

# Rule 026

## Rule Regarding Regulatory Account Procedures Pertaining to the Implementation of the International Financial Reporting Standards

This rule as amended was approved by the Alberta Utilities Commission on December 6, 2011, and is effective on December 20, 2011.

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### Contents

1	Definitions .....	2
2	Application.....	3
3	Guiding principles.....	4
4	Expected regulatory accounting disclosure.....	4
5	IFRS initial adoption adjustments (IFRS 1).....	4
6	Specific regulatory accounting items.....	5
	Appendix 1 – Guiding principles .....	10
	Appendix 2 – Notes .....	11

## 1 Definitions

In this rule,

- (a) “existing accounting practice” means the accounting procedures and policies in use by a utility, that have been approved by the Commission for rate-making purposes, immediately prior to the adoption of this rule
- (b) “existing Canadian GAAP” means the widely accepted set of rules, conventions, standards, and procedures for reporting financial information, as established by the Canadian Accounting Standards Board
- (c) “first IFRS-compliant GRA/GTA” means the first general rate application/general tariff application filed by a utility which includes the utility’s IFRS adoption date in the forecast test period
- (d) “IAS” or “International Accounting Standards” refers to the standards issued by the International Accounting Standards Committee from 1973 to 2000, when it was replaced by the International Accounting Standards Board (IASB), and as amended or replaced by the IASB
- (e) “IASB” or “International Accounting Standards Board” is the independent standard-setting body of the International Accounting Standards Committee Foundation
- (f) “IFRIC” means the International Financial Reporting Interpretations Committee; the interpretative body of the International Accounting Standards Committee Foundation
- (g) “IFRS” means the entire body of IASB pronouncements, including standards and interpretations approved by the IASB, and the IAS and Standing Interpretations Committee Interpretations approved by the predecessor International Accounting Standards Committee
- (h) “IFRS adoption date” means the date by which a utility determines it shall adopt IFRS as the basis of its forecast - either January 1, 2010, January 1, 2011, or January 1, 2012; for the filing of actual results, all utilities adopting IFRS are required to file using IFRS effective either January 1, 2011 or January 1, 2012, in accordance with Section 2(4)
- (i) “regulatory accounting” means the collective accounting guidelines, procedures, policies, and practices used by utilities when providing financial information to the AUC for rate-making purposes
- (j) “regulatory assets and liabilities” are assets and liabilities that result from rate actions of regulatory agencies. For the purposes of this rule, regulatory assets and liabilities can specifically result from rate regulation as follows:

- (i) regulatory assets arise when the regulator has previously ruled that certain previously incurred costs will be collected from customers either directly or through rates in a future period,<sup>1</sup> and
- (ii) regulatory liabilities arise when a utility collects from customers in rates amounts that the regulator has previously ruled must be refunded to customers either directly or through rates in a future period or that are intended to cover costs to be incurred in the future<sup>2</sup>

For the purposes of this definition, the term “costs” can include revenue shortfall, expenses, and gains and losses on sale of assets.<sup>3</sup>

- (k) “uniform system of accounts” means the system of accounts to be filed by an electric utility as set out in Decision 2007-017,<sup>4</sup> or by a gas utility as set out in Alberta Regulation 546/63 (*Uniform Classification of Accounts for Gas Utilities*)
- (l) “utility” or “utilities” means all Commission-regulated electric utilities and gas utilities, and includes regulated rate providers and default supply providers

## **2 Application**

- (1) Subject to subsection (3), this rule applies to all utilities.
- (2) Utilities have filed letters with the AUC indicating whether or not they will be adopting IFRS. Utilities adopting IFRS have also indicated what their IFRS adoption date will be.
- (3) Utilities that indicated that they are not adopting IFRS have also indicated the reasons why they are not subject to IFRS.
- (4) Utilities that indicated to the Commission under subsection (2) that they will be adopting IFRS shall adhere to the following schedule:

