes regarding asset impairment and potential subsequent reversals have been completed. The adoption of this guidance is not expected to have any significant effect on our consolidated financial statements.