

STAFF PAPER

July 2019

IASB[®] Meeting

Project	Rate-regulated Activities		
Paper topic	The consultation document—an exposure draft or a discussion paper		
CONTACT(S)	Umair Shahid	ushahid@ifrs.org	+44 (0)20 7246 6414
	Mariela Isern	misern@ifrs.org	+44 (0)20 7246 6483
	Neal Beauchamp	nbeauchamp@ifrs.org	+44 (0)20 7246 6423
	Jane Pike	jpike@ifrs.org	+44 (0)20 7246 6925

This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (Board) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS[®] Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB[®] Update.

Purpose of this paper

1. The purpose of this paper is to ask the Board whether it plans to publish an exposure draft or a discussion paper as the next consultation document to obtain feedback on the accounting model for regulatory assets and regulatory liabilities (the model).

Staff recommendation

2. The staff recommend that the Board publish an exposure draft rather than a discussion paper.

Structure of the paper

3. This paper is structured as follows:
 - (a) background (paragraphs 4–11);
 - (b) selecting the appropriate type of consultation document (paragraphs 12–16);
 - (c) next steps (paragraphs 17–18);

- (d) Appendix A—extracts from the *Due Process Handbook*; and
- (e) Appendix B—analysis of factors to consider in selecting the appropriate type of formal consultation document for the Rate-regulated Activities project.

Background

4. Paragraph 5.5 of the [Due Process Handbook](#) (the Handbook) states that:
 - 5.5 ... The IASB would normally put together a proposal to develop a new Standard or to make major amendments to a Standard only after it has published a Discussion Paper and considered the comments it received from that consultation. Publishing a Discussion Paper before adding a standards-level project to its agenda is not a requirement, but the IASB must be satisfied that it has sufficient information and understands the problem and the potential solutions well enough to proceed without a Discussion Paper. The IASB might conclude that a Discussion Paper is not necessary because it has sufficient input from a research paper, Request for Information or other research to proceed directly to an Exposure Draft. The reasons for not publishing a Discussion Paper need to be set out by the IASB and reported to the [Due Process Oversight Committee].
5. Paragraph 6.1 of the Handbook explains that an exposure draft is a mandatory step in the due process before a Standard is issued or amended.
6. Appendix A includes extracts from the Handbook relating to the content of discussion papers and exposure drafts.
7. The Rate-regulated Activities project (the project) was added to the Board's agenda in December 2008 because of ongoing differences of views in practice about whether it was appropriate for entities to recognise assets and liabilities arising from rate regulation and ongoing requests for guidance on this issue. Since then the project has gone through various phases and various consultative documents have been published (see Table 1).

Table 1		
Timeline	Event or public consultation document	Comments
July 2009	Publication of Exposure Draft <i>Rate-regulated Activities</i> (the '2009 ED') ¹	<p>The Board's objectives for the 2009 ED were:</p> <ul style="list-style-type: none"> (a) to establish criteria for the recognition of assets and liabilities arising from rate regulation; (b) to clarify that regulated entities follow the requirements of all other IFRS Standards in addition to the proposed Standard; and (c) to require disclosures to enable users to understand the nature and financial effects of rate regulation on an entity's activities. <p>The 2009 ED focused on a particular type of rate-regulatory scheme (a cost-of-service scheme).</p> <p>Respondents to the 2009 ED expressed divergent views as to how the consequences of rate regulation should be reflected in the financial statements, if at all.</p> <p>Many suggested that the scope of the project should be expanded to look at a wider variety of rate regulation in order to identify common characteristics from which accounting guidance might be developed.²</p>
Sept 2010	Project suspended	<p>The Board reconfirmed that addressing rate-regulated activities could not be resolved quickly. The Board decided to include in its public consultation on its future agenda a request for views on what form a future project might take, if any, to address rate-regulated activities.</p>

¹ The 2009 ED can be found: <http://archive.ifrs.org/Rate-regulated-activities/Exposure-draft-and-Comment-Letters/Pages/Exposure-draft-and-Comment-Letters.aspx>

