30 August 2013

Attention: Mr. Hans Hoogervorst
Chair, International Accounting Standards Board
30 Cannon Street
London EC4M6XH
United Kingdom

Dear Mr. Hoogervorst:

Re: Exposure Draft ED/2013/5 Regulatory Deferral Accounts

CAMPUT, Canada's Energy and Utility Regulators, appreciates this opportunity to respond to the International Accounting Standards Board's (the IASB's) Exposure Draft Regulatory Deferral Accounts (the "Exposure Draft" or "interim Standard").

CAMPUT consists of the following fourteen federal, provincial, territorial rate regulators of electricity and natural gas in Canada[1]:

- Alberta Utilities Commission
- British Columbia Utilities Commission
- Manitoba Public Utilities Board
- National Energy Board
- New Brunswick Energy and Utilities Board
- Newfoundland & Labrador Board of Commissioners of Public Utilities
- Northwest Territories Public Utilities Board
- Nova Scotia Utility and Review Board
- Nunavut Utility Rates Review Council
- Ontario Energy Board
- Prince Edward Island - Island Regulatory and Appeals Commission
- Régie de l'énergie du Québec
- Saskatchewan Rate Review Panel
- Yukon Utilities Board

The objectives for the above regulatory bodies of electricity and gas sectors, among others, include protecting the interests of consumers with respect to prices and the adequacy, reliability and quality of services and promoting economic efficiency and cost effectiveness in the generation, transmission, and distribution of electricity, gas and oil. To serve the public interest and to maintain financial viability of the regulated companies are the key common, high-level objectives of the Canadian rate regulators. The Canadian rate regulators' comments in this document, unless otherwise specified, relate to rate-

[1] Some of the Canadian regulatory agencies also regulate oil pipelines, water and sewer utilities and other non-utility mandates.

regulated companies that are first time adopters of IFRS, since the scope of the Exposure Draft has been limited to these entities. Overall, all the Canadian rate regulators strongly support the interim Standard and the IASB's proposals contained in the Exposure Draft for regulatory deferral accounts. The Canadian rate regulators endorse the IASB's initiative to enable rate-regulated utilities to continue to recognize regulatory balances in their financial statements. The chairs of these regulatory commissions and boards have approved the contents of this comment letter and considered it very important that the interim Standard be put in place.

We are encouraged to observe that the IASB will permit rate-regulated utilities to apply financial accounting policies for financial reporting that are similar to those determined by rate regulators for the purposes of rate-making. We applaud the IASB's effort in developing the draft interim Standard to reduce uncertainty until the IASB completes its Comprehensive Rate-regulated accounting project**. It is our position that it would be a significant detriment to rate-regulated utilities in Canada, their rate-setting authorities, and their investors and financers if the interim Standard was not to be adopted in substantially the form proposed.** The reasons for our position to fully support the interim Standard are explained in the following paragraphs using the IASB's Effects Analysis, as outlined in the Exposure Draft. We have also provided additional comments in the Appendix to this letter in response to the ten questions from the IASB.

In evaluating the likely effects of permitting rate-regulated entities that are first-time adopters of IFRS to continue to recognize regulatory deferral account balances, IASB has considered the following factors in its Effects Analysis:[2]

a) How the proposed changes to the presentation of regulatory deferral account balances affect the financial statements of a rate-regulated entity.

We strongly endorse the IASB's statement "A number of rate-regulatory methodologies exist and, for each, application can vary by rate regulator, the entity that is being regulated and the particular circumstances. The objective of many methodologies is **to set 'just and reasonable' rates**, in other words, rates that balance both customer and investor interests. Rate regulators that use such methodologies establish rates that charge customers a fair price and are reasonably stable from year to year. At the same time, these rate regulators wish to ensure that the entity that is providing the regulated goods or services **remains financially viable**. Consequently, they may set rates to not only recover the costs of providing the goods or services, but also to provide a fair return to the entity's owners [emphasis added in bold]."[3]

We agree with the IASB that "regardless of the regulatory methodology that is used, the economic reality of an entity with operations that are subject to rate regulation is shaped in part by the actions of its rate regulator. By restricting prices, rate regulation can affect the amount and timing of the entity's revenues and cash flows, thereby affecting its financial position and performance."[4] We support the IASB's observation that "the nature and extent of rate regulation can have **a significant impact on the amount and timing of revenue and cash flows of a rate-regulated entity** [emphasis added in bold]".[5] We endorse the IASB's position that "discontinuing the recognition of regulatory deferral account

