IFRS 14 REGULATORY DEFERRAL ACCOUNTS
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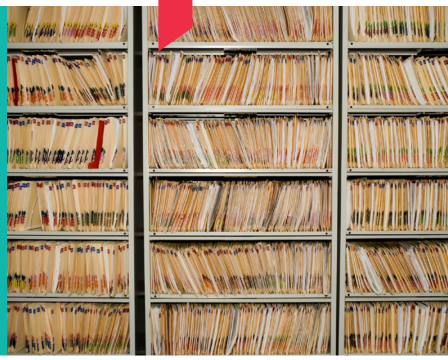

Summary

On 30 January 2014, the International Accounting Standards Board (IASB) published IFRS 14 *Regulatory Deferral Accounts*. IFRS 14 is an interim standard, pending the outcome of the IASB's more comprehensive Rate-regulated Activities project, which was re-opened in September 2012.

In many countries, industry sectors (including utilities such as gas, electricity and water) are subject to rate regulation where governments regulate the supply and pricing. This can have a significant effect on the amount and timing of an entity's revenue. Some national GAAPs require entities, that operate in industry sectors subject to rate regulation, to recognise associated assets and liabilities.

The scope of IFRS 14 is narrow, with this extending to cover only those entities that:

- Are first-time adopters of IFRS
- Conduct rate regulated activities
- Recognise associated assets and/or liabilities in accordance with their current national GAAP.

Entities within the scope of IFRS 14 would be afforded an option to apply their previous local GAAP accounting policies for the recognition, measurement and impairment of assets and liabilities arising from rate regulation, which would be termed regulatory deferral account balances.

Any regulatory deferral account balances, and their associated effect on profit or loss, would be recognised and presented separately from other items in the primary financial statements. As a result, for those entities that elect to adopt IFRS 14, all other line items and subtotals would exclude the effects of regulatory deferral accounts, meaning that they would be comparable with other entities that report in accordance with IFRS but do not apply IFRS 14.

Application guidance is included in IFRS 14 in respect of other IFRSs that would need to be considered alongside the previous national GAAP accounting requirements in order for these regulatory deferral accounts to be accounted for appropriately in an entity's IFRS financial statements, including:

- IAS 10 *Events after the Reporting Period*
- IAS 12 *Income Taxes*
- IAS 28 *Investments in Associates and Joint Ventures*
- IAS 33 *Earnings per Share*
- IAS 36 *Impairment of Assets*
- IFRS 3 *Business Combinations*
- IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*
- IFRS 10 *Consolidated Financial Statements*
- IFRS 12 *Disclosure of Interests in Other Entities*.

IFRS 14 has an effective date of 1 January 2016, with early application permitted.

STATUS
Final

EFFECTIVE DATE
1 January 2016, with earlier application permitted

ACCOUNTING IMPACT
May be significant.

Background

In many jurisdictions, the charges that entities in certain industries can demand from their customers for the delivery of goods and services are set by regulatory bodies or governments. Common examples are entities involved in the transportation and utility sectors. This price-setting activity is commonly referred to as rate regulation.

Prior to the issue of IFRS 14, there was no IFRS that specifically addressed the accounting requirements for entities subject to rate regulation. The IASB previously issued an exposure draft covering the topic, but this was not taken forward to a final IFRS. In contrast, some national GAAPs either permit or require entities to capitalise rate–regulated assets and liabilities in their statements of financial position.

As more jurisdictions that currently permit or require the recognition of rate-regulated assets and liabilities transition (or consider moving) to IFRS, questions have continued to be raised about whether these rate-regulated assets and liabilities meet the definitions of assets and liabilities in the current IFRS *Conceptual Framework*. The effects of accounting for rate regulated activities can be significant, meaning that for those entities which currently report under a framework which permits the recognition of associated assets and liabilities, the inability to recognise them in accordance with IFRS can be a barrier to the adoption of those accounting standards.

Consequently, IFRS 14 introduces an option for entities that are first-time adopters of IFRS (but not entities that have already adopted IFRS), to continue to account for balances arising from rate regulated activities (these balances are termed 'regulatory deferral account balances') in their financial statements, in accordance with their previous GAAP. If an entity wishes to take advantage of this option, it must do this on adoption of IFRS.

The IASB believes that, by affording first time adopters this option while also isolating the recognition and presentation of regulatory deferral account balances and the effects of regulatory deferral accounts in the primary financial statements, it will facilitate further adoption of IFRS which will enhance the comparability of financial statements around the globe.

Summary of the Standard

1. Objective

The objective of IFRS 14 is to specify the financial reporting requirements for rate-regulated assets and liabilities (which are termed 'regulatory deferral account balances') that arise when an entity is subject to rate regulation.