² The comment letters summary of the 2009 ED can be found: http://archive.ifrs.org/Rate-regulated-activities/Meeting-Summaries-and-Observer-Notes/Documents/RRA0210b07_Revised5Feb2010.pdf

Table 1		
Timeline	Event or public consultation document	Comments
May 2012	2011 Agenda consultation	At its May 2012 meeting, on the basis of the messages received in response to the Request for Views <i>Agenda Consultation 2011</i> , the Board supported developing standards-level proposals for rate-regulated activities.
September 2012	Project restarted	At its September 2012 meeting, the Board decided to restart the project.
Mar 2013	Publication of Request for Information (RfI) ³	<p>The objective of the RfI was to identify a range of rate-regulatory schemes to help determine the scope of the research project.</p> <p>The RfI asked specific questions about the objectives of rate regulation and how those objectives were reflected in the rate-setting mechanisms employed by rate regulators.</p> <p>The fact patterns identified through the RfI and other research were aimed to be used to develop a Discussion Paper that would analyse the common features of rate regulation.</p> <p>The Board analysed the responses received in July 2013.⁴</p>

³ The RfI can be found: <http://archive.ifrs.org/Rate-regulated-activities/Request-for-information-March-2013/Pages/Request-for-Information-and-comment-letters.aspx>

⁴ Agenda Paper 9 discussed at the July 2013 Board meeting can be found: <http://archive.ifrs.org/Meetings/MeetingDocs/IASB/2013/July/09-Rate-regulated%20Activities-Rate%20Regulation.pdf>

Table 1		
Timeline	Event or public consultation document	Comments
Sept 2014	Publication of Discussion Paper <i>Reporting the Financial Effects of Rate Regulation</i> (the '2014 DP') ⁵	<p>The 2014 DP described a type of rate regulation that contains elements of both cost recovery and incentive approaches—this type of rate regulation is termed <i>defined rate regulation</i>.</p> <p>The 2014 DP sought comments on whether or not the distinguishing features of defined rate regulation, as identified by the Board, sufficiently captured the type(s) of rate regulation that have the most significant financial effects.</p> <p>The 2014 DP did not include any specific accounting proposals. Instead, it explored what information about rate-regulated activities is most useful to users of financial statements and outlined possible approaches (and the accompanying advantages and disadvantages) that the Board could consider in deciding how best to report the financial effects of rate regulation.</p> <p>The Board analysed the responses received in February 2015.⁶</p>

⁵ The 2014 DP can be found: <http://archive.ifrs.org/Current-Projects/IASB-Projects/Rate-regulated-activities/Discussion-Paper-September-2014/Pages/Discussion-Paper-and-Comment-letters.aspx>

⁶ Agenda Paper 9 discussed at the February 2015 Board meeting can be found: <http://archive.ifrs.org/Meetings/MeetingDocs/IASB/2015/February/AP09-Rate-regulated%20Activities.pdf>

8. As stated in Table 1, in February 2015, the Board reviewed the feedback received on the 2014 DP through outreach and comment letters. The main messages received were as follows:
- (a) many respondents suggested that the combination of rights and obligations created by defined rate regulation creates unique or distinguishable economic conditions that are not faithfully represented by the existing predominant practice in IFRS financial statements. As a result, we heard that users of financial statements need to rely on non-GAAP information obtained from a variety of sources outside the audited financial statements, which they were concerned typically lacks comparability. Although some users are content with this situation, others would prefer to obtain the information in a more accessible and comparable format within audited IFRS financial statements. However, there was limited support for the Board to develop disclosure-only requirements.
 - (b) many respondents suggested that the scope of any future IFRS requirements should focus on the rights and obligations and how they relate to the basis for setting the regulated rates.
 - (c) there was strong support for developing principle-based, specific accounting requirements that will lead to the recognition of at least some regulatory deferral account balances in IFRS financial statements. The strongest support was for an approach based on principles-based IFRS requirements using a revenue-focussed approach.
9. In May 2015 the Board decided to move the project from the Research programme to the Standards-level programme.⁷ In the same meeting, the Board was informed that although the 2014 DP achieved its objectives, there were complexities in the interactions between the project and the *Conceptual Framework* and IFRS 15 *Revenue from Contracts with Customers*. At that time, it was believed that these issues could be explained and explored more thoroughly and effectively through a second

⁷ [Agenda Paper 9A](#) discussed at the May 2015 Board meeting.

discussion paper rather than an exposure draft. All Board members tentatively agreed that development of a second discussion paper would be the fastest way to progress the project.