[2] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC70, page 45.
[3] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC23, page 33.
[4] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC27, page 34.
[5] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC66, page 44.

balances in advance of the comprehensive Rate-regulated Activities project could be a significant barrier to the adoption of IFRS for those entities for which **regulatory deferral account balances represent a significant proportion of net assets** [emphasis added in bold]".[6] As noted by the IASB, because of significant impact on the amount and timing of revenue and cash flows of a rate-regulated entity and because of significance of deferral account balances, rate regulators need to ensure the entity that is providing the regulated goods or services remains financially viable. This is part of the objective of setting just and reasonable rates for rate-regulated utilities. We note that IASB has acknowledged these considerations throughout the Exposure Draft as benefit drivers for developing the proposed interim Standard in order to remove a major barrier to the adoption of IFRS for many rate-regulated entities.[7,8]

The interim Standard resolves one major problem for entities with rate-regulated operations. Our observation is that, without the interim Standard, these rate-regulated entities will be required to provide two sets of financial statements, as has happened in some other jurisdictions and as was acknowledged by the IASB[9]: one to meet general purpose financial reporting requirements under IFRS; and, the other to present to the rate regulator for purpose of (i) requesting rate adjustments, (ii) regulatory accounting and rate-making, and (iii) regulatory reporting. As regulators, we find it unsatisfactory and not serving the public interest if there are two views of economic reality of entities with rate-regulated operations. Rate regulators are aware that their actions have significant economic impact, including investment, lending and consumer prices. The IASB has acknowledged that many of rate-regulated entities argue that recognizing such balances as assets and liabilities would provide more relevant information and would be a more representationally faithful way of reporting their rate-regulated activities.[10] Some of these utilities had to eliminate regulatory deferral account balances from the statement of financial position when they adopted IFRS and do not recognize such balances in IFRS financial statements. It behooves the accounting profession to find the appropriate ways to ensure all economic events are reflected in the base numbers reported in general purpose financial statements. Requiring rate-regulated entities to leave certain economic events outside the purview of the financial statements, or at best relegated to note disclosure, is not good enough for regulatory actions that affect prices. Furthermore, exclusion of certain economic events would not serve the needs of users of the financial statements.

Finally on this point, the results of having two views will add confusion and unnecessary complexity and higher cost to the rate-regulated entities and their customers such as maintaining two sets of books. Furthermore, the investors or the lenders of the rate-regulated entities will find it confusing to decide which set of financial statements to use when monitoring financial performance to judge the financial soundness of the enterprises. The IASB's proposed interim Standard addresses the above concerns. Therefore, we support the IASB's development and application of the interim Standard.

b) Whether those changes improve the comparability of financial information between different reporting periods for a rate-regulated entity and between different rate-regulated entities in a particular reporting period.

On this point, we fully support the IASB's views and reasons that the interim Standard will help achieve the following two stated IASB's objectives:

[6] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC15, page 31.
[7] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC20, page 32.
[8] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC70, page 45.
[9] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC84, page 48.
[10] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC10, page 30.

(a) "enhance the comparability of financial reporting by reducing barriers to the adoption of IFRS by entities with rate-regulated activities until guidance is developed through the IASB's comprehensive Rate-regulated Activities project; and

(b) ensure that users of financial statements will be able to identify clearly the amounts of regulatory deferral account balances, and movements in those balances, in order to be able to compare the financial statements of entities that recognize such balances in accordance with this [draft] interim Standard against the financial statements of entities that do not recognize such balances." [11]

Contrary to the views of Messrs. Gomes and Zhang, we believe that the objectives of general purpose financial reporting and regulatory reporting are not competing with each other; rather they are complementary, and therefore must be integrated to better serve the public interest and all users of the financial statements of entities with rate-regulated operations. The interim Standard will help bring the financial statements closer to the economic reality of the rate-regulated entities. We agree with the IASB that the interim Standard will improve the comparability between different reporting periods for a rate-regulated entity and between different rate-regulated entities in a particular reporting period. Our position is that IASB's proposed changes to recognize valuing and reporting regulatory deferral account balances not only enhance the comparability of information within the general financial statements, but also, they offer transparency of financial information to the users. Thus, the proposed changes by the IASB are vital to the credibility and usefulness of any financial statements that are prepared for the users.

c) Whether the changes will improve the quality of the financial information that is available to investors and its usefulness in assessing the future cash flows of a rate-regulated entity.

