financial executives international
dirigeants financiers internationaux
canada

November 20, 2009

Technical Director
International Accounting Standards Board
30 Cannon Street
London, UK EC4M 6XH
Dear Sir or Madam:

Re: Exposure Draft – Rate-regulated Activities

The Committee on Corporate Reporting of Financial Executives International Canada (FEI Canada) is pleased to submit its comments in response to the Exposure Draft on Rate-regulated Activities as issued by the International Accounting Standards Board (IASB).

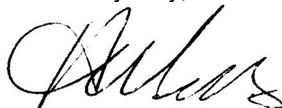
FEI Canada is the all-industry professional membership association for senior financial executives. With eleven chapters across Canada and more than 2,000 members, FEI Canada provides professional development, thought leadership and advocacy services to its members. The association membership, which consists of Chief Financial Officers, Audit Committee Directors and senior executives in the Finance, Controller, Treasury and Taxation functions, represents a significant number of Canada's leading and most influential corporations.

The Committee on Corporate Reporting (CCR) is one of two national advocacy committees of FEI Canada. CCR comprises more than 30 senior financial executives representing a broad cross-section of the FEI Canada membership and of the Canadian economy who have volunteered their time, experience and knowledge to consider and recommend action on a range of issues related to accounting, corporate reporting and disclosure. In addition to advocacy, CCR is devoted to improving the awareness and educational implications of the issues it addresses, and is focused on continually improving the standards and regulations impacting corporate reporting.

The CCR commends the Board on its ability to quickly and effectively address the issues of a large segment of the Canadian economy that has unique accounting requirements due to the economic form of rate-regulation, and the ability of external regulatory bodies' to set prices for services provided. The CCR is supportive of the direction the board has taken in terms of recognizing the specialized nature of the assets and liabilities that arise out of the regulatory process. Our primary concern relates to whether the ability of the IASB to approve a Rate-regulated Activities standard within the proposed timeframe. We understand that the IASB has many projects on its current agenda and, given resource constraints, we are concerned that the potential volume of responses may delay the publication of the standard. With Canadian public companies set to adopt IFRS on January 1, 2011, it is important for the rate regulated industry in Canada to have sufficient time to incorporate this new standard into their IFRS implementation plans. Accordingly, issuing a standard in advance of the January 1, 2011 conversion date is of primary importance to CCR. Our comments on the Exposure Draft are noted in the appendix attached to this letter.

We hope that our comments will be useful to the IASB in its deliberations. If you have any questions or would like to discuss any of these matters, please do not hesitate to contact us.

Yours very truly,



Victor Wells
Chair
Committee on Corporate Reporting
FEI Canada

Copy: Mr. Peter Martin, Accounting Standards Board (Canada)

The CCR's responses to the questions raised in the Exposure Draft are set out below.

Scope

Question 1

The exposure draft proposes two criteria that must be met for rate-regulated activities to be within the scope of the proposed IFRS (see paragraphs 3–7 of the draft IFRS and paragraphs BC13–BC39 of the Basis for Conclusions).

Is the scope definition appropriate? Why or why not?

In general, we agree with the scope definition included in the Exposure Draft. We do believe that some clarifying wording around the term "cost-of-service" could be added to the proposed standard to reduce the potential for differing interpretations. The interpretation of this term could lead to similar economic situations being scoped in or out. We note that there is some inconsistency in the application of this term between the standard and the Appendices in the following areas:

- the scope definition provided in paragraphs 3–7 of the draft IFRS and paragraphs BC13–BC39 of the Basis for Conclusions are appropriate. The application guidance in Appendix B, however, presents additional restrictions and conflicting wording within its descriptions of cost-of-service regulation. Appendix B indicates cost-of-service requires the rate setting mechanism to recover specific actual costs incurred or a true-up to actual costs incurred but does not include rate setting mechanisms that include assumptions for forecasted or estimated costs along with forecasted productivity factors. The implications of the use of projections, estimates, adjudication by the regulatory board in determination of 'prudent' costs to be included, and regulatory lag issues are not considered in the scope section but are discussed in the recognition and measurement section of Appendix B. A strict interpretation of the words 'the cost of service can only consider actual costs incurred' potentially reduces the number of entities that can apply this draft IFRS since many regulated entities incorporate forecast cost estimates and target efficiency rates in submitting rate applications.

- Appendix B paragraph B5 and B6 indicate that the return for shareholders must be adequate to be considered within scope but this appears to be a scope requirement beyond what is provided in the Scope paragraphs 3-7 of the draft IFRS.