2. Scope

(i) Applicable entities

The scope of IFRS 14 is very narrow. Only entities that are first-time adopters of IFRS are able to apply its requirements – both in the period in which they prepare their first IFRS financial statements, and in each subsequent period.

Therefore, IFRS 14 is not available to entities that have already adopted IFRS.

(ii) Applicable rate-regulation activities

IFRS 14 only applies to entities that:

– Conduct 'rate regulated activities'

  Rate regulated activities are activities subject to a rate regulation framework that are overseen by a rate regulator, being an authorised body that has the power (through either law or regulation) to impose a rate or range of rates that are charged by an entity to its customers.

– Recognise rate-regulated assets and liabilities in accordance with their existing national GAAP.

(iii) An 'all or nothing' choice

If an entity qualifies for, and elects to apply, IFRS 14, it must do so for all of its rate-regulated assets and liabilities, and must apply all of the requirements of its existing national GAAP to those balances.

3. Recognition and measurement requirements

(i) General

In preparing its first IFRS financial statements, an entity within the scope of (which elects to apply) IFRS 14 continues to apply its previous national GAAP accounting policies for the recognition, measurement and impairment of regulatory deferral account balances.

Consequently, an entity is exempt from applying paragraph 11 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. IAS 8.11 requires an entity to apply the requirements of other IFRSs dealing with similar and related issues, as well as the definitions, criteria, and concepts of the *Conceptual Framework*, in developing accounting policies in the absence of a specific IFRS in accordance with IAS 8.10.

However, an entity is permitted to change its brought forward national GAAP accounting policy should the change result in the financial statements either being:

– More relevant to the economic decision-making needs of users, and no less reliable

– More reliable, and no less relevant to the economic decision-making needs of users.

(ii) Additional guidance for interaction with other IFRSs

While an entity within the scope of IFRS 14 would continue to apply the recognition, measurement and impairment requirements of its previous national GAAP when accounting for regulatory deferral account balances (rather than applying IFRSs), there are still a number of situations in which other IFRSs may be required to be applied.

The application of these IFRSs is outlined in detail in IFRS 14.16-17 and Appendix B, and are summarised in the table below.

IAS 10 *Events after the Reporting Period*

Estimates used in determining regulatory deferral account balances

IAS 10 is to be applied in determining whether information obtained after reporting date but prior to the authorisation of the financial statements, relating to estimates and assumptions used in determining the recognition and measurement of its regulatory deferral account balances are:

- Adjusting events
- Non-adjusting events.

IAS 12 *Income Taxes*

Scope of IAS 12

The scope of IAS 12 extends to regulatory deferral account balances.

Where rates are permitted or required to be increased to recover some or all of an entity's tax expense

In this circumstance, local GAAP may require an entity recognising a regulatory deferral account balance in relation to income tax. If the recognition of such a regulatory deferral account balance in itself results in a temporary difference in accordance with IAS 12, deferred tax associated with this temporary difference would need to be recognised.

Presentation

Any deferred tax balance recognised, and any movement in those balances during the period, in relation to regulatory deferral account balances, is not to be presented in the statement of financial position and statement of profit or loss and other comprehensive income accordance with IAS 12. Instead, an entity either:

- Presents the balance/movement within the line item related to the regulatory deferral accounts, or
- In a separate line item alongside the line item related to the regulatory deferral accounts.

IAS 28 *Investments in Associates and Joint Ventures*

Consistent accounting policies

In applying the equity method, an entity must make any required adjustments to the accounting policies of its associates or joint ventures in relation to regulatory deferral account balances so that they are consistent with its own accounting policies.

IAS 33 *Earnings per Share*

Presentation of basic and diluted earnings per share

Calculation of basic and diluted earnings per share excludes the net movement in the regulatory deferral account balances.

IAS 36 *Impairment of Assets*

Impairment of regulatory deferral account balances

If an entity recognises regulatory deferral account balances, it is required to apply its previous national GAAP in respect of impairment of regulatory deferral account balances. The requirements of IAS 36 are not applicable to those balances.

Impairment of cash generating units (CGU) containing regulatory deferral account balances

IAS 36 is applied in assessing whether regulatory deferral account balances are to be included in a CGU for the purpose of the impairment test (for example, because the CGU contains goodwill of an indicator of impairment has been identified).

If it is determined that an impairment loss is to be recognised, the related requirements of IAS 36 are applied (the impairment loss applied first to any goodwill included in the CGU, and then proportionally to any other remaining balances).