10. Since then the staff has continued working on the development of an accounting model for defined rate regulation (the model). The publication of the *Conceptual Framework for Financial Reporting* (the *Conceptual Framework*) in March 2018 enabled the model to progress considerably during 2018 as it provided the Board with a stable base to use when making decisions on some of the core aspects of the model. The Board has discussed staff proposals on various aspects of the model and has reached a comprehensive set of tentative decisions. As a result, during 2018 the staff stated that once the model was developed it would ask the Board whether to publish an exposure draft or a second discussion paper as the next consultation document for the project.
11. We have not sought formal feedback from stakeholders on whether to publish a discussion paper or an exposure draft. However, at their April 2018 meeting, some members of the Accounting Standards Advisory Forum (ASAF) expressed their support for developing an exposure draft as the next consultation document whereas some other members expressed support for a second discussion paper.⁸

Selecting the appropriate type of formal consultation document

12. In the February 2018 Board meeting, the staff presented Agenda Paper 28, which discusses the differing purposes of and requirements for discussion papers and exposure drafts. It also provides the following factors to consider in selecting the appropriate type of formal consultation document:⁹
 - (a) the need for formal consultation;
 - (b) the stage of development;
 - (c) the significance of proposed changes;
 - (d) the effect on timelines; and
 - (e) the risk of re-exposure.

⁸ [Summary note](#) of Accounting Standards Advisory Forum (ASAF) meeting held in April 2018.

⁹ [Agenda Paper 28](#) discussed at the February 2018 Board meeting.

13. The staff think there is general agreement among Board members and stakeholders that the Board should publish a formal consultation document for this project (ie the factor described in paragraph 12(a)). Consequently, we do not discuss this factor further in this paper.
14. To determine whether to publish a discussion paper or an exposure draft, the Board should consider holistically the four factors listed in paragraphs 12(b)–(e). Appendix B provides detailed analysis of each of these four factors with respect to the Rate-regulated Activities project to support our recommendation in paragraph 15. In the staff’s view, the following considerations are particularly important:
- (a) users’ demand for this project is strong (see paragraphs B16(a) in Appendix B and AP9E *Effect analysis*). The project’s objective is to address users’ long-standing concerns and information requirements. It is preferable to respond to users’ needs without unnecessary delay.
 - (b) users support the overall direction of the project (see paragraph B12(c) in Appendix B and AP 9E *Effect analysis*). This implies there is a need for improved information about the effects of defined rate regulation in entities’ financial statements that, in our view, the proposals in this project would address.
 - (c) the problem is well defined and the proposals are sufficiently detailed for publication of an exposure draft (see paragraphs B5–B7 in Appendix B).
 - (d) drafting is critical for key concepts included in the proposals (see paragraph B13 in Appendix B). It would be more effective to test drafting in the form of an exposure draft rather than in the form of a discussion paper.
15. Accordingly, based on the feedback on the 2014 DP, evidence gathered subsequently, outreach conducted till date and the level of development of the proposals, we recommend the Board publishes an **exposure draft**.¹⁰ We are of the view that the Board has:

¹⁰ See Appendix C in Agenda Paper 9F *Due process and permission to begin the balloting process*.

- (a) gathered sufficient information from the various consultation documents (Table 1) and outreach with stakeholders and understands the problem and potential solutions well enough to proceed directly to an exposure draft without a second discussion paper;
 - (b) duly considered alternative approaches and the feedback of stakeholders when establishing the scope of the project; and
 - (c) set out its view and developed specific requirements for accounting for activities that are subject to defined rate regulation. An exposure draft would be seeking feedback on the specific proposed requirements of the model.
16. Also, the staff think it would be more effective and efficient to publish an **exposure draft**, considering the factors discussed in this paper in Appendix B.