As one of the key users of financial statements, the lending and investment communities of the rate-regulated utilities will be most negatively impacted if regulatory deferral account balances are not recognized and reported in the rate-regulated utilities' financial statements.

Our position is that the IASB's interim Standard will improve the quality of the financial information that is available to investors and its usefulness in assessing the future cash flows of a rate-regulated entity. This is due to the fact that recognition of regulatory deferral accounts in the financial statements will increase transparency related to:

- "the amounts that the rate regulator decides are included as allowable costs when determining the customer rates and the amounts that eventually are recognized through the entity's statement of profit or loss and other comprehensive income for financial reporting purposes;"[12] and

- "all of the entity's expenditures that could have a significant effect on rates are usually subject to a prudency review by the rate regulator. This includes expenditures for the construction of property, plant and equipment and some intangible assets." [13]

[11] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, page 5.
[12] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC27, page 34.
[13] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC27(b), page 34.

We note that interim Standard states that "If a single cause has a significant effect on a regulatory deferral account balance, the entity shall disclose it separately"[14] and "when an entity concludes that a regulatory deferral account balance is no longer fully recoverable, it shall disclose that fact, the reason why it is not recoverable and the amount by which the regulatory deferral account balance has been reduced."[15] First, such transparency and availability of the financial information to lenders and investors will permit them to clearly note the facts, assess possible risks, and determine if the amounts reported in the financial statements are fairly and appropriately represented. Furthermore, having the financial information disclosed in financial statements is useful to investors and lenders because it provides them with a higher level of relevancy, reliability, and accuracy of information related to the recoverability of the amounts. Finally, transparency regarding financial information arising from rate-regulated activities will allow these users to make consistent apples to apples comparisons among these entities and make informed decisions.

We believe that the public interest is impaired by the fact that the transparency that exists today under current Generally Accepted Accounting Principles for these key users of the financial statements could be diminished in absence of the recognition of regulatory deferral accounts. Rate-regulated entities are capital intensive and require substantial financing. It is quite possible that a lack of transparency in how regulatory deferral account balances are reported and disclosed could lead to a higher risk assessment (lower credit rating) and therefore increased financing costs. This may further lead to higher costs to rate-regulated utilities, the lending and investing communities, and rate payers because of a false perception of increased risks.

d) Whether users will benefit from better economic decision-making as a result of improved financial reporting.

Rate regulation can significantly affect the economic environment of rate-regulated entities and their operations. The IASB has also noted this by stating "the nature and extent of rate regulation can have a significant impact on the amount and timing of revenue and cash flows of a rate-regulated entity. Hence, the IASB concluded that such disclosures should be part of the financial statements and that they could be given either in the financial statements or incorporated by cross-reference from the financial statements to some other statement that is available to users of the financial statements on the same terms as the financial statements and at the same time. IASB has also stated that this approach is consistent with certain risk disclosures required by IFRS 7 *Financial Instruments: Disclosures.*"[16]

We agree with the IASB that proposed changes and especially the improvements in comparability noted in paragraphs BC76–BC77, compared to the current IFRS standards will provide all users of financial statements including rate-regulated enterprises, the preparers of statements, the lenders and investors, the regulator, and the rate payers with relevant and reliable information to help them better understand the impact of rate regulation on rate-regulated entities and make informed decisions. The interim Standard can help improve the communication of relevant information for users of financial statements, rather than leaving it to the users to identify the nature and extent that rate-regulation can have on the amount and timing of revenue and cash flows arising from rate-regulated entities' activities. As the economic rate regulators who use and rely on the audited financial statements, we recognize the

[14] Draft International Financial Reporting Standard - Regulatory Deferral Accounts, paragraph 28, page 16.
[15] Draft International Financial Reporting Standard - Regulatory Deferral Accounts, paragraph 33, page 17.
[16] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC66, page 44.

significance of the interim Standard to our rate making decision process. In the absence of regulatory deferral accounts under IFRS, the interim Standard will provide temporary relief to enable the public to discern that the Regulators have set just and reasonable rates for rate-regulated entities, and monitor their financial performance.

e) ***The likely effect on compliance costs for preparers, both on initial application and on an ongoing basis; and whether the likely costs of analysis for users are affected.***

IASB has rightfully determined that the likely effect of these proposals on the costs of analysis for users of financial statements is expected to be outweighed by the benefits of improved reporting. It stated that the proposals should have little or no impact on the net assets or on the net profit reported in the financial statements of those entities within the scope of the draft interim Standard.[17]

In summary, we support the IASB's decision to prioritize the issues related to rate-regulated activities through the interim Standard. We believe that the IASB's proposed interim Standard begins to address our concerns and resolves the uncertainty and apparent exclusion of rate-regulated activities from IFRS compliant financial statements that would otherwise occur. We view the IASB's interim Standard as a means to align financial reporting with the regulatory rate-making and regulatory accounting and reporting.

