



The Institute of
Chartered Accountants
of Pakistan

CA
PAKISTAN

HEAD OFFICE

Circular No. 11/2018

August 28, 2018

ALL MEMBERS OF THE INSTITUTE

Dear Member

Request for comments on IFRS 14, *Regulatory Deferral Accounts*

In 2014, the International Accounting Standards Board (IASB) issued IFRS 14, *Regulatory Deferral Accounts*. IASB issued IFRS 14 as an interim standard, with a plan to develop and issue a final standard outlining a comprehensive accounting model of rate-regulated activities. However, until the development of new accounting model by IASB the current issue of IFRS 14 will be applicable.

The Accounting Standards Board (ASB) has started the due process for recommending the adoption of IFRS 14. In this regard, stakeholder feedback is a critical input to the ASB's due process for recommending the adoption of an IFRS in Pakistan.

In this context, ASB requests for your comments on the adoption of IFRS 14, in line with its policy to consider and safeguard the public interest and analyse eventual impact of IFRS 14 on the financial reporting and business processes of rate-regulated companies across various sectors.

Snapshot of IFRS 14

Before explaining the scope, accounting and reporting requirements of IFRS 14, it is of foremost importance to understand what the rate regulation is and why it is necessary. Below paragraphs, summarize some of the basic features of rate-regulatory business environment.

Rate regulatory environment

Who regulates - The government regulates the supply and pricing of particular types of goods and services by entities.

What is regulated - The 'rate-regulated activities' usually involve providing goods and services that are considered in that jurisdiction to be essential to the citizens (i.e. customers), including utilities such as gas, electricity and water.

Therefore, in a rate-regulatory structure three significant stakeholders include the Rate regulator, Rate-Regulated entity and Entity's customer.

Why rate is regulated - The rate regulator not only regulates the rate per unit to be charged to customers for the rate-regulated goods or services, but also regulates the activities that the entity must perform and regulates the quality and profitability of those activities.

On one hand the objective of these rate regulation activities are to protect the entity's financial viability for the well-being of customers because it facilitates continuing investment in the infrastructure and other resources used to supply the rate-regulated goods and service. On the other hand, rate regulation is also designed to protect the interests of customers by ensuring quality, quantity and availability of supply along-with stability and affordability of prices.

(Established under the Chartered Accountants Ordinance, 1961 - X of 1961)

Chartered Accountants Avenue, Clifton, Karachi-75600 (Pakistan). Ph: (92-21) 111-000-422, Fax: 99251626

Website: www.icap.org.pk, E-mail: info@icap.org.pk



Regulatory agreements/regulations are often designed to allow the suppliers to recover specified costs and to earn a specified amount of consideration through the rates (that is, the prices or tariffs) they charge to customers. As a result, the rate regulator may allow the entity to recover specified costs by increasing rates charged to customers, but may spread the rate increase over a period to dampen rate fluctuations for customers. The rate regulator may also provide a financing return to the entity as compensation for the deferral. The rate-regulated entities, for regulatory purposes, usually keep track of these deferred and other specified amounts in separate regulatory deferral accounts until they are recovered through future sales of the regulated goods or services.

Why rate regulatory accounting is necessary - The rate regulation may affect not only the amount of revenue and profit that a rate-regulated entity can earn, but also the timing of the cash flows associated with the entity's rate-regulated activities. The timing may be affected because, when establishing the rate to be charged to customers, the rate regulator attributes some costs (or income) to a period other than the period in which those costs (or income) would normally be recognised in profit or loss for financial reporting purposes. Consequently, differences arise between amounts recognised as assets, liabilities, income and expense using regulatory accounting requirements compared to the amounts recognised using accounting policies established in accordance with IFRS.

The rate-regulated entity accounts for revenue from the customer in accordance with IFRS 15 *Revenue from Contracts with Customers* (previously IAS 18, *Revenue*). However, the relationship between the rate-regulator and rate-regulated entity is the focus of IFRS 14, as no other IFRS covers the impact of timing difference of above explained regulatory accounting.

IFRS 14

What IFRS 14 outlines - IFRS 14 prescribes special accounting for the effects of rate regulation. Except for IFRS 14 there is no specific guidance in IFRS about how to account for the balances in the regulatory deferral accounts.

Under the grandfathering approach of IFRS 14, rate-regulated entities that adopt IFRSs for the first time are permitted to continue the existing accounting policies to the recognition, measurement, and impairment and derecognition of regulatory deferral account balances.

Who could be impacted - IFRS 14 scopes in those entities that are first time adopters of IFRSs, conduct rate-regulated activities and have recognised regulatory deferral account balances under their previous local GAAP.

On the adoption of IFRS 14, you are requested to send your views, if any, to the Technical Services Department at dtscomments@icap.org.pk latest by September 28, 2018.

Yours truly

Sohail Malik
Director Technical Services