Question for the Board

Consultation document

1. Does the Board agree with the staff recommendation that the Board publish an exposure draft rather than a second discussion paper?

Next steps

17. Agenda Paper 9F *Due process and permission to begin the balloting process* asks the Board for permission to begin the balloting process.
18. If the Board decides to publish an exposure draft, we will need to consider whether to present the proposals as amendments to IFRS 14 *Regulatory Deferral Accounts* and/or existing IFRS Standards or as a new IFRS Standard. The staff prefer **withdrawing IFRS 14 and developing a new Standard** as a result of this project because:
- (a) IFRS 14 has always been presented as an interim Standard that permitted entities within its scope to continue to account for regulatory deferral account balances in their financial statements in accordance with their previous GAAP and helped them avoid making a major change to their

accounting policies for those balances until the comprehensive Rate-regulated Activities project is completed.

- (b) the proposed model will introduce specific principles-based requirements to account for and provide information about incremental rights and incremental obligations created by defined rate regulation that are not captured by existing IFRS Standards. Because these requirements are largely unrelated to existing requirements in IFRS 14, labelling them as amendments to IFRS 14 may mislead stakeholders.
- (c) incorporating the requirements of the model by amending existing IFRS Standards would most probably hinder stakeholders from gaining a holistic understanding of the principles and requirements of the model which may create challenges in their implementation of the model.

Question for the Board

Next steps

2. Does the Board have any questions or comments on the proposed next steps (ie withdrawing IFRS 14 and developing a new Standard)?

Appendix A—Extracts from the *Due Process Handbook*

A1. Paragraphs 4.12–4.13 of the *Due Process Handbook* state that:

4.12 The main output of the research programme is expected to be Discussion Papers and research papers. Discussion Papers and research papers are designed to elicit comments from interested parties that can help the IASB decide whether to add a project to its standard-setting programme. Discussion and research papers typically include a comprehensive overview of the issue, possible approaches to addressing the issue, the preliminary views of its authors or the IASB and an invitation to comment.

4.13 Discussion Papers are issued by the IASB and present the analysis and collective views of the IASB on a particular topic. The matters presented will have been discussed in public meetings of the IASB. Discussion Papers do not contain a Basis for Conclusions or any dissenting opinions. The discussion itself should reflect and convey differences in views of the IASB members.

A2. Paragraphs 6.1–6.3 of the *Due Process Handbook* state that:

6.1 Publication of an Exposure Draft is a mandatory step in the due process before a new Standard can be issued or an existing Standard can be amended.

6.2 An Exposure Draft sets out a specific proposal in the form of a proposed Standard (or amendment to a Standard) and is therefore generally set out in the same way as, and has all of the components of, a Standard. The main differences are that the:

(a) Basis for Conclusions is written to explain the IASB's rationale for the proposal, and is not a draft of the rationale for the final Standard or final amendments to the Standard; and

(b) consequential amendments need not be set out in as much detail as they would be in a final Standard, particularly where such amendments are changes to cross-references or terminology and other matters that are more administrative in nature.

- 6.3 An Exposure Draft is the IASB's main vehicle for consulting the public and therefore includes an invitation to comment, setting out the issues that the IASB has identified as being of particular interest. Although it is normally included with the ballot draft, it is not necessary for the IASB to ballot the invitation to comment.

Appendix B—Analysis of factors to consider in selecting the appropriate type of formal consultation document for the Rate-regulated Activities project

- B1. AP28 discussed at the February 2018 Board meeting presents the following factors to consider in selecting the appropriate type of formal consultation document:
- (a) the stage of development;
 - (b) the significance of proposed changes;
 - (c) the effect on timelines; and
 - (d) the risk of re-exposure.
- B2. The following paragraphs analyse those factors with respect to the Rate-regulated Activities project.

