



OICV-IOSCO

Organización Internacional de Comisiones de Valores
International Organisation of Securities Commissions
Organisation internationale des commissions de valeurs
Organizaçào Internacional das Comissões de Valore

January 14, 2010

Exposure Draft: Rate-regulated Activities
International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

RE: Exposure Draft: *Rate-regulated Activities*

Dear IASB Members:

The International Organization of Securities Commissions (IOSCO) Standing Committee No. 1 on Multinational Disclosure and Accounting (Standing Committee No. 1) thanks you for the opportunity to provide our comments regarding the International Accounting Standards Board (IASB or the Board) Exposure Draft on *Rate-regulated Activities* (the Exposure Draft).

IOSCO is committed to promoting the integrity of international markets through promotion of high quality accounting standards, including rigorous application and enforcement. Members of Standing Committee No. 1 seek to further IOSCO's mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. The comments we have provided herein, unless indicated otherwise, reflect a general consensus among the members of Standing Committee No. 1 and are not intended to include all of the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

Following are our general comments regarding the Exposure Draft. We did not attempt to respond to the specific questions in the Exposure Draft.

Consistency of ED with the Framework

Some members of the Committee agree with the Board's conclusion (paragraph BC 15) that regulatory assets and liabilities recognized pursuant to the Exposure Draft meet the definitions of assets and liabilities set forth in the IASB's Framework for the Preparation and Presentation of Financial Statements (Framework). These members agree that the recognition

Calle Oquendo 12
28006 Madrid
ESPAÑA
Tel.: (34.91) 417.55.49 • Fax:
(34.91) 555.93.68
mail@oicv.iosco.org
• www.iosco.org

of regulatory assets and liabilities arising from cost-of-service regulation is supportable based on the Framework, however they also acknowledge that jurisdictions and entities might apply the Framework differently in the absence of the proposed IFRS. Therefore, these members believe that the Exposure Draft would help to reduce potential diversity in practice, particularly as more jurisdictions adopt IFRS.

Other members of the Committee do not agree that the recognition of assets and liabilities as proposed by the Exposure Draft is consistent with the Framework. These members generally agree with the alternative views of those Board members who voted against publication of the Exposure Draft. While these members believe that information about the effects of rate-regulation on an entity would be useful to financial statement users, these members believe that such information is better provided through disclosure and not recognition in the financial statements. In summary, these members believe that the Exposure Draft is inconsistent with the Framework for the reasons set forth below.

The Framework defines an asset as “a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.” [paragraph 49(a)]. These members do not believe that regulatory assets represent resources controlled by the regulated entity. Rather, the actions of the regulator are simply the permission to charge customers at specified rates, but do not obligate those customers, either individually or in the aggregate as a customer base, to purchase the entity’s product or service. These members believe that the activities within the scope of the Exposure Draft are not so economically different from activities of certain non-rate-regulated entities that operate as a monopoly or as part of an oligopoly. Consequently, these members believe that the Exposure Draft would have the effect of broadening significantly the Framework’s definition of an asset.

Some members also do not believe that the Exposure Draft is consistent with the Framework’s notion that an asset arises as a result of past events. These members believe that the event which gives rise to the asset is not the incurrence of a cost, but rather the future transaction(s) with the customer or customer base.

The Framework defines a liability as “a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.” [paragraph 49(b)]. These members do not believe that most regulatory liabilities that would be recognized pursuant to the Exposure Draft meet this definition, for reasons similar to those described above for regulatory assets (e.g., the past event obligating the entity is the transaction with the customer). Of the types of liabilities described in paragraph B20 of the Exposure Draft, these members believe that only those obligations that are for determinable amounts and that will be refunded to specified customers are liabilities under the Framework. These members believe the fact that a probable cash inflow will, as a result of actions by a regulator, be less than it otherwise might have been is not analogous to an outflow of economic resources.

If the Board ultimately decides to issue a standard resulting in the recognition of regulatory assets and liabilities similar to that proposed in the Exposure Draft, some members suggest the Board consider the following alternatives.

Alternative 1 – Define regulatory assets as intangible assets in the context of an entity’s legal right to operate as a monopoly and increase future billings to its customer base. Some

members believe such an approach would be more consistent with the decisions reached in IFRIC Interpretation 12, *Service Concession Arrangements*.

Alternative 2 – Amend the Framework’s definitions of assets and liabilities.

Alternative 3 - In the absence of Alternatives 1 and 2, clearly state that regulatory assets and liabilities recognized pursuant to the Exposure Draft are exceptions to the Framework’s definitions of assets and liabilities. This would help to limit further departures from the Framework that might otherwise result from analogy to the Exposure Draft.

Scope

We believe that the Exposure Draft should contain a recognition threshold for specific costs. By asserting that regulatory assets recognized pursuant to the Exposure Draft are consistent with the Framework’s definition of assets, the Board appears to have established through the Exposure Draft’s scope provisions an implicit recognition threshold that such assets must be probable (greater than fifty-percent probability) of being recovered. However, the scope provisions of the Exposure Draft apply to an entity’s rate-regulated activities as a whole and not to specific costs. In certain jurisdictions that employ cost of service regulation, not all costs may be recoverable or recoverable at their full amounts. As a result, once an entity has concluded that its activities are within the scope of the Exposure Draft, the Exposure Draft’s measurement provisions may require an entity to recognize a regulatory asset even though that entity believes it is not probable that the regulator will allow recovery of that cost. We recommend that the Board either add a recognition threshold for specific costs, or clarify in the Basis for Conclusions its intent and reasons for not doing so. If the Board does not clarify its intent, we believe that some entities might apply the Framework’s recognition threshold to specific costs, whereas other entities might not, resulting in potentially significant diversity.

