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13 January 2015

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
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Dear Hans

Re: Comment on Discussion Paper DP/2014/2 *Reporting the Financial Effects of Rate Regulation*

1. The Accounting Standards Board of Japan ('ASBJ' or 'we') welcomes the opportunity to provide comments on the International Accounting Standards Board (IASB)'s Discussion Paper DP/2014/2 *Reporting the Financial Effects of Rate Regulation* (DP).

2. Overall, the ASBJ thinks the DP provides a very good starting point to consider whether, and if so, what kind of special accounting requirements should be developed for some types of rate regulated activities. In the following, the ASBJ would like to highlight its views on the following areas, as we considered them as the most important parts of the DP.

   (a) Scope of consideration;

   (b) Needs of special accounting requirements; and

   (c) Alternative approaches to consider.

3. Firstly, the ASBJ generally agrees with the proposal outlined in the DP that the IASB starts its consideration with a narrow scope (that is a 'defined rate regulation' as explained in the DP) albeit recognising the need for further improvements regarding some of its descriptions. The ASBJ thinks that a defined rate regulation is likely to give rise to unique rights and obligations that warrant consideration as to whether a combination of such rights and obligations should be recognised in the financial statements (thus having an economic effect). At the same time, the ASBJ found that very few rate regulatory schemes in Japan would meet the definition of a defined rate regulation.

4. Secondly, the ASBJ has not drawn a firm conclusion as to whether special accounting

requirements would be necessary to account for a combination of such rights and obligations in the financial statements. The ASBJ thinks that such rights and obligations are sufficiently distinct and that special accounting requirements would be necessary if the IASB determines that assets or liabilities should be recognised. The ASBJ also finds that it is very difficult to conclude that assets and liabilities should *not* be recognised for a combination of such rights and obligations, given the IASB's tentative decisions regarding the definitions of an asset and a liability and the threshold for recognition that are considered as part of the project of the *Conceptual Framework*.

5. However, the ASBJ does not believe that this would immediately conclude that assets and liabilities should be recognised for such rights and obligations. This is primarily because these tentative decisions may not be sufficiently precise to conclude that an asset or a liability should *not* be recognised, although they would work quite well in explaining why certain assets or liabilities need to be recognised. Furthermore, the ASBJ finds that users are relatively neutral as to whether an asset or a liability should be recognised, although they believe that information relevant to a rate regulation would be useful for users to assess the prospect for future cash inflows to an entity. Thus, the ASBJ is not sure if financial information would become more relevant and provide more faithful representation if assets or liabilities relating to rate regulatory schemes are recognised.

6. Lastly, the ASBJ does not support the following alternative approaches explained in the DP for the reasons stated in paragraphs 29 to 31 of this letter.

   (a) Recognising as an intangible asset the package of rights and obligations, or part of them, established by the regulatory arrangement;

   (b) Recognising as a financial asset or liability the package of rights and obligations; or

   (c) Reporting using the regulatory accounting requirements.

7. Of the possible remaining approaches, the ASBJ does not support the approach that requires or permits acceleration of recognising revenue from customers. The ASBJ thinks that revenue from customers should not be recognised before goods or services are provided to customers. In addition, it would be inappropriate to accelerate recognition of costs based on the projection of anticipated costs, primarily because the estimate would be too subjective. On the other hand, the ASBJ thinks that the approach requiring deferral of relevant costs or revenue or a combination of both are worthy of further consideration in parallel with considering whether to recognise a relevant asset and liability for a defined rate regulation, as long as the effect of rate regulation is clearly disclosed in the financial statements.

8. Based on the considerations stated in paragraphs 3 to 7 of this paper, the ASBJ thinks that viable approaches that the IASB may consider in deciding the next steps would be either of the following, focusing on a scope similar to a 'defined rate regulation':

   (a) An approach which requires recognising the effect of rate regulation using separate items for an asset or a liability as well as income or expenses while changes in the balances of an asset or a liability are recognised through profit or loss (either as a separate line item or as part of costs or revenue).

   (b) 'Disclosure-only' approach which would help users of financial reports to understand the effect of rate regulation (including the amount that is expected to be adjusted in the future operation of rate regulated entities).