<b>Fiscal year</b>	<b>Year filed</b>	<b>Actual / forecast</b>	<b>Accounting/reporting standard to use</b>
2011	2012	Actual	For utilities that have adopted IFRS effective January 1, 2011 - this rule is to be followed for regulatory filings with the AUC, complete with 2010 comparatives prepared using this rule; IFRS is to be used for financial statements, including 2010 comparatives prepared under IFRS  For utilities adopting IFRS effective January 1, 2012 – existing accounting practice is to be followed for regulatory filings with the AUC; existing Canadian GAAP is to be used for financial statements
2012 & beyond	2013 & beyond	Actual	This rule is to be followed for regulatory filings with the AUC, complete with prior year comparatives prepared using this rule; IFRS is to be followed for financial statements, including prior year comparatives prepared under IFRS
2012 (first year in test period) & beyond	2011 & beyond	Forecast	This rule is to be used for forecasts filed with the AUC

### **3 Guiding principles**

The guiding principles in Appendix 1 will be used when considering any proposed changes to the existing provisions of this rule or when developing and establishing any new provisions to this rule.

### **4 Expected regulatory accounting disclosure**

For greater clarity, the applicable IFRS, IAS or IFRIC reference is provided for each following sections or subsections.

### **5 IFRS initial adoption adjustments (IFRS 1)**

Utilities shall disclose each IFRS adoption adjustment separately if the adjustment has an impact on a regulatory account. These adjustments shall be included in a utility's first IFRS-compliant GRA/GTA, along with the utility's proposal for the method for settling each adjustment.<sup>5</sup>

## 6 Specific regulatory accounting items

### (1) Regulatory assets and liabilities: deferral accounts

Utilities shall maintain the existing practice of applying to the Commission for approval of any deferral accounts that may be required for the purpose of establishing regulatory assets and liabilities and proposing the mechanism for their disposition.<sup>6</sup>

### (2) Property, plant and equipment

#### (a) Revaluation option (IAS 16.31-16.42)

Utilities shall maintain the existing accounting practice of using historical costs to record property, plant and equipment accounts.

#### (b) Capitalization/non-capitalization of costs: general and administrative overhead (IAS 16.16 and 16.19(d))

Utilities shall adhere to the IFRS requirements for capitalization of costs that are not directly attributable to an asset.<sup>7</sup> Any financial difference that arises as a result of the adoption of the IFRS requirements is to be identified in a utility's first IFRS-compliant GRA/GTA, and the utility shall also propose in that rate application the method for settling the difference.<sup>8</sup> In addition, the utility will file a copy of its updated capitalization policy as a part of its first IFRS-compliant GRA/GTA.<sup>9</sup>

#### (c) Capitalization/non-capitalization of costs: borrowing costs/equity allowance for funds used during construction (AFUDC) (IAS 23)

(i) Subject to subsection (ii), utilities shall maintain the existing accounting practice of including the debt and equity components of AFUDC when accounting for construction work in progress and plant in service.

(ii) Utilities may submit an application to the AUC requesting approval to make their regulatory accounting practice the same as the practice under IFRS.<sup>10</sup>

#### (d) Capitalization/non-capitalization of costs: depreciation of assets used in the construction of other assets (IAS 16.48-16.49)

Utilities shall adhere to the IFRS requirement of capitalizing the depreciation of assets used in the construction of other assets.

- (e) Capitalization/non-capitalization of costs: asset relocation costs (IAS 6.20(c))

Utilities shall adhere to the IFRS requirements regarding the treatment of asset relocation costs.<sup>11</sup> Any financial difference that arises as a result of the adoption of the IFRS requirements is to be identified in a utility's first IFRS-compliant GRA/GTA. The utility shall also propose in that rate application the method for settling the difference.<sup>12</sup> In addition, the utility shall file a copy of its updated capitalization policy as a part of its first IFRS-compliant GRA/GTA.<sup>13</sup>

- (f) Capitalization/non-capitalization of costs: pre-operating costs (IAS 16.19, 16.20 (a) and 16.20(b))

Utilities shall adhere to the IFRS requirements regarding the treatment of pre-operating costs.<sup>14</sup> Any financial difference that arises as a result of the adoption of the IFRS requirements is to be identified in a utility's first IFRS-compliant GRA/GTA. The utility shall propose in that rate application the method for settling the difference.<sup>15</sup> In addition, the utility shall file a copy of its updated capitalization policy as a part of its first IFRS-compliant GRA/GTA.<sup>16</sup>

