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The International Accounting Standards Board
30 Cannon Street
London, UK
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To Whom It May Concern,

Exposure Draft – ED/2013/5 – Regulatory Deferral Accounts

The Halifax Regional Water Commission (Halifax Water) is the first and only regulated water, wastewater, and stormwater utility in Canada. The issues affecting natural gas and electric utilities with respect to conversion to IFRS also affect municipal government business enterprises that are regulated utilities delivering some of or all of water, wastewater and stormwater services. For such government business enterprises, financial statements prepared in IFRS are a requirement for consolidation with the municipal governments which follow Public Sector Accounting Board (PSAB) standards. The prospect of potentially having to maintain a set of financial statements for regulatory purposes, and a set of financial statements in IFRS for consolidation purposes, imposes significant additional effort and cost and creates potential confusion for financial statement users.

In general, the recommendations found in the Exposure Draft will enhance the comparability of financial reporting by reducing barriers to first time adoption of IFRS by rate-regulated entities. It is a positive first step, until a financial accounting standard is developed through the Rate-Regulated Activities project.

Although Halifax Water's present structure has existed since 1945, its creation was related to earlier events. As with any growing metropolis throughout the last century, the former City of Halifax had struggled to meet the ever-increasing demands of its residents for clean, safe drinking water. In 1861, after serious degradation, the water supply system was purchased by the City from a private company and operated in one form or another for 75 years, without ever resolving its maintenance and wastage problems.

Ravaged by two World Wars and the Great Depression, by 1943, Halifax's water supply had deteriorated to a critical condition. Responding to a government-commissioned report on the need for a complete overhaul of the system, the City, on January 1, 1945, formed the Public Service Commission (renamed the Halifax Regional Water Commission in 1987) to operate and manage the water utility.

Eight years later, in 1952, Halifax Water purchased the assets of the water utility outright from the City to ensure that the utility operated in a business-like manner. This business-like approach has enabled Halifax Water to continually improve and upgrade the water supply system by funding operational and capital expenditures directly from utility charges, without any financial assistance from the municipal government. On April 1, 1996, as a result of metro amalgamation, the Dartmouth and Halifax County water utilities were merged with Halifax Water, bringing with it new challenges and opportunities.

On August 1, 2007, the Commission expanded its mandate once again with the transfer of wastewater and stormwater assets to Halifax Water from the municipality, and becoming the first regulated water and wastewater/stormwater utility in Canada.

With wastewater and stormwater governance established under the purview of the Nova Scotia Utility and Review Board (NSUARB), the focus of Halifax Water is to improve asset management, secure stable funding, and meet Provincial and Federal regulatory requirements. The merger is viewed as an excellent opportunity to deliver water, wastewater and stormwater services in an integrated, cost effective, and environmentally sound manner.

Halifax Water is regulated by the Nova Scotia Utility and Review Board (NSUARB), and meets the definition of a rate-regulated entity as defined by CICA 1300. Currently, the utility’s financial statements are prepared based on the financial reporting provisions of the Accounting and Reporting Handbook for Water Utilities issued by the NSUARB, which deviates in some instances from Canadian GAAP, and are prepared for the special purpose of the regulator. A reconciliation of the special purpose financial statements to PSAB (Public Sector Accounting Board Standards) is prepared to enable consolidation of Halifax Water’s financial statements with the Halifax Regional Municipality (HRM).

The following specific feedback is provided to Exposure Draft ED/2013/5 – Regulatory Deferral Accounts:

Question 1 – The Exposure Draft proposes to restrict the scope to those first-time adopters of IFRS that recognize regulatory deferral account balances in their financial statements in accordance with their previous GAAP.

Is the Scope restriction appropriate? Why or why not?

Response: The scope restriction is appropriate, however should recognize that there may be utilities converting to IFRS from a previous method that may differ from GAAP, thus resulting in some additional regulatory deferrals. For example, the Halifax Regional Water Commission currently has a regulatory deferral account balance – a regulatory asset associated with deferred depreciation, which the regulator has approved. The deferred depreciation is being amortized over the remaining useful life of the assets and is included in the revenue requirements approved by the regulator.