9. Yet, as stated in paragraph 3 of this letter, the applicability of the project would be very limited in the context of Japanese circumstances if the IASB focused on a 'defined rate regulation. Taking into account the global trend to promote competition among rate regulated entities, the ASBJ wonders if it would also be the case in other jurisdictions. If this is the case, the ASBJ recommends that the IASB carefully assess whether further actions are justifiable or immediately necessary in light of balancing the benefits and the costs associated with standard-setting activity before formally launching the standard-setting process. Having considered the challenges that the ASBJ has observed on the project, the ASBJ believes that it would be appropriate to prioritize the 'disclosure-only' approach over the other.

10. For further details, please refer to specific comments on questions in the DP in the Appendix-I.

11. If you have any questions on any matters in the comment letter, please feel free to contact us.

Yours sincerely

Tomo Sekiguchi

Tomo Sekiguchi

Board member of the Accounting Standards Board of Japan

Appendix-I

Comments on Specific Questions in the DP

Question 1

(a) What information about the entity's rate-regulated activities and the rate-regulatory environment do you think preparers of financial statements need to include in their financial statements or accompanying documents such as management commentary? Please specify what information should be provided in: (i) the statement of financial position; (ii) the statement(s) of profit or loss and other comprehensive income; (iii) the statement of cash flows; (iv) the note disclosures; or (v) the management commentary. (b) How do you think that information would be used by investors and lenders in making investment and lending decisions?

12. When the ASBJ Staff reached out to users of financial reports, we were informed that it would, at a minimum, be helpful if a general description about the rate regulatory framework (which gives rise to the unique rights and obligations of entities operating under the framework) was disclosed somewhere in the financial reports. Yet users did not express preference as to whether that should be disclosed in financial statements or another part of the financial reports.

Question 2

Are you familiar with using financial statements that recognise regulatory deferral account balances as regulatory assets or regulatory liabilities, for example, in accordance with US generally accepted accounting principles (GAAP) or other local GAAP or in accordance with IFRS 14? If so, what problems, if any, does the recognition of such balances cause users of financial statements when evaluating investment or lending decisions in rate-regulated entities that recognise such balances compared to: (a) non-rate-regulated entities; and (b) rate-regulated entities that do not recognise such balances?

13. No. Under Japanese accounting standards, regulatory deferral account balances are not recognised as regulatory assets or regulatory liabilities. In addition, as for entities that may fall under the scope of the project, the ASBJ Staff found that very few securities

analysts compare financial statements prepared in accordance with different accounting standards. Thus, Japanese users are considered to have very little experience in using financial statements in which regulatory deferral assets and liabilities are recognised in the statements of financial condition.

Question 3

Do you agree that, to progress this project, the IASB should focus on a defined type of rate regulation (see Section 4) in order to provide a common starting point for a more focused discussion about whether rate regulation creates a combination of rights and obligations for which specific accounting guidance or requirements might need to be developed (see paragraphs 3.6–3.7)? If not, how do you suggest that the IASB should address the diversity in the types of rate regulation summarised in Section 3?

14. Yes. The ASBJ agrees that the IASB should focus on a defined type of rate regulation in order to perform analysis as to whether specific accounting guidance or requirement might need to be developed. The ASBJ suspects that starting with a broader scope would result in less efficient utilisation of resources both for the IASB Board and its Staff, because it is likely that the IASB would eventually have to segregate part of the scope, such that different sets of analyses would need to be performed.

15. Having said that, the ASBJ found that the applicability would be very limited in Japan if the IASB decides to establish specific accounting guidance or requirements for a defined rate regulation. This is primarily because rate regulated schemes in Japan do not usually have a mechanism to reverse specified differences between the amount of the revenue requirement accrued to date and the amounts billed to customers. Taking into account the global trend to promote competition among entities, the ASBJ wonders if it would also be the case in other jurisdictions. Thus, the ASBJ recommends that the IASB assess whether further actions are justifiable or immediately necessary in light of balancing benefits and the costs for associated standard-setting activity before formally launching the standard-setting process.

16. Nevertheless, the ASBJ would like to draw the IASB’s attention to the feedback received from general insurance companies when reaching out to our constituents. They noted that some insurance contracts are sufficiently distinct enough to require special accounting treatments, and suggested that the IASB broaden the scope of the project so as to include the particular type of contracts. Although the ASBJ has not necessarily gone through assessment as to whether this type of contracts should be addressed in the context of the

project, it would be valuable if the IASB examine real-life examples (including this one) when furthering the consideration regarding the focus of the discussion.