- (g) Capitalization/non-capitalization of costs: training costs (IAS 16.19 (c))

Utilities shall adhere to the IFRS requirements regarding the capitalization of training costs.<sup>17</sup> Any financial difference that arises as a result of the adoption of the IFRS requirements is to be identified in a utility's first IFRS-compliant GRA/GTA. The utility will propose in that rate application the method for settling the difference.<sup>18</sup> In addition, the utility will file a copy of its updated capitalization policy as a part of its first IFRS-compliant GRA/GTA.<sup>19</sup>

- (h) Capitalization/non-capitalization of costs: asset commissioning costs (IAS 16)

Utilities shall adhere to the IFRS requirements regarding the treatment of asset commissioning costs.<sup>20</sup> Any financial difference that arises as a result of the adoption of the IFRS requirements is to be identified in a utility's first IFRS-compliant GRA/GTA. The utility will propose in that rate application the method for settling the difference.<sup>21</sup> In addition, the utility will file a copy of its updated capitalization policy as a part of its first IFRS-compliant GRA/GTA.<sup>22</sup>

- (i) Treatment of gains and losses upon retirement or disposal of assets (IAS 16.68)

Utilities shall maintain the existing accounting practice of recording gains and losses upon retirement or disposal of assets. Utilities shall identify and

record any difference in accounting between the IFRS reporting requirements and these regulatory reporting requirements in a separate subsidiary accumulated depreciation account.

- (j) Componentization: tracking, depreciation rates, commencement of depreciation (IAS 16.43-16.62)
  - (i) Depreciation rates
    - (A) Subject to subsection (B), utilities shall continue to use the depreciation rates utilized under the existing accounting practice.
    - (B) If the adoption of the IFRS requirements for external financial reporting results in depreciation rates that differ from existing accounting practice or results in a difference in the timing of commencement of depreciation, or both, then a utility may, by way of application to the AUC, request approval to account for regulatory depreciation in accordance with IFRS.<sup>23</sup>
  - (ii) Componentization of major overhauls

Utilities shall adhere to the IFRS requirements regarding the depreciation treatment of major overhauls.<sup>24</sup> Any financial difference that arises as a result of the adoption of the IFRS requirements is to be identified in a utility's first IFRS-compliant GRA/GTA. The utility will propose in that rate application the method for settling the difference.<sup>25</sup> In addition, the utility will file a copy of its updated capitalization policy as a part of its first IFRS-compliant GRA/GTA.<sup>26</sup>
  - (iii) Componentization
    - (A) Subject to subsection (B), with respect to componentization, utilities shall record assets at the level of detail being reported under the existing accounting practice.
    - (B) If the adoption of IFRS requirements for external financial reporting results in a different level of componentization, then a utility may, by way of application to the AUC, request approval to account for regulatory componentization in accordance with IFRS.<sup>27</sup>
- (k) Asset retirement obligations/future removal and site restoration costs (IAS 16.16(c), 16.18 and IAS 37)

- (i) Subject to subsection (ii), utilities shall maintain the existing accounting practice regarding the treatment of asset retirement obligations and future removal and site restoration costs.
- (ii) Utilities may, by way of application to the AUC, request approval to account for asset retirement obligations and future removal and site restoration costs in accordance with IFRS.<sup>28</sup>

(l) Treatment of insurance proceeds (IAS 16.65-16.66)

Utilities shall identify any insurance proceeds received for a loss of an asset and record these in a separate deferral account.<sup>29</sup> Utilities shall propose in their first IFRS-compliant GRA/GTA the method for settling the deferral account.<sup>30</sup>

(m) Impairment of assets (IAS 16.63 and IAS 36)

Utilities shall maintain the existing accounting practice of having no impairment (or impairment reversal) charges included when providing or reporting financial information to the AUC.

(n) Deemed finance leases (IAS 17)

Utilities shall maintain the existing accounting practice regarding the treatment of deemed finance leases.

