IFRS Global office
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IFRS in Focus
IASB publishes IFRS 14 *Regulatory Deferral Accounts*

Contents

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This edition of IFRS in Focus outlines the requirements of IFRS 14 *Regulatory Deferral Accounts*, which specifies the accounting for regulatory deferral account balances that arise from rate regulation. The Standard is available only to first-time adopters of IFRSs who recognised regulatory deferral account balances under their previous GAAP.

The Bottom Line

- IFRS 14 permits eligible first-time adopters of IFRSs to continue their previous GAAP rate-regulated accounting policies, with limited changes.
- The Standard requires separate presentation of regulatory deferral account balances in the statement of financial position and of movements in those balances in the statement of profit or loss and other comprehensive income.
- Disclosures are required to identify the nature of, and risk associated with, the form of rate regulation that has given rise to the recognition of regulatory deferral account balances.
- IFRS 14 is effective for an entity's first annual IFRS financial statements for a period beginning on or after 1 January 2016, with earlier application permitted.

Why has the new Standard been issued?

The lack of specific guidance in IFRSs addressing the accounting for rate-regulated activities has resulted in a number of requests for guidance to the IASB. As a consequence, the IASB started a comprehensive project on rate-regulated activities in September 2012. This comprehensive project is currently in its research phase, with a discussion paper expected to be issued later in 2014.

However, the IASB was concerned that the lack of guidance may be a barrier to the adoption of IFRSs for those entities that undertake rate-regulated activities.
As a result, the IASB decided to add an additional phase to develop a limited-scope Standard to provide a short-term, interim solution for rate-regulated entities that have not yet adopted IFRSs but that recognise regulatory deferral account balances under their previous GAAP.

The issue of IFRS 14 as a limited-scope Standard does not anticipate the outcome of the comprehensive project which aims to address the broader issue of whether regulatory deferral account balances meet the definitions of assets and liabilities in the *Conceptual Framework*. Instead, IFRS 14 is an interim solution to promote the adoption of IFRSs and to aid comparability by ensuring that amounts of regulatory deferral account balances and movements therein are clearly identified in the financial statements.

Observation

The interim Standard issued by the IASB is similar in nature to the interim Standards that have been issued in the past – IFRS 4 *Insurance Contracts* and IFRS 6 *Exploration for and Evaluation of Mineral Resources*. These interim Standards effectively 'grandfather' existing requirements under previous GAAP pending the development of a comprehensive IFRS. The experience with both IFRS 4 and IFRS 6 suggests that 'interim' can mean a considerable period of time given the complexity of the issues involved.

Which entities are eligible to apply the new Standard?

An entity is permitted (but not required) to apply IFRS 14 if it:

- adopts IFRSs for the first time;
- is involved in rate-regulated activities; and
- recognised amounts for regulatory deferral account balances under its previous GAAP.

Therefore, an entity may only apply IFRS 14 upon the adoption of IFRSs if it has previously recognised regulatory deferral account balances in its financial statements under its previous GAAP.

Perhaps one of the more complex aspects of the Standard is identifying what types of rate regulation fall within the scope of the Standard. Rate regulation is defined as "a framework for establishing the prices that can be charged to customers for goods or services and that framework is subject to oversight and/or approval by a rate regulator". A rate regulator is an authorised body that is empowered by statute or regulation to establish the rate or a range of rates that bind an entity.

Entities involved in self-regulated activities, i.e. activities that are not subject to a pricing framework that is overseen and/or approved by a rate regulator, are not eligible to apply IFRS 14. Therefore, IFRS 14 is not applicable to an entity with a dominant position in a market that decides to self-regulate to avoid potential government intervention that may occur if the entity were perceived to be abusing its dominant position. Instead, a formal rate regulator needs to be involved. However, a self-regulated entity may be eligible to apply the Standard if:

- the entity's own governing body or a related party sets prices both in the interests of the customers and to ensure the overall financial viability of the entity within a specified framework; and
- this framework is subject to oversight and/or approval by an authorised body that is empowered by statute or regulation.

Observation

The exposure draft preceding IFRS 14 proposed that it would apply only to rate regulated regimes under which the permitted rate is designed to recover the entity's allowable costs of providing the regulated goods or services. In the Board's redeliberations and after considering the responses received on the ED, this criterion has been removed. The IASB took this decision in line with its objective to reduce barriers to the adoption of IFRSs and to avoid being perceived as prejudicing the outcome of the ongoing comprehensive project on rate regulation. The IASB took the view that restricting the scope of IFRS 14 to first-time adopters that currently recognise regulatory balances under their previous GAAP would sufficiently limit the population of entities recognising regulatory deferral account balances under IFRSs.