- Paragraph B4 does not indicate whether all indicators are necessary to be considered cost-of-service or whether any will suffice. Paragraph B4 item (a) requires the regulation to be designed for the 'recovery of the specific entity's costs' which can be interpreted more broadly than Scope paragraph 3(b) which requires the regulation to be designed to 'recover the specific costs the entity incurs'. We recommend that these requirements be specifically outlined.

Recognition and Measurement

Question 2

The exposure draft proposes no additional recognition criteria. Once an activity is within the scope of the proposed IFRS, regulatory assets and regulatory liabilities should be recognised in the entity's financial statements (see paragraphs BC40–BC42 of the Basis for Conclusions).

Is this approach appropriate? Why or why not?

We agree with the Board's assessment that if rate-regulated activities meet the scope criteria then regulatory assets and regulatory liabilities should be recognized in the entity's financial statements to the extent approved or likely to be approved by the regulator.

Question 3

The exposure draft proposes that an entity should measure regulatory assets and regulatory liabilities on initial recognition and subsequently at their expected present value, which is the estimated probability-weighted average of the present value of the expected cash flows (see paragraphs 12–16 of the draft IFRS and paragraphs BC44–BC46 of the Basis for Conclusions).

Is this measurement approach appropriate? Why or why not?

We believe this measurement provides the users of the financial statements with valuable information regarding the best estimate of the amounts to be recovered. However, inconsistency arises where income tax amounts are included as a regulatory asset because income tax amounts reported outside of regulatory assets and liabilities are not subject to discounting. This will lead to the recording of a tax liability at the undiscounted amount while the offsetting asset for the recovery of this liability will be at a discounted amount.

Question 4

The exposure draft proposes that an entity should include in the cost of self-constructed property, plant and equipment or internally generated intangible assets used in regulated activities all the amounts included by the regulator even if those amounts would not be included in the assets' cost in accordance with other IFRSs (see paragraph 16 of the draft IFRS and paragraphs BC49–BC52 of the Basis for Conclusions). The Board concluded that this exception to the requirements of the proposed IFRS was justified on cost-benefit grounds.

Is this exception justified? Why or why not?

We strongly agree that amounts approved by the regulator should be included within the cost of self-constructed property, plant and equipment or internally generated intangible assets even if those amounts would be excluded according to other IFRSs. The expense involved in developing and maintaining two costing systems is very significant for a utility, with potentially hundreds of thousands of asset records. We believe this requirement does not provide additional benefit to the users of the financial statements (or the customer base should these additional costs be applied to rates).

Question 5

The exposure draft proposes that at each reporting date an entity should consider the effect on its rates of its net regulatory assets and regulatory liabilities arising from the actions of each different regulator. If the entity concludes that it is not reasonable to assume that it will be able to collect sufficient revenues from its customers to recover its costs, it tests the cash-generating unit in which the regulatory assets and regulatory liabilities are included for impairment in accordance with IAS 36 Impairment of Assets. Any impairment determined in accordance with IAS 36 is recognised and allocated to the assets of the cash-generating unit in accordance with that standard (see paragraphs 17–20 of the draft IFRS and paragraphs BC53 and BC54 of the Basis for Conclusions).

Is this approach to recoverability appropriate? Why or why not?

We believe the approach to recoverability is reasonable. The likelihood of an impairment issue arising, however, is remote if the measurement process in paragraphs 12-16 of the draft IFRS is applied. The regulatory asset should reflect the probability of the recoverability of the amounts to be charged in the future and therefore would already be appropriately valued.

Disclosures

Question 6

The exposure draft proposes disclosure requirements to enable users of financial statements to understand the nature and the financial effects of rate regulation on the entity's activities and to identify and explain the amounts of regulatory assets and regulatory liabilities recognised in the financial statements (see paragraphs 24–30 of the draft IFRS and paragraphs BC59 and BC60 of the Basis for Conclusions).

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 IFRS.

We believe the proposed disclosure requirements provide decision-useful information. We are concerned, however, with the requirement to disclose assumptions used to arrive at the value of the regulated asset prior to a rate case being finalized. Publicly disclosing this information could influence the outcome of the rate proceedings and could lead to a situation where the accounting would inappropriately influence the economic outcome.

Transition

Question 7

The exposure draft proposes that an entity should apply its requirements to regulatory assets and regulatory liabilities existing at the beginning of the earliest comparative period presented in the period in which it is adopted (see paragraph 32 of the draft IFRS and paragraphs BC62 and BC63 of the Basis for Conclusions). Any adjustments arising from the application of the draft IFRS are recognised in the opening balance of retained earnings.

Is this approach appropriate? Why or why not?

We believe this transition approach is appropriate.

Other Comments

Question 8

Do you have any other comments on the proposals in the exposure draft?

We have no further comments.