IFRS 3 *Business Combinations*

Recognition and measurement of regulatory deferral account balances in an acquiree

If an entity acquirers a business that contains recognised regulatory deferral account balances, it accounts for these balances at acquisition and subsequently in its consolidated financial statements in accordance with its accounting policy related to regulatory deferral account balances.

This means that, if an entity is outside of the scope of IFRS 14 or has opted not to apply IFRS 14, it would not be permitted to recognise regulatory deferral account balances that were included in acquired subsidiaries.

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*

Presentation

Any regulatory deferral account balances, and the net movement in those balances during the period, in relation to regulatory deferral account balances that are included in a discontinued operation, are not to be presented as part of the 'single-line' approach in accordance with IFRS 5. Instead, an entity either:

- Presents the balance/movement within the line item related to the regulatory deferral accounts, or
- In a separate line item alongside the line item related to the regulatory deferral accounts.

IFRS 10 *Disclosure of Interests in Other Entities*

Consistent accounting policies

In consolidating its subsidiaries in its consolidated financial statements, a parent must make any required adjustments to the accounting policies of its subsidiaries in relation to regulatory deferral account balances so that they are consistent with its own accounting policies.

IFRS 12 *Disclosure of Interests in Other Entities*

Disclosures of regulatory deferral account balances in material subsidiaries with non-controlling interests, material joint ventures, and material associates

- Disclose the net movement in regulatory deferral account balances (IFRS 12.12(e))
- Disclose the regulatory deferral account debit balance, the regulatory deferral account credit balance, and the net movement in those balances during the period for each entity.

Disclosures of gain or loss on the loss of control over a subsidiary

- In addition to the disclosures required by IFRS 12.19 (gain or loss on disposal, the portion of that gain or loss attributable to any retained investment in the former subsidiary, and the line item(s) in profit or loss in which the gain or loss is recognised) disclosure is required for the portion of that gain or loss that is attributable to derecognising regulatory deferral account balances in the former subsidiary at the date on which control is lost.

Figure 1: Application of other IFRS's on regulatory deferral balances

4. *Presentation*

(i) Regulatory deferral account balances

IFRS 14 requires an entity to present the following as separate line items in the statement of financial position:

- The total of all regulatory deferral account debit balances (which would have been assets under national GAAP)
- The total of all regulatory deferral account credit balances (which would have been liabilities under national GAAP).

In addition, an entity must use additional subtotals in order clearly to distinguish the above line items from the entity's other asset and liability line items that are presented in accordance with other IFRSs. The figure below is an extract from illustrative example 1 of IFRS 14.

XYZ Group – Statement of financial position as at 31 December 20X7		
	31 Dec 20X7	31 Dec 20X6
ASSETS		
Non-current assets		
…	…	…
Total non-current assets	**888,910**	**935,920**
Current assets		
…	…	…
Total current assets	**464,640**	**476,410**
Total assets	**1,353,550**	**1,412,330**
Regulatory deferral account debit balances and related deferred tax asset	112,950	111,870
Total assets and regulatory deferral account balances	**1,466,500**	**1,524,200**
EQUITY AND LIABILITIES		
Equity attributable to owners of the parent		
…	…	…
	903,700	782,900
Non-controlling interests	70,050	48,600
Total equity	**973,750**	**831,500**
Non-current liabilities		
…	…	…
Total non-current liabilities	177,650	238,280
Current liabilities		
…	…	…
Total current liabilities	217,140	377,950
Total liabilities	**394,790**	**616,230**
Total equity and liabilities	**1,368,540**	**1,447,730**
Regulatory deferral account credit balances	97,960	79,470
Total equity, liabilities and regulatory deferral account credit balances	**1,466,500**	**1,524,200**

Figure 2: Example presentation of the additional subtotals required to distinguish regulatory deferral account balances from other line items in the statement of financial position

(ii) Movement in regulatory deferral account balances

The net movement in all regulatory deferral account balances for the reporting period, except for amounts acquired or disposed of, are presented as a separate line item in the statement of profit or loss and other comprehensive income (or in the separate statement of profit or loss).

In addition, additional subtotals are required in order clearly to distinguish the net movement in all regulatory deferral account balances during the reporting period from the other income and expense line items that are presented in accordance with other IFRSs. The figure below is an extract from illustrative example 1 of IFRS 14.

