accounting guideline AcG-19 disclosures by entities subject to rate regulation

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PURPOSE AND SCOPE

1 This Guideline presents the views of the Accounting Standards Board on certain aspects of the disclosure and presentation of information in the financial statements of entities providing services or products for which customer rates are established, or subject to approval, by a regulator or a governing body empowered by statute or contract to set rates. The purpose is to ensure that financial statement users are better informed about the existence, nature and effects of all forms of rate regulation.

2 The requirements in this Guideline supplement those found elsewhere in Part II of the Handbook, as they pertain to rate-regulated operations.

3 This Guideline does not address recognition and measurement issues associated with the accounting for rate-regulated operations, and applies regardless of the accounting policies selected by an entity for its rate-regulated operations.

DISCLOSURE

Principles

4 Rate regulation can affect both the revenue-generating ability of an entity and the period in which its revenues are earned. In certain circumstances, it may result in the creation of material economic benefits and obligations. Therefore, it is an important consideration in evaluating the financial performance of entities with rate-regulated operations.

5 To meet the needs of financial statement users, entities subject to rate regulation shall disclose general information facilitating an understanding of the nature of the rate regulation and its effects on the entity's financial statements. The information shall be presented in such a manner as to enable a clear understanding of these effects.

General information on rate regulation

6 An entity subject to rate regulation shall disclose the following:

(a) the fact that the entity is subject to rate regulation, and a description of the nature and extent of the rate-regulated operations; and

(b) for each set of operations subject to a different rate-setting authority or type of regulation, the identity of the rate-setting authority and, if it meets the definition of a related party (see RELATED PARTY TRANSACTIONS, Section 3840), a statement to this effect, together with an explanation of why this is the case.

Additional information on the financial statement effects of rate regulation

7 When rate regulation has caused an entity to account for a transaction or event differently than it would have in the absence of rate regulation, the entity shall disclose the following:

(a) the specific financial statement items affected;

(b) for each item, how it has been reflected in the financial statements, as well as the rationale for this treatment, including information about either the supporting regulatory action (for example, issuance of a final rate order or approval to accumulate amounts pending final disposition at a later date, with the date being disclosed when known), or the expectations of the entity regarding future regulatory actions; and

(c) when a separate asset or liability has been recognized solely as a result of the effects of rate regulation:

(i) the carrying amount of the asset or liability, as at the most recent balance sheet date, and the balance sheet line item that includes it when it is not otherwise evident;

(ii) the income statement effect of such recognition for the current period;

(iii) the remaining period over which the carrying amount of the asset is expected to be recovered or the liability is expected to be settled;

(iv) a description of the regulatory risks and uncertainties affecting the eventual recovery of the asset or settlement of the liability and its timing, consistent with MEASUREMENT UNCERTAINTY, Section 1508; and

(v) when the regulator does not include a return on investment in the rate base for the asset during its recovery period, a statement to that effect; and

(d) when accounting for the effects of rate regulation has been discontinued since the last financial statements issued, a statement to that effect, together with the reasons for the discontinuance and identification of the rate-regulated operations affected.

8 The financial statement note providing the information required by paragraph 7(a) shall make reference to any other note containing the information required by paragraphs 7(b)-(c).

PRESENTATION

9 Assets and liabilities, including those recognized as a result of the effects of rate regulation, shall be offset only when specifically permitted or required by another Section or Guideline.

EFFECTIVE DATE

10 This Guideline applies to annual financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier application is permitted.

ILLUSTRATIVE EXAMPLE

This material is illustrative only.

This example illustrates how certain of the disclosure requirements specified in this Guideline might be applied in a particular situation. Matters of principle relating to particular situations should be decided in the context of this Guideline.

The example relates only to the requirements of paragraph 7 of the Guideline. It does not show the disclosures required by the remainder of the Guideline, or other disclosures required by generally accepted accounting principles. The financial statement items included in the example are particularly relevant to utilities in the gas or electricity industries. However, since the primary purpose of the example is to illustrate the extent of the disclosures required by the Guideline, and to indicate how a tabular format may be used, it has relevance for all entities subject to rate regulation.

RRO Inc.
Notes to the Consolidated Financial Statements (extract)

Note X: Financial statement effects of rate regulation

The following describes each of the circumstances in which rate regulation affects the accounting for a transaction or event. Regulatory assets represent future revenues associated with certain costs, incurred in the current period or in prior periods, that are expected to be recovered from customers in future periods through the rate-setting process. Regulatory liabilities represent future reductions or limitations of increases in revenues associated with amounts that are expected to be refunded to customers as a result of the rate-setting process.

