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July 26, 2012

Mr. Duane McNair, CGA
Treasurer and Vice-President, Administration
Algonquin College
1385 Woodroffe Avenue
Ottawa, ON K2G 1V8
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Dear Sir:

Draft Energy Performance Contract (EPC) – Accounting consideration

Thank you for providing us with the draft energy performance contract dated April 23, 2012 between Algonquin College and an Energy Services Company (ESCO).

We understand that the College's predecessor auditors provided you on June 29, 2006 with a letter describing the accounting impact of a similar proposed energy performance contract. Paragraph 7600.06 of the Canadian Institute of Chartered Accountants' Assurance Handbook (Reports on the Application of Accounting Principles) prohibit us in providing a written opinion (…) on the application of accounting principles of a hypothetical transaction; as such we cannot provide an opinion on this hypothetical transaction. Notwithstanding the previous, we have summarized the facts surrounding the draft contract and the related guidance under Public Sector Accounting Standards as they apply to the proposed transaction and the accounting impacts to the College.

We noted the following key facts related to the draft energy performance contract and discussions with the College's management that:

- Upon signature of the draft energy performance contract, the College will enter into a lease agreement for a period of up to 20 years with ESCO.
- The College's financial obligations with regards to lease payments are to pay ECSO a percentage of the savings calculated using a pre-determined formula based entirely on energy usage of the selected buildings There are no other financial obligations related to lease payments.
- Upon completion of the contract, the College will acquire the equipment at a cost of $1.
- The College is deemed a government not-for-profit organization in accordance with the Introduction to Public Sector Accounting Standards (the "Introduction") and has elected in accordance with paragraph 7 of the Introduction to adopt accounting standards for government not-for-profit organizations (e.g. Section 4200 of Public Sector Accounting Standards), supplemented by Public Sector Accounting Standards.

The following summarizes the accounting impacts related to lease agreements in the Public Sector Accounting (PSA) Handbook:

- The accounting guidance in the PSA Handbook for lease agreements is included in Public Sector Guidance 2 (PSG-2), "Leased Tangible Capital Assets". Paragraph 2 of the Introduction to Accounting Guidelines states that "Guidelines are a primary source of GAAP"; as such, the College is subject to the accounting interpretations included in this Guideline.
- Paragraph 4 of PSG-2 details the quantitative criteria for determining whether a lease should be classified as a capital lease or an operating lease[1].
    - The first criterion states that "There is reasonable assurance that the government will obtain ownership of the leased property by the end of the lease term." As previous indicated, the College will obtain ownership of the assets for an amount of $1.
    - As such, a criterion is met, and the lease would be deemed a capital lease.
- Paragraph 14 of PSG-2 defines the amount to be recorded for a capital lease; specifically, "The value of the leased tangible capital asset and the amount of the lease liability, recorded at the beginning of the lease term, would be the present value of the minimum lease payments, excluding the portion thereof relating to executory costs."
    - PSG 2, paragraph 22 states that "contingent rentals should be charged to expense as incurred", i.e. they are not capitalized as part of the asset or liability.
    - The Glossary to PSG-2 defines contingent rentals as "rental that is based on a factor other than the passage of time. However, if some portion of the factor (e.g., a minimum capacity or expected usage) is reasonably estimable at inception of the lease, the contingent rental portion includes only that proportion that is greater than a minimum capacity or expected usage that is reasonably estimable at inception of the lease."
    - Contingent rentals are not part of the minimum lease payments; as such, the only amount that would be capitalized by the College would be the purchase amount of $1. The accounting entry would be as follows:

DT: Capital asset	$1[2]
CT Capital Lease obligation	$1

[1] The College should note that the quantitative criteria under PSG-2 are similar to the criteria under CICA Handbook Section 3065, "Leases", which was the previous accounting framework the College used for financial reporting purposes.
[2] This amount would be discounted to its net present value; for presentation purposes, the purchase amount is included in the accounting entry.

Our analysis described above represents our professional assessment based on current accounting standards and facts, circumstances and assumptions provided to us, which have not been audited. Should the facts, circumstances or assumptions differ, our conclusion may change. Our advice is as of the date of this report and we do not assume any obligation to update this report for subsequent changes in relevant rules or practice. Our report is intended solely for the information and use of Algonquin College and is not intended to be and should not be used by anyone other than Algonquin College.

If you have any questions, please don't hesitate to contact us at (613) 751-5234 or by e-mail at sedesrochers@deloitte.ca.

Yours truly,

Chartered Accountants
Licensed Public Accountants

Enclosure