The stage of development

- B3. As set out in AP28 for the February 2018 Board meeting, a project typically has the following phases:
- (a) the idea generation phase—the Board defines the problem and the scope of the project and considers possible approaches to address the issue. A discussion paper conveys information about and seeks feedback on the possible approaches.
 - (b) the idea implementation phase—the Board will have selected an approach and sets out its view of what the accounting requirements should be. An exposure draft seeks feedback on specific proposed requirements.
 - (c) the refinement phase—the Board considers how to modify the proposed requirements in the light of feedback. This typically occurs after the Board has published an exposure draft and is not discussed further in this paper.
- B4. To help assess the phase of the project we have considered the following questions:
- (a) is the problem defined and the scope decided?
 - (b) has the Board decided on a preferred approach and is the proposed solution detailed?
 - (c) has the Board considered feedback and evidence?

Is the problem defined and the scope decided?

- B5. The Board has discussed the problem definition and the scope of the project at various meetings.¹¹ AP9E *Effect analysis* includes a description of the problem and includes the scope of the project in Table 1 of its Appendix.
- B6. The decisions on the scope of the model were informed by the feedback on the 2014 DP and subsequent discussions with the stakeholders, including those with the members of the Consultative Group for Rate Regulation (CGRR).¹²

Has the Board decided on a preferred approach and is the proposed solution detailed?

- B7. In the staff's view, the Board's proposals have been developed in sufficient detail for publication of an exposure draft and the Board has provided suggestions for staff to consider when drafting.

Has the Board considered feedback and evidence?

- B8. The Board has considered feedback and evidence in defining the problem, identifying potential solutions and developing proposals.¹³ The Board:
- (a) considered feedback for identifying and developing potential solutions to the problems identified, including feedback obtained from:
 - (i) consultation through the Discussion Paper [Reporting the Financial Effects of Rate Regulation](#) published in 2014; and
 - (ii) outreach with stakeholders through more than 20 public and non-public meetings;
 - (b) discussed proposals with the Board's consultative groups and advisory bodies in more than 15 meetings; and
 - (c) considered the results of the following research:

¹¹ Agenda Paper 9A discussed with the Board in [May 2019](#) and [June 2019](#) include a description of the problem and [Agenda Paper 9B](#) discussed with the Board in June 2019 includes the scope of the model.

¹² [Summary of information received from the Consultative Group for Rate Regulation \(CGRR\), December 2017.](#)

¹³ See Appendix C in Agenda Paper 9F *Due process and permission to begin the balloting process* for a list of public meetings and non-public meetings and outreach events held for this project.

- (i) a desk review of selected academic literature and reports and guidance published by other organisations;
- (ii) a desk review of the research on decision-usefulness of financial information that reflects economics of rate-regulated activities published by the Canadian Accounting Standards Board (AcSB) in September 2016 and November 2018.

Overall assessment of the stage of development

B9. Based on the discussion above, the staff assess that this project is in the idea implementation phase, thus it is appropriate to publish an **exposure draft**.

The significance of proposed changes

B10. Paragraphs 30–33 in [AP28](#) for the February 2018 Board meeting discuss how the significance of proposed changes could affect the type of consultation document published. *AP9E Effect analysis* provide a summary of the likely effects of the model in entities' financial statements.

B11. On the basis of that analysis we think the proposals in this project would result in significant changes for entities that currently do not recognise regulatory balances in their financial statements, with changes being less significant for entities that currently do recognise regulatory items in their financial statements.

B12. We think the following factors would suggest a second discussion paper may not be necessary and the Board could move straight to an **exposure draft**:

- (a) the Board has developed a single approach to each aspect of the model rather than developing alternative approaches.
- (b) as discussed in paragraph B8, the Board has conducted extensive outreach throughout the project. Feedback from outreach suggests that many of the project proposals are supported by the stakeholders.
- (c) we have heard generally positive feedback on the direction of the project. Many aspects of the model, including the key proposals for scope, recognition, measurement, presentation and disclosure are generally supported across stakeholder groups. User feedback on disclosure

objective and disclosure requirements informed the proposals for the model.¹⁴

- (d) while the changes arising from application of the model are significant as discussed in paragraph B11, in our view many of the outcomes of the model are likely to be similar for those entities that currently recognise regulatory assets and regulatory liabilities, however the underlying thought process and principles underpinning the requirements will likely be significantly different. Also, we expect that implementation of the model will not be onerous because:
- (i) most of the information required to apply the model should already be available (because of the detailed record-keeping requirements in regulatory agreements); and
 - (ii) and the proposed requirements have been developed considering operational aspects.