What are the accounting implications of applying IFRS 14?

An entity that is eligible, and elects, to apply IFRS 14 in its first IFRS financial statements continues to use its previous GAAP accounting policies for the recognition, measurement, impairment and derecognition of regulatory deferral account balances. Essentially, this means that, in respect of those balances, the provisions of the entity's previous GAAP continue to apply.

However, IFRS 14 introduces specific presentation and disclosure requirements as set out below.

If an eligible entity chooses to apply the Standard, it should apply the requirements to all regulatory deferral account balances arising from all its rate-regulated activities.

IFRS 14 does not apply to amounts that are permitted or required to be recognised as assets or liabilities in accordance with other Standards. Such amounts should, therefore, not be included as part of the regulatory deferral account balances.

Regulatory deferral account balances are therefore those balances of any expense (or income) account that would not be recognised as an asset or liability in accordance with other Standards, but that qualify for deferral in accordance with the rate regulation regime.

Observation

The IASB has deliberately avoided the terms "regulatory assets" and "regulatory liabilities" so as not to prejudge the outcome of their comprehensive project which is considering whether regulatory deferral account balances meet the definition of assets or liabilities in the *Conceptual Framework*. Instead, IFRS 14 requires such balances to be presented as regulatory deferral debit balances or regulatory deferral credit balances.

Also, other Standards continue to apply and may also need to be applied to regulatory deferral account balances to reflect them appropriately in the financial statements.

The Application Guidance sets out how the new Standard will interact with other IFRSs. The table below set out exceptions to, and exemptions from, other Standards and additional presentation and disclosure requirements applicable.

Standard	Application
IAS 10 *Events after the Reporting Period*	Adjustments to estimates and assumptions used in determining regulatory deferral account balances to be considered for the impact of events that occur between the end of the reporting period and the date the financial statements are authorised for issue.
IAS 12 *Income Taxes*	Deferred tax assets and deferred tax liabilities related to regulatory deferral account balances should not be presented as part of the total deferred tax asset (liability) required by IAS 12, but either: • as part of the related regulatory deferral account balances; or • as a separate line item alongside the related regulatory deferral account balance. Similarly, movements in deferred tax assets and deferred tax liabilities related to regulatory deferral account balances should not be presented as part of the tax expense (income) line items in the income statement or statement of other comprehensive income required by IAS 12, but either: • as part of the movements in regulatory deferral account balances; or • as a separate line item alongside the related line items presented for movements in regulatory deferral account balances.
IAS 33 *Earnings per Share*	For each EPS amount presented, additional measures of basic and diluted EPS to be presented which exclude the net movements in the regulatory deferral account balances.
IAS 36 *Impairment of Assets*	The entity's previous GAAP accounting policies are applied to identify, recognise, measure and reverse any impairment of its recognised regulatory deferral account balances. However, for a cash-generating unit (CGU) that includes regulatory deferral account balances, the requirements of IAS 36 apply to that CGU. An entity should apply the guidance in IAS 36 to determine whether the regulatory deferral account balances form part of the carrying amount of the CGU for impairment purposes. If an impairment loss is identified for the CGU, it should be recognised in accordance with IAS 36.

Standard	Application
IFRS 3 *Business Combinations*	If an entity applying IFRS 14 acquires a business, the acquirer should apply its previous GAAP accounting policies for the recognition and measurement of regulatory deferral account balances to the acquiree's regulatory deferral account balances at the date of acquisition. The acquiree's regulatory deferral account balances should be recognised in the consolidated financial statements, regardless of whether the acquiree recognised those balances in its own financial statements. However, if an acquirer does not recognise regulatory deferral account balances and subsequently acquires a subsidiary that does, the acquirer is not eligible to apply IFRS 14.
IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*	Measurement requirements of IFRS 5 do not apply to regulatory deferral account balances. Where a discontinued operation includes a rate-regulated activity, the movements in the regulatory deferral account balances are not included as part of the line items required under IFRS 5. Instead, movements in regulatory deferral account balances related to the discontinued operation are presented in the income statement either: • as part of the movements in regulatory deferral account balances; or • as a separate line item alongside the related line item presented for other movements in regulatory deferral account balances related to profit or loss. Similarly, if a disposal group includes regulatory deferral account balances, those balances should not be included in the line items required by IFRS 5. Instead, the regulatory deferral account balances that form part of the disposal group should be presented either: • as part of the regulatory deferral account balances; or • as a separate line item alongside the other related regulatory deferral account balances.
IFRS 10 *Consolidated Financial Statements*	If a parent recognises regulatory deferral account balances under IFRS 14 in its consolidated financial statements, the same accounting policies should be applied to the regulatory deferral account balances of all of its subsidiaries. This is irrespective of whether the subsidiaries recognise such balances in their own financial statements.
IAS 28 *Investments in Associates and Joint Ventures*	For investments accounted for using the equity method, an investor that recognises regulatory deferral account balances under IFRS 14 should apply the same accounting policies to regulatory deferral account balances of its associates and joint ventures when applying the equity method. This is irrespective of whether the associate or joint venture recognises such balances in their own financial statements.
IFRS 12 *Disclosure of Interests in Other Entities*	Additional disclosures are required: • net movements in regulatory deferral account balances included in the profit or loss allocated to the non-controlling interest for each of an entity's subsidiaries with material non-controlling interests; • total regulatory deferral debit balances, regulatory deferral credit balances and the net movements in those balances, split between amounts recognised in profit or loss and in other comprehensive income, for all those entities for which summarised financial information is required to be disclosed under IFRS 12 (i.e. each subsidiary with material non-controlling interests, each material joint venture and in aggregate for all other joint ventures, each material associate and in aggregate for all other associates); and • the portion of the gain or loss recognised on the loss of control of a subsidiary that is attributable to derecognising regulatory deferral account balances of that subsidiary.