Regulatory assets and liability

	20X2	20X1	Remaining recovery / settlement period (years)
Year ended December 31 ($ millions)			
Regulatory assets			
Recoverable losses on debt retired prior to maturity	$ 11	$ 8	14-20
Recoverable storm costs (a)	5	—	5
Purchased power cost variance	—	37	N/A
Total regulatory assets	$ 16	$ 45	

Regulatory liability			
Purchased power cost variance	26	—	1
Total regulatory liability	$ 26	—	
	===	===	

(a) The rate base does not include an allowance for a return on investment for this item.

As prescribed by a regulatory rate order, gains and losses on debt retired prior to the date of maturity are included in allowed rates on a gradual basis, over the period from the retirement date to the original maturity date of the debt. Since it is expected that the long-term application of this regulatory policy will result in these gains and losses being refunded or recovered through customer rates in their entirety, they are recognized as a regulatory liability or asset in the year the debt is retired, with a corresponding charge or credit to income. The regulatory liability or asset is amortized and included in operating results on an annuity basis over the same period as that approved for rate-setting purposes. In 20X2, $3 million (20X1 — $4 million) in losses on debt retired prior to the date of maturity was recognized as a regulatory asset, and the amortization of previously capitalized amounts totalled $1 million (20X1 — $1 million). The regulatory asset is presented net of accumulated amortization as at December 31, and is included in recoverable debt costs.

In 20X2, RRO Inc. incurred storm costs amounting to $5 million. The regulator has issued an order requiring the exclusion of these costs from the determination of customer rates until their final rate treatment is decided in the next rate hearing (scheduled for 20X3). The Company intends to seek, and expects to receive, approval for recovery of the costs through future rates over a five-year period commencing in 20X3. Accordingly, the costs have been recognized as a regulatory asset to be amortized over the same period. The regulatory asset is included in other recoverable costs.

Purchased power costs are included in allowed rates on a forecast basis. For rate-setting purposes, differences between forecast and actual purchased power costs in the rate year are held until the following year, when their final disposition is decided. RRO Inc. recognizes purchased power cost variances as a regulatory asset or liability, based on the expectation that amounts held from one year to the next for rate-setting purposes will be approved for collection from, or refund to, future customers. The regulatory liability (20X1 — asset) represents the excess of forecast over actual (20X1 — actual over forecast) purchased power costs. The regulatory liability (20X1 — asset) is included in refundable purchased power charges (20X1 — recoverable purchased power costs).

For certain of the regulatory items identified above, the expected recovery or settlement period, or likelihood of recovery or settlement, is affected by risks and uncertainties relating to the ultimate authority of the regulator in determining the item's treatment for rate-setting purposes. For example, RRO Inc.'s treatment of purchased power costs is dependent on the continued use of an automatic adjustment mechanism for regulatory purposes, and would require reconsideration if the regulator decided to discontinue the use of this mechanism or require the Company to absorb cost variances in a particular year. Similarly, there is a risk that the regulator may disallow a portion of the storm costs incurred in 20X2 for recovery through future rates, or disagree with the proposed recovery period.

Other items affected by rate regulation

The regulator permits an allowance for funds used during construction (AFUDC), based on RRO Inc.'s weighted average cost of capital, to be included in the rate base. AFUDC is also included in the cost of property, plant and equipment for financial reporting purposes, and is depreciated over future periods as part of the total cost of the related asset, based on the expectation that depreciation expense, including the AFUDC component, will be approved for inclusion in future customer rates. Since AFUDC includes not only an interest component, but also a cost-of-equity component, it exceeds the amount allowed to be capitalized in similar circumstances in the absence of rate regulation.

This compilation reproduces all of the specific disclosure requirements contained in accounting standards for private enterprises set out in Part II of the CPA Canada Handbook – Accounting.

This compilation is not an exhaustive list of all disclosures that might be required for fair presentation in accordance with generally accepted accounting principles. Fair presentation is discussed in GENERAL STANDARDS OF FINANCIAL STATEMENT PRESENTATION, paragraph 1400.04, as follows:

A fair presentation in accordance with generally accepted accounting principles is achieved by:

(a) applying GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100;

(b) providing sufficient information about transactions or events having an effect on the entity's financial position, results of operations and cash flows for the periods presented that are of such size, nature and incidence that their disclosure is necessary to understand that effect; and

(c) providing information in a manner that is clear and understandable.

Accordingly, this compilation cannot be used as a checklist to determine if all necessary disclosures have been made in a set of financial statements.

Disclosure requirements are commonly satisfied by inclusion of information in the notes to the financial statements but may also be satisfied, when considered appropriate, by inclusion in the income statement, balance sheet or cash flow statement.

Disclosure of information that is not material to the financial statements is not required.