Attached are our responses to the questions in the invitation to comment. If you require any further information, please contact me at the telephone number below or at rochefort@camput.org.

Yours very truly,

Terry Rochefort
Executive Director, CAMPUT
Telephone: +1 905 827-5139

[17] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC72, page 46.

Appendix: Response to Questions in the Exposure Draft

Question 1

The Exposure Draft proposes to restrict the scope to those first-time adopters of IFRS that recognised regulatory deferral account balances in their financial statements in accordance with their previous GAAP.

Is the scope restriction appropriate? Why or why not?

We support the IASB's approach. However, we encourage the IASB to extend the scope of the interim Standard to all rate-regulated entities to recognize regulatory deferral account balances in IFRS financial statements for increased transparency, comparability, consistency, and relevancy of the information to the users of the financial statements. We note that this is especially important when the comprehensive Rate-regulated Activities project is completed.

Question 2

The Exposure Draft proposes two criteria that must be met for regulatory deferral accounts to be within the scope of the proposed interim Standard. These criteria require that:

- ***(a) an authorised body (the rate regulator) restricts the price that the entity can charge its customers for the goods or services that the entity provides, and that price binds the customers; and***
- ***(b) the price established by regulation (the rate) is designed to recover the entity's allowable costs of providing the regulated goods or services (see paragraphs 7 -8 and BC33-BC34).***

Are the scope criteria for regulatory deferral accounts appropriate? Why or why not?

We agree with the scope criteria for regulatory deferral accounts.

Question 3

The Exposure Draft proposes that if an entity is eligible to adopt the [draft] interim Standard it is permitted, but not required, to apply it. If an eligible entity chooses to apply it, the entity must apply the requirements to all of the rate-regulated activities and resulting regulatory deferral account balances within the scope. If an eligible entity chooses not to adopt the [draft] interim Standard, it would derecognise any regulatory deferral account balances that would not be permitted to be recognised in accordance with other Standards and the Conceptual Framework (see paragraphs 6, BC11 and BC49).

Do you agree that adoption of the [draft] interim Standard should be optional for entities within its scope? If not, why not?

We support the IASB's approach. However, we encourage the IASB to require all rate-regulated entities to apply the requirements to all of the rate-regulated activities and resulting regulatory deferral account balances within the scope for increased consistency, transparency, and comparability. This is an important consideration as our assessment is it is more likely than not that rate-regulated utilities in

Canada will choose to adopt the proposed interim Standard and continue to recognize regulated assets and liabilities.

Question 4

The Exposure Draft proposes to permit an entity within its scope to continue to apply its previous GAAP accounting policies for the recognition, measurement and impairment of regulatory deferral account balances. An entity that has rate-regulated activities but does not, immediately prior to the application of this [draft] interim Standard, recognise regulatory deferral account balances shall not start to do so (see paragraphs 14–15 and BC47–BC48).

Do you agree that entities that currently do not recognise regulatory deferral account balances should not be permitted to start to do so? If not, why not?

We agree that entities that have not adopted IFRS and currently do not recognize regulatory deferral balances should not be permitted to start to do so. This is important given the proposed Standard is intended to be applicable only as a short-term interim solution until the comprehensive Rate-regulated Activities project is completed.

Question 5

The Exposure Draft proposes that, in the absence of any specific exemption or exception contained within the [draft] interim Standard, other Standards shall apply to regulatory deferral account balances in the same way as they apply to assets and liabilities that are recognised in accordance with other Standards (see paragraphs 16–17, Appendix B and paragraph BC51).

Is the approach to the general application of other Standards to the regulatory deferral account balances appropriate? Why or why not?

Yes, we agree with the IASB's approach.

Question 6

***The Exposure Draft proposes that an entity should apply the requirements of all other Standards before applying the requirements of this [draft] interim Standard. In addition, the Exposure Draft proposes that the incremental amounts that are recognised as regulatory deferral account balances and movements in those balances should then be isolated by presenting them separately from the assets, liabilities, income and expenses that are recognised in accordance with other Standards (see paragraphs 6,
18–21 and BC55–BC62).***

Is this separate presentation approach appropriate? Why or why not?

Yes, we agree with the IASB's approach.