Consistent with comments made above regarding consistency of the Exposure Draft with the Framework, some members believe that because a rate regulator’s guarantee of the rate does not equate to recovery, activities within the scope of the Exposure Draft are not significantly different economically from a non-regulated monopoly dependent on future demand from customers. Similarly, certain types of regulation such as price-cap regimes that are excluded from the scope of the Exposure Draft may result in obligations no different than those under cost of service regulation.

We believe that the Board’s intent was that the specified return criteria should be applied in the aggregate (e.g., whether the rate-regulated activities in the aggregate will provide a return) and not on an individual cost-by-cost basis (e.g., when a regulator permits recovery only of a cost, or partial recovery but overall rates in aggregate provide a return). However, we suggest that the Board should clarify this in any final standard.

Measurement

While some members agree with the proposed probability-weighted approach, other members believe that the Board should consider as an alternative a deterministic method, for example management’s best estimate. These members believe that the proposed approach may be overly complex and difficult for some preparers to implement, and that a best estimate approach could, combined with the selection of an appropriately risk-adjusted discount rate, result in an equally useful measurement of an entity’s regulatory assets and liabilities.

We are unclear what the Board's intent was when in the Exposure Draft (paragraph 15) it states that "... the discount rates used shall not reflect risks for which the estimated cash flows have been adjusted. However, the fact that the estimated future cash flows have been adjusted for the probability of different outcomes occurring does not eliminate the need to include in the discount rate the price for bearing the uncertainty inherent in the regulatory asset or regulatory liability." The first sentence is consistent with the requirement in IAS 36 that risks not be "double-counted". However, the meaning of the second sentence is unclear. The Exposure Draft already requires an entity to incorporate into measurement the uncertainty regarding both timing and probability of potential outcomes (e.g., whether and at what amount a regulator would permit recovery of a specific cost). We suggest that the Board conform the language in paragraph 15 to that in IAS 36, and consider clarifying the nature of what factors might represent additional uncertainties incremental to those incorporated into the assessment of probability-weighted outcomes.

Some members do not agree with the Exposure Draft's requirement to include in the cost of self-constructed or internally generated assets amounts that would not otherwise be eligible for inclusion under other IFRS (paragraph 16). These members believe that this requirement represents another departure from the Framework and principles established by other IFRS.

Recoverability

We believe that the Board should more clearly explain the relationship amongst expected customer demand, measurement of individual regulatory assets and the recoverability of the cash-generating unit in which those regulatory assets reside. Paragraphs 17 – 20 of the Exposure Draft seem to indicate that if an entity, as a result of decreases in expected customer demand, does not believe it will recover the entire aggregate carrying amount of its regulatory assets, then that entity should then test the entire cash-generating unit for impairment in accordance with IAS 36. However, it is not clear why possible changes in customer demand should not or could not be included in the recurring remeasurement of individual regulatory assets required by paragraphs 13 – 15. The Board should consider including an example(s) of the impact of expected decreases in customer demand on regulatory asset remeasurement combined with the impact of this expected decrease in customer demand on an entity not recovering some or all of its regulatory assets (e.g., impairment indicator and resulting impairment of cash-generating unit(s)).

We also believe that an entity that concludes it will not recover some or all of its regulatory assets based on customer demand would need to reconsider whether its activities are still within the scope of the Exposure Draft. In such cases, the regulatory regime would appear to no longer meet the definition of cost-of-service regulation as it is no longer designed to recover costs, much less provide a return on those costs.

The Exposure Draft requires that an impairment loss recognized pursuant to IAS 36 be allocated to the assets (including regulatory assets) of the cash-generating unit, and that an entity "reflect the impairment loss allocated to each regulatory asset by reducing the entity's estimate of future cash flows that it will receive from the regulatory asset as required by paragraphs 13(a) and 14 of this [draft] IFRS". We suggest that the Board include in any final standard an example(s) of how to apply this requirement, including recurring re-measurements of the regulatory asset(s) in periods subsequent to the recognition of impairment. Because the aggregate impairment recognized under IAS 36 is for the cash-

generating unit as a whole, measurement of the impairment likely will be affected by factors other than those directly relating to measurement of individual regulatory assets under paragraphs 13 – 15 of the Exposure Draft.

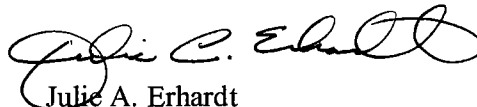
Derecognition

Some members of the Committee agree with the Board’s proposed approach toward derecognition. These members generally are those who do not believe that recognition of regulatory assets and liabilities is consistent with the Framework. Other members, however, disagree with the proposed approach toward derecognition. Specifically, these members disagree with the Board’s conclusion that an entity must always derecognize regulatory assets and liabilities when that entity’s activities no longer meet the scope provisions of the Exposure Draft. These members believe that in certain circumstances, regulatory assets and liabilities arising from cost-of-service regulation might be supportable based on the Framework alone, notwithstanding the specific requirements of the Exposure Draft.

* * * *

We appreciate your thoughtful consideration of the comments raised in this letter. If you have any questions or need additional information on the recommendations and comments that we have provided, please do not hesitate to contact me at 202-551-5300.

Sincerely,



Julie A. Erhardt
Chairman
IOSCO Standing Committee No. 1