How are regulatory deferral account balances presented?

An entity applying IFRS 14 is required to present separate line items for regulatory deferral account debit balances and regulatory deferral account credit balances. Regulatory deferral account balances should not be classified as current or non-current. Instead, they are presented after a sub-total for total assets (total liabilities) before regulatory deferral account balances, followed by a total for assets (liabilities) and regulatory deferral account debit (credit) balances.

To illustrate, the asset section of the statement of financial position may be presented in the following manner, with a similar presentation for liabilities.

Non-current assets	xxx
Current assets	xxx
Total assets	xxx
Regulatory deferral account debit balances	xxx
Deferred tax asset related to regulatory deferral account balances*	xxx
Total assets and regulatory deferral account debit balances	xxx

* The related deferred tax asset may also be presented within the regulatory deferral account debit balances line item.

The net movement in regulatory deferral account balances in the period that relate to items recognised in other comprehensive income should be presented separately in the statement of other comprehensive income. Separate line items are required for the net movement that will subsequently be reclassified to profit or loss (i.e. "recycled") and the net movement which will not be subsequently reclassified.

The remaining net movement in regulatory deferral account balances (excluding movements not reflected in profit or loss such as acquisitions) should be presented as a separate line item in profit or loss. A sub-total of income and expenses before the net movement in regulatory deferral account balances should be presented.

To illustrate, the income statement may be presented in the following manner.

Revenue	xxx
Cost of sales	(xxx)
Gross profit	xxx
Other income	xxx
Distribution costs	(xxx)
Administrative expenses	(xxx)
Other expenses	(xxx)
Finance costs	(xxx)
Profit before tax	xxx
Income tax expense	(xxx)
Profit for the year before net movement on regulatory deferral account balances	xxx
Net movement in regulatory deferral account balances related to profit or loss	xxx
Net movement in deferred tax arising from regulatory deferral account balances related to profit or loss*	(xxx)
Profit for the year and net movement in regulatory deferral account balances	xxx

* The related deferred tax movement may also be presented within the net movement in regulatory deferral account balances line item.

What additional disclosures are required by IFRS 14?

The table above includes additional disclosures required by IFRS 14 for entities applying IAS 33 and IFRS 12.

In addition, IFRS 14 contains specific disclosure requirements to enable users to evaluate the nature of, and the risks associated with, each type of rate-regulated activity and the effects of the rate regulation on the financial position, financial performance and cash flows of the entity. These disclosures include:

- explanation of each type of rate-regulated activity;
- reconciliations of the carrying amount at the beginning and end of the period for each class of regulatory deferral account balance;
- the rate of return or discount rate used to reflect the time value of money applicable to each class of regulatory deferral account balance; and
- the remaining periods over which the entity expects to recover (or amortise) the carrying amount of each class of regulatory deferral account debit balance or reverse each class of regulatory deferral account credit balance.

Observation

The overarching principle that underlies the presentation and disclosure requirements is that the effects of continuing to apply rate-regulated accounting on a basis consistent with previous GAAP are shown separately from the assets, liabilities and results of other activities in the financial statements. The separate presentation of regulatory deferral account balances and movements therein will enhance comparability with the financial statements of rate-regulated entities that are not eligible, or choose not, to apply the new Standard as well as with entities without rate-regulated activities.

When do the new requirements apply?

IFRS 14 can be applied if an entity's first annual IFRS financial statements are for a period beginning on or after 1 January 2016. Earlier application is permitted.

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