(o) Capital inventories (IAS 2 and IAS 16)

- (i) Subject to subsection (ii), utilities shall maintain the existing accounting practice of recognizing capital inventory and any associated depreciation.<sup>31</sup>
- (ii) If the adoption of the IFRS requirements for external financial reporting results in depreciation rates that differ from existing accounting practice or results in a difference in the timing of commencement of depreciation, or both, then a utility may, by way of application to the AUC, request approval to account for regulatory depreciation in accordance with IFRS.<sup>32</sup>

(p) Treatment of customer contributions (IFRIC 18)

Utilities shall maintain the existing accounting practice of recognizing customer contributions in their property, plant and equipment accounts and including the amortization as an offset to depreciation.

**(3) Accounting method for income taxes (IAS 12)**

Utilities shall maintain the existing accounting practice for income taxes. Utilities shall include the future income tax regulatory asset or liability in their rate applications when necessary.<sup>33</sup>

**(4) Pension costs/other employment benefits (IAS 19)**

Utilities shall maintain the existing accounting practice of recognizing pension costs and other post-employment benefits. Utilities shall include the regulatory asset or liability associated with the pension costs and other post-employment benefits in their rate applications when necessary.<sup>34</sup>

**(5) Intangible assets (IAS 38)**

Utilities shall maintain the existing accounting practice of recognizing intangible assets as part of their property, plant and equipment accounts.<sup>35</sup>

**(6) Debt transaction costs (IAS 23)**

(a) Subject to subsection (b), utilities shall maintain the existing accounting practice for amortizing debt costs.

(b) Utilities may, by way of application to the AUC, request approval to account for debt transaction costs in regulatory applications in accordance with IFRS.<sup>36</sup>

**(7) Discount rate**

Utilities shall maintain the existing accounting practice of having no impairment (or impairment reversal) charges included when determining rates.<sup>37</sup>

**(8) Reserves for general damages and self insurance**

Utilities shall maintain the existing accounting practice regarding the treatment of reserves for general damage and self insurance.

**(9) Business combinations (IFRS 3)**

Utilities shall maintain the existing accounting practice regarding the treatment of business combinations.

## Appendix 1 – Guiding principles

These guiding principles are all equally important and are to be viewed as a collective set of principles rather than a list of individual statements.

- The methodologies used by the AUC to establish just and reasonable rates have not always been the same as those used for external financial reporting purposes. The Commission has and will retain the authority to establish regulatory accounting and regulatory reporting requirements and as such, IFRS requirements will not be the sole driver of regulatory requirements.
- Future regulatory accounting and regulatory reporting requirements established by the Commission will continue to be based on historical, sound regulatory principles. Examples of these principles can be found in statutes, regulatory and court decisions and regulatory texts and include intergenerational equity, minimizing rate volatility and use of historical costs rather than fair market, or any other values.
- Future regulatory accounting and regulatory reporting requirements established by the Commission will, in considering IFRS requirements, balance the effects on customer rates and shareholders' return. Any shifting of risk between customers and shareholders will be minimized.
- Future regulatory accounting and regulatory reporting requirements established by the Commission will be aligned as much as possible with IFRS. In establishing any future regulatory accounting and regulatory reporting requirements that deviate from IFRS, the Commission will ensure that any such deviations and their impact are in the public interest.
- Future regulatory accounting and regulatory reporting requirements established by the Commission will be universal and standardized for all utilities while still recognizing that utility-specific issues can be addressed through that utility's applications.