AP9E *Effect analysis* provides a summary of the likely effects of the model in entities' financial statements.

- B13. In addition, for many of the project proposals, drafting is critical (for example, the proposed scope and definitions of regulatory assets and regulatory liabilities). As discussed in [AP28](#) for the February 2018 Board meeting, an exposure draft is more effective than a discussion paper for proposals in which drafting is critical, for example in defining new terms.
- B14. In considering the significance of the change, the staff note that:
- (a) while the proposals would cause significant change, users have been requesting this change for a long time and initial indications are that the proposals will be well received; and
 - (b) while there could be divergent views relating to some aspects of the model, we think such views would not affect the core aspects of the proposed model.
- B15. Consequently, the staff assess that an **exposure draft** may be appropriate.

¹⁴ [Capital Markets Advisory Committee \(CMAC\) meeting summary](#) March 2018.

The effect on timelines

- B16. The staff think it is important that this project is completed without unnecessary delay. Delays in completing the project:
- (a) will cause delays in addressing users' needs. For many years, users have expressed the need for information that would help them understand the consequences of rate regulation on an entity's financial position and financial performance.
 - (b) will further delay issuance of a final standard for rate-regulated activities considering the fact that the Board issued IFRS 14 as an interim standard that was intended to be a practical and short-term solution to address a significant barrier to the adoption of IFRS in some jurisdictions.¹⁴ Also, in response to the Board's 2015 Agenda Consultation, stakeholders strongly called for the completion of the remaining major projects, including this project.¹⁵
 - (c) may result in stakeholders becoming disengaged from the project. Solving users' most pressing performance reporting problems quickly would help maintain the project's momentum and a high level of stakeholder engagement.
 - (d) can create operational difficulties, through lack of continuity of staff and Board members. At least five of the current 14 Board members will leave the Board by June 2021. Two of the current 14 Board members have joined the Board in July 2019.
- B17. Although the timetable is tight, the staff think that publication of a consultation document—a discussion paper or an exposure draft—is possible by the first half of 2020. Assuming there is no re-exposure, publishing an exposure draft as the consultation document would enable the improvements proposed in this project to be implemented two to three years earlier than if a discussion paper were published.

¹⁴ Paragraphs BC8 and BC10 of the Basis for Conclusions of IFRS 14 *Regulatory Deferral Accounts*.

¹⁵ [Feedback Statement](#) 2015 Agenda Consultation.

Would there be benefits in dividing the project to allow some parts to be finalised sooner?

B18. The Board could consult on those parts of the project on which stakeholders' views diverge separately from the other project proposals. However, till date we have not heard of any critical aspect of the model for which stakeholders have strong diverging views that would warrant the Board to consider dividing the process to allow some parts to be finalised sooner.

The risk of re-exposure

B19. In considering whether there is a need for re-exposure before finalising the project, the Board:¹⁶

- (a) identifies substantial issues that emerged during the comment period on the exposure draft and that it had not previously considered;
- (b) assesses the evidence that it has considered;
- (c) determines whether it has sufficiently understood the issues, implications and likely effects of the new requirements and actively sought the views of interested parties; and
- (d) considers whether the various viewpoints were appropriately aired in the exposure draft and adequately discussed and reviewed in the basis for conclusions.

B20. Based on the analysis in this paper (see paragraphs B5–B14), the staff think that although we can never rule out the risk of re-exposure, the Board could publish an **exposure draft**.

B21. Even if followed by another exposure draft, publishing an exposure draft as the next step would enable the improvements proposed in this project to be implemented sooner than if the Board published a discussion paper. This is because a second exposure draft is usually narrower in scope and thus takes less time to prepare, respond to and analyse. It is important to note, however, that the Board's ability to respond to feedback can be more limited after an exposure draft than it would be after a discussion paper.¹⁷

¹⁶ The *Due Process Handbook* paragraph 6.25.

¹⁷ Paragraph 41 in [AP28](#) for the February 2018 Board meeting.