Financial Reporting Council

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Chairman
IASB
30 Cannon Street
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16 September 2013

Dear Hans

IASB Exposure Draft ED/2013/5 *Regulatory Deferral Accounts*

I am writing on behalf of the Financial Reporting Council (FRC), in response to the above Exposure Draft (ED).

The FRC does not support the issue of the proposed interim standard, for the following reasons:

- It is not principles-based. The IASB should firstly determine if regulatory deferral account balances are assets and liabilities in accordance with the *Conceptual Framework* and if it is found they are not then the IASB should be wary of including them in financial statements.

- The objective of a single set of International Financial Reporting Standards (IFRSs) will no longer be obtainable, as different jurisdictions will be permitted to carry forward previous practices, which may give rise to diversity in practice. This will result in there being two or more versions of IASB sanctioned IFRSs.

- Users will need to determine whether financial statements have applied existing IFRSs or an 'alternative' form of IFRSs, so the introduction of the proposed interim standard erodes the confidence that users have in those financial statements and also the confidence they have in the IASB for producing high quality accounting standards.

- The effects of the proposed interim standard are more wide-ranging than existing transitional arrangements found in IFRS 1 *First-time Adoption of International Financial Reporting Standards* and may have a long life. This is because completion of the *Conceptual Framework* project may be necessary before a comprehensive review of rate regulation can resolve the question of whether regulatory deferral account balances are assets or liabilities.

Although interim standards have previously been issued in relation to the insurance and extractive industries as a means of reducing diversity in practice, the FRC does not support the issue of the proposed interim standard for rate regulation. This is because it does not provide a level playing field for all users of IFRSs and therefore may prove to be disadvantageous to those jurisdictions that already use IFRSs.

The Appendix to this letter includes the FRC's responses to the questions set out in the Invitation to Comment in the ED. Although we do not agree with the introduction of this interim standard, our responses have been written on the assumption that this standard will be developed into an IFRS.

Should you have any queries about the comments in this letter please do not hesitate to contact either me or Annette Davis at 020 7492 2322 or a.davis@frc.org.uk.

Yours sincerely

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Appendix: Response to Questions

<u>**Please note that the FRC's default position is that an interim standard should not be issued. However, the responses below are drafted with the assumption that the draft standard will be issued.**</u>

Scope

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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we agree with restricting the scope as described.

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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we consider that the above criteria to be appropriate because it will restrict the use of this standard to those entities that are regulated by an authorised body and are not just self-regulated and setting a price cap upon themselves.

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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we consider entities that wish to apply existing IFRSs, rather than an 'alternative' form of IFRSs, should be permitted and encouraged to do so. Although this may lead to diversity in accounting policies within a particular jurisdiction during the period of application of the interim standard, it will minimise international diversity by maximising the global number of entities applying current IFRSs.

Recognition, measurement and impairment

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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we agree that entities which currently do not recognise regulatory deferral account balances should be required to wait until the IASB has completed its comprehensive review of rate regulation before amending their accounting treatment in this regard. There is no obvious beneficial reason for permitting such entities to do otherwise.

Question 5
The Exposure Draft proposes that, in the absence of any specific exemption of 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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we agree that the general application of other standards to regulatory deferral account balances would seem to be appropriate.

Presentation

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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we agree that separate presentation in the form of an extra line item will serve to segregate the 'alternative IFRS' balances, thus keeping them separate from existing IFRS balances to a degree, which will help to facilitate comparability.

Disclosure

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.

Response:

If the IASB proceeds with issuing the proposed interim standard, we agree that, in the same way that regulatory deferral account balances are proposed to be shown separately in the financial statements, they should also be separated in the notes to the financial statements.

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:

If the IASB proceeds with issuing the proposed interim standard, we consider the references to materiality and other factors are relevant to ensure that the financial statements do not become cluttered and therefore obscure relevant information.

Transition

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?

Response:

If the IASB proceeds with issuing the proposed interim standard, we consider that the transition requirements seem appropriate.

Other comments

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

Response:

No.