There are other areas of difference between the utility's financial information for regulatory purposes and GAAP, which upon conversion to IFRS may give rise to regulatory deferrals, subject to the approach of the regulator. For example, Pension expense is recorded in the utility's financial statements on an accrued basis, but is recognized within the rates on a cash basis. Upon conversion to IFRS, a regulatory deferral account (asset) would result. Similarly, some debt servicing costs associated with pre-financing of assets are recorded on an accrual basis in the utility's financial statements, and deferred from a regulatory perspective until the asset comes into service, potentially giving rise to a regulatory asset upon conversion to IFRS.

Future events or regulatory direction may give rise to additional regulatory deferral accounts. The necessity to produce two sets of financial statements, one for audit and consolidation purposes in accordance with IFRS, and the other in accordance with regulatory requirements causes additional administrative costs, and potential confusion for financial statements users as there would be significant differences between the two sets of financial statements. The primary financial statement users are the regulator and the stakeholders who participate in public regulatory proceedings where the audited financial statements are relied upon to demonstrate revenue requirements, and the financial position and viability of the utility.

Having all of the differences between IFRS and utility accounting and reporting handbook requirements reflect as regulatory deferral accounts will enhance the financial statement users' ability to identify and understand the differences.

Question 2 – The Exposure Draft proposes two criteria that must be met for regulatory deferral accounts to be within scope of the proposed interim Standard. These criteria require that:

a) an authorized 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?

Response: The scope criteria for regulatory deferral accounts are entirely appropriate as it recognizes that only the decisions/directions of the authorized body (the rate regulator) give rise to regulatory deferral accounts. Similarities in the rate regulation process, cost of service based rate making in particular, will promote consistency and comparability from a reporting perspective amongst rate–regulated entities.

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 derecognize any regulatory deferral account balances that would not be permitted to be recognized in accordance with other Standards and the *Conceptual Framework* (see paragraphs 6, BC11 and BC 49)

Do you agree that adoption of the (draft) interim Standards should be optional for entities within its scope? If not, why not?

Response:

Adoption of the (draft) interim Standards should be optional for entities within its scope, given the broad range, nature and variety of entities that are rate-regulated and are within scope. There are some entities (such as Halifax Water) that do not have comparable organizations, thus comparability of financial statements is not a major concern and election to adopt the (draft) interim Standard should be made based on specific circumstances of the rate-regulated entity.

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, recognize 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 recognize regulatory deferral account balances should not be permitted to start to do so? If not, why not?

Response: Utilities and regulators utilize regulatory deferral account balances as an important tool for rate-smoothing and to develop cost-of-service based rates that reflect inter-generational equity. I believe that utilities that currently do not recognize regulatory deferral account balances should not be restricted from doing so in future. With proper recording and disclosure to financial statement users, regulatory deferral account balances do not result in financial statements which are less useful to users. Continued permitted use of regulatory deferral account balances will ensure continued transparency and understandability with regulators and participants in regulatory proceedings and will reduce differences between audited financial statements and information used for rate-setting purposes.

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 recognized 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?

Response: Yes. If a regulatory asset or liability is recognized, it should be subject to the other Standards thus reducing additional differences between the IFRS financial statements of rate-regulated entities and other entities.

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 recognized 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 recognized in accordance with other Standards (see paragraphs 6, 18-21 and BC55-BC62).

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

Response: Yes, the separate presentation approach is appropriate. It provides additional transparency and will be beneficial to regulators to track compliance with regulatory direction/approvals with respect to regulatory deferral accounts.

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 recognized in the financial statements (see paragraphs 22-23 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.

Response: Yes, the proposed disclosure requirements provide decision-useful information, as it will ensure that all the financial effects of rate-regulation (for each rate-regulated service) can be easily discerned in one spot by financial statement users.

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?

Response: This approach is appropriate, because there is nothing to preclude a rate-regulated entity from utilizing a threshold of materiality for reporting purposes that is lower than what normal standards would dictate. For example, transactions regarding regulatory deferral accounts may not be material within the overall context of the entity as a whole, but there may be specific reasons why a utility may want to record and disclose transactions regarding regulatory deferral accounts at a more refined level of detail; particularly if it assists in demonstrating regulatory compliance.

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 this transition approach appropriate? Why or why not?

Response: Yes, this transition approach is appropriate; however it is very important to finalize comprehensive Standards for rate-regulated entities.

Question 10 – Do you have any other comments on the proposals in the Exposure Draft?

Response: No

Thank-you for the opportunity to provide comments.

Yours truly,

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Halifax Regional Water Commission