XYZ Group – Statement of profit or loss and other comprehensive income for the year ended 31 December 20X7	31 Dec 20X7	31 Dec 20X6
Revenue	390,000	355,000
…	…	…
Profit before tax	**193,185**	**106,204**
Income tax expense	(43,587)	(44,320)
Profit for the year before net movements in regulatory deferral account balances	**149,598**	**61,884**
Net movement in regulatory deferral account balances related to profit or loss and the related deferred tax movement	(27,550)	(3,193)
Profit for the year and net movements in regulatory deferral account balances	**122,048**	**65,077**
Other comprehensive income: Items that will not be reclassified to profit or loss, net of income tax		
…		
Net movement in regulatory deferral account balances related to other comprehensive income	7,140	4,207
Other comprehensive income for the year, net of income tax	**(798)**	**423**
Total comprehensive income for the year	**121,250**	**65,500**
Profit and net movements in regulatory deferral account balances attributable to:		
Owners of the parent	…	…
Non-controlling interests	…	…
	122,048	**65,077**
Total comprehensive income attributable to:		
Owners of the parent	…	…
Non-controlling interests	…	…
	121,250	**65,500**

Figure 3: Example presentation of the additional sub-totals required to distinguish regulatory deferral account balances from other line items in the statement of profit or loss and other comprehensive income

5. Disclosure

(i) General disclosure objective

IFRS 14 contains specific disclosure requirements which are designed clearly to identify:

- The nature of, and the risks associated with, the rate regulation that restricts the prices that the entity can charge customers for the goods and services it provides
- The effects of that rate regulation on its financial position, financial performance and cash flows.

In order to meet these requirements an entity is required to consider:

- The level of detail that is necessary to satisfy the disclosure requirements
- How much emphasis to place on each of the various requirements
- How much aggregation or disaggregation to include
- Whether users of financial statements need additional information to evaluate the quantitative information disclosed.

(ii) Explanation of activities subject to rate regulation

For each type of rate-regulated activity, an entity is required to disclose:

- A brief description of the nature and extent of the rate-regulated activities
- A brief description of the nature of the regulatory rate setting process
- The identity of the rate regulator and, if it is a related party, disclosure of this fact with an explanation of how it is a related party
- How the future recovery of each regulatory deferral account debit balance or reversal of each regulatory deferral account credit balance is affected by risks and uncertainty, for example:
  - Demand risk (e.g. changes in consumer attitudes, availability of alternative sources of supply, levels of competition)
  - Regulatory risk (e.g. the submission or approval of a rate-setting application, expected future regulatory actions)
  - Other risks (e.g. currency, other market risks).

The above information is required to be presented either:

- In the financial statements
- Another statement (i.e. management commentary, risk report) that is available at the same time and with the same ease as the financial statements, with a cross reference to this other statement in the financial statements.

(iii) Explanation of recognised amounts

For each regulatory deferral account balances, disclosure is required of the basis of initial and subsequent recognition and measurement – including an assessment of recoverability and allocation of any impairment losses.

For each type of rate-regulated activity, an entity must disclose:

- A tabular reconciliation between the opening and closing amounts. While the level of detail is a matter of judgement, the following components would usually be relevant:
  - Amounts recognised in the current period as regulatory deferral account balances to be recovered or reversed in the current or future periods
  - The amount recognised relating to balances that have been recovered, amortised or reversed in the current period
  - Other amounts (for example, items acquired or assumed in a business combination, items disposed of, the effects of changes in foreign exchange rates, changes in discount rates, changes in estimated cash flows).
- The rate of return or discount rate allowed (or required) by the rate regulator to reflect the time value of money that is applicable to each regulatory deferral account balance
- The remaining periods over which the entity expects to recover or amortise/reverse the carrying amount of each regulatory deferral account debit/credit balance.

In addition, the entity applies presentation requirements of other IFRSs identified in Figure 1 above:

- Presentation of deferred tax balances that arise in respect of the regulatory deferral account debit and credit balances as a separate category of deferral account (in the reconciliation required above)
- Any regulatory deferral account balances, and the net movement in those balances, that are related to a discontinued operation or a disposal group are presented as part of the regulatory deferral account balances and movements as opposed to within the disposal groups or discontinued operations as would usually be required by IFRS 5
- The regulatory deferral account debit and credit balances and the net movement in the balances relating to interest in a subsidiary, associate or joint venture, where this disclosure is required by IFRS 12.

When a regulatory deferral account balance is no longer fully recoverable, disclose:

- That fact
- The reasons why it is not recoverable
- The amount of the associated reduction in the regulatory deferral account balance.

6. Transition

There are no specific transitional requirements in IFRS 14.

First time adopters of IFRS will also be able to obtain relief from the requirements of IFRS 1 *First-time Adoption of International Financial Reporting Standards*, including, for example, the use of previous GAAP carrying amounts as deemed cost for property, plant and equipment and intangible assets.

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