## Appendix 2 – Notes

### These notes have been included for informational purposes only

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- <sup>1</sup> This can arise from the timing of collection of certain expenses in rates charged to customers that differs from the period in which the expense would be recognized under IFRS by companies that are not subject to rate regulation.
  - <sup>2</sup> This can occur if costs are below a previously approved forecast or if they are collected from customers in a period before they are incurred. This can also arise when the revenue is recognized in a period that is different from the period that it would be recognized under IFRS by companies that are not subject to rate regulation;
  - <sup>3</sup> Regulatory assets and liabilities can arise from the approval by the regulator of a specific deferral account or the approval of a methodology for recovering costs such as using the cash method to recover income taxes and post employment benefit costs.
  - <sup>4</sup> Decision 2007-017: EUB Proceeding, Implementation of the Uniform System of Accounts and Minimum Filing Requirements for Alberta’s Electric Transmission and Distribution Utilities, Application No. 1468565, March 6, 2007.
  - <sup>5</sup> For example, the establishment of a regulatory asset or liability.
  - <sup>6</sup> Regulatory deferral accounts will continue regardless of the IFRS reporting standards. The AUC will continue to determine the process that the utilities must follow in order to have their deferral accounts approved as well as the process to have the deferral accounts recovered in a timely and effective manner. The Commission will consider including wording in future decisions that the approved methodologies that gave rise to the regulatory asset or liability will continue into the future. This will provide evidence on the high probability, subject to future regulatory review as required, of the collection or payment of regulatory assets and liabilities that may help utilities to record these items in their financial statements.
  - <sup>7</sup> IFRS does not allow the capitalization of costs that are not “directly attributable” to the asset.
  - <sup>8</sup> For example, the establishment of a regulatory asset or liability.
  - <sup>9</sup> The AUC and interested parties will review these proposals and capitalization policies as part of the rate-making process.
  - <sup>10</sup> This request would be subject to review by the AUC and interested parties as part of the AUC’s decision-making process.
  - <sup>11</sup> Under IFRS, the installation cost in the new location can be capitalized as long as the costs in the old location are retired. The cost of actually relocating existing assets has to be expensed as it is deemed to not provide future economic benefit.
  - <sup>12</sup> For example, the establishment of a regulatory asset or liability.
  - <sup>13</sup> The AUC and interested parties will review these proposals and capitalization policies as part of the rate-making process.
  - <sup>14</sup> Certain pre-operating costs currently capitalized under generally accepted accounting principles would not be capitalized under IFRS.
  - <sup>15</sup> For example, the establishment of a regulatory asset or liability.
  - <sup>16</sup> The AUC and interested parties will review these proposals and capitalization policies as part of the rate-making process.

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- 17 Certain training costs currently capitalized would not be capitalized under IFRS or under the early adoption of IFRS for intangible assets in 2009.
- 18 For example, the establishment of a regulatory asset or liability.
- 19 The AUC and interested parties will review these proposals and capitalization policies as part of the rate-making process.
- 20 Certain asset commissioning costs currently capitalized under generally accepted accounting principles would not be capitalized under IFRS.
- 21 For example, the establishment of a regulatory asset or liability.
- 22 The AUC and interested parties will review these proposals and capitalization policies as part of the rate-making process.
- 23 These proposed depreciation rates would be subject to review by the AUC and interested parties as part of the AUC's regulatory process.
- 24 IFRS requires that expected major overhauls be estimated and separately componentized upon initial recognition of an asset. This portion of the asset's cost would then be depreciated over a different period of time than the related asset.
- 25 For example, the establishment of a regulatory asset or liability.
- 26 The AUC and interested parties will review these proposals and capitalization policies as part of the rate-making process.
- 27 Such request would be subject to review by the AUC and interested parties as part of the rate-making process.
- 28 Such request would be subject to review by the AUC and interested parties as part of the rate-making process.
- 29 Under IFRS, insurance proceeds are treated as income. Currently insurance proceeds received for a loss of an asset are considered proceeds of disposition with the resulting gain or loss going to accumulated depreciation.
- 30 The AUC and interested parties will review the proposal as part of the rate-making process.
- 31 Under IFRS, capital inventories will be classified as property, plant and equipment and amortized when available for use.
- 32 These proposed depreciation rates would be subject to review by the AUC and interested parties as part of the AUC's regulatory process.
- 33 This future income tax regulatory asset or liability will have no impact on the revenue requirement as it will be offset by the future income tax liability or asset.
- 34 This regulatory asset or liability will have no impact on the revenue requirement as it will be offset by the pension liability or asset.
- 35 Under IFRS, software development costs and land rights will be classified as intangible assets.
- 36 This request would be subject to review by the AUC and interested parties as part of the AUC's regulatory process.
- 37 Consequently, the issue of differing discount rates will not affect regulatory reporting.