Question 7

The Exposure Draft proposes disclosure requirements to enable users of financial statements to understand the nature and financial effects of rate regulation on the entity's activities and to identify

and explain the amounts of the regulatory deferral account balances that are recognised in the financial statements (see paragraphs 22–33 and BC65).

Do the proposed disclosure requirements provide decision-useful information? Why or why not? Please identify any disclosure requirements that you think should be removed from, or added to, the [draft] interim Standard.

Yes, we agree with the IASB's approach.

Question 8

The Exposure Draft explicitly refers to materiality and other factors that an entity should consider when deciding how to meet the proposed disclosure requirements (see paragraphs 22–24 and BC63–BC64).

Is this approach appropriate? Why or why not?

Yes, we agree with the IASB's approach.

Question 9

The Exposure Draft does not propose any specific transition requirements because it will initially be applied at the same time as IFRS 1, which sets out the transition requirements and relief available.

Is the transition approach appropriate? Why or why not?

Yes, we agree with the IASB's approach.

Question 10

Do you have any other comments on the proposals in the Exposure Draft?

Canada's adoption of IFRS for publicly accountable enterprises has led to a wide diversity and inconsistency of practices in terms of the financial accounting and regulatory accounting frameworks among Canadian rate-regulated entities. The non-recognition of regulatory assets and liabilities under IFRS has been a significant barrier to the adoption of IFRS by the majority of Canadian utilities. The effective date for adoption of IFRS in Canada was January 1, 2011. However, four extensions to the mandatory IFRS adoption have been granted by the Canadian Accounting Standards Board (AcSB) to rate-regulated entities. The current extension date granted for mandatory changeover to the IFRS is as at January 1, 2015. To date, less than 10% of rate-regulated utilities in Canada have adopted IFRS. Most rate-regulated utilities have remained under current Canadian GAAP. There are certain rate-regulated entities that have been granted approval by their rate regulators to use US GAAP for regulatory rate-making and reporting purposes. These entities have received permission to use US GAAP for financial reporting purposes effective January 1, 2012 through to December 31, 2014. It is likely that most these utilities would seek to remain under US GAAP if regulatory assets and liabilities are not approved by the IASB. Furthermore, there are a number of large Canadian electricity utilities that are owned by provincial governments and are required to use US GAAP effective January 1, 2012 through regulations that were issued by these governments.

IFRS may not be required by the AcSB or the Canadian Public Sector Accounting Board (PSAB) for rate-regulated enterprises for whom some other standard may apply. For example, private enterprises that are not owned by the government and not listed on a public exchange may choose to use Accounting Standards for Private Enterprises (ASPE), which is similar to the old Canadian GAAP, for financial reporting purposes. An Ontario utility has received approval by the OEB to use ASPE for regulatory rate-making and reporting purposes. Its parent company operating in another province has received approval from its regulator to use US GAAP. This has led to reduced comparability among rate-regulated utilities for users of financial statements. The transition to IFRS in Canada has led to divergence in practices with respect to rate-making, regulatory accounting, and financial reporting among Canadian rate-regulated entities. We believe that the interim Standard will help reduce this divergence and facilitate future convergence and comparability among rate-regulated entities, including benchmarking, consistent reporting, etc. This will ultimately help rate regulators better serve the public interest and benefit all users of the general financial statements.

In its Exposure Draft, IASB has acknowledged that "in recent years there has been a trend among rate regulators towards applying incentive-based regulatory methodologies, such as so-called 'price-cap' regulation"[18] or "hybrid methodologies that are combinations of price-cap and cost-of-service approaches".[19] We would like to emphasize that the operation as well as regulatory accounting treatment and reporting of the regulatory deferral accounts are not affected by the methods used by rate regulators for establishing rates. This is due to the fact that it is still highly likely that the governments' policies and rate regulators' actions and initiatives may cause differences between the accounting treatment of a transaction or event for rate-setting purposes and its accounting treatment under IFRS (e.g., regulatory deferral accounts established for investment in renewable generation, smart grids, asset management, storm costs, etc.). The revenues and costs associated with these initiatives are subject to prudency review and approval of the rate regulators. Therefore, an interim Standard will still be required under all rate-regulatory regimes that regulators will use for setting just and reasonable rates. Furthermore, the application of interim Standard during any rate regulation regimen will help the transparency, comparability, and the relevancy of the information to the users of the financial statements.

[18] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC25, page 33.
[19] Exposure Draft – ED/2013/5, Regulatory Deferral Accounts, paragraph BC25, page 33.