Question 4

Paragraph 2.11 notes that the IASB has not received requests for it to develop special accounting requirements for the form of limited or 'market' rate regulation that is used to supplement the inefficient competitive forces in the market (see paragraphs 3.30–3.33). (a) Do you agree that this type of rate regulation does not create a significantly different economic environment and, therefore, does not require any specific accounting requirements to be developed? If not, why not? (b) If you agree that this type of rate regulation does not require any specific accounting requirements, do you think that the IASB should, alternatively, consider developing specific disclosure requirements? If so, what would you propose and why?

17. The ASBJ agrees that special accounting requirements should not be developed for the form of limited or 'market' rate regulation that is used to supplement the inefficient competitive forces in the market.

18. In many jurisdictions (including Japan), rate regulatory schemes are increasingly of a limited or 'market' rate regulatory nature, and that many rate regulatory schemes would be outside the scope of the project unless the IASB broaden the scope of the project. However, the ASBJ does not think that the nature of such rate regulatory schemes would give rise to unique rights or obligations that are significantly different from an entity's activities that operate outside such regulatory schemes. Accordingly, the ASBJ does not think that such rate regulatory schemes warrant any special accounting requirements that would require or permit recognition of unique assets or liabilities.

19. Yet the ASBJ thinks that the IASB should explore the development of specific disclosure requirements for entities operating in the context of such rate regulatory schemes. Even if rights and obligations are not unique, the ASBJ thinks that these schemes could significantly affect the amount, timing and uncertainty of future net cash inflows to the entity. Therefore, the ASBJ thinks that such disclosures would be helpful for users to assess the prospects for future net cash inflows to an entity.

Question 5

Paragraphs 4.4–4.6 summarise the key features of defined rate regulation. These features have

been the focus of the IASB's exploration of whether defined rate regulation creates a combination of rights and obligations for which specific accounting guidance or requirements might be developed in order to provide relevant information to users of general purpose financial statements.

(a) Do you think that the description of defined rate regulation captures an appropriate population of rate-regulatory schemes within its scope? If so, why? If not, why not?

(b) Do you think that any of the features described should be modified in order to include or exclude particular types of rate-regulatory schemes or rate-regulated activities included within the scope of defined rate regulation? Please specify and give reasons to support any modifications to the features that you suggest, with particular reference to why the features may or may not give rise to circumstances that result in particular information needs for users of the financial statements.

(c) Are there any additional features that you think should be included to establish the scope of defined rate regulation or would you omit any of the features described? Please specify and give reasons to support any features that you would add or omit.

20. The ASBJ generally thinks that the description of defined rate regulation stated in the DP captures an appropriate population of rate-regulatory schemes that should be addressed within the project. The ASBJ thinks that it would be very difficult to conclude that unique rights and obligations are created if important features of a defined rate regulation were to be modified to accommodate a wider spectrum of various rate regulations. Having regards to the importance of the clear cause-and-effect relationship between specific expenses and incomes, the ASBJ thinks that it would be inappropriate for the IASB to try to provide flexibility regarding important features of a defined rate regulation.

21. However, the ASBJ suggests that the IASB give consideration to the following matters:

(a) It would be easier to understand the scope of a defined rate regulation, if the linkage among paragraphs 4.4 to 4.6 of the DP is clearer. Without a clear linkage, some could even interpret that only features stated in paragraph 4.4 constitutes the elements of a defined rate regulation.

(b) It would be helpful for the proper understanding of the scope of a defined rate regulation, if the IASB segregates the features of rate regulation that affect judgment as to whether specific rights and obligations give rise to assets and liabilities and the features essential for a particular activity to be subject to a rate regulation but that do not affect the judgment. For example, maintenance of the 'quality' of the supply of the rate-regulated goods or services would be essential for the relevant activity to be subject to rate regulation but may not be necessary for the determination as to whether rights or obligations meet the definitions of an asset or a liability under the *Conceptual Framework*.

(c) It would be helpful if the elements of a defined rate regulation could be described in a more *objective-based* manner, such that the nature of the relationship between each element is clearer. This approach would be advantageous, because IFRSs cannot prescribe detailed descriptions about the necessary elements in regards to a particular rate regulatory framework, where national accounting standards can do so. For example, the ASBJ thinks that many elements of the condition (a) in paragraph 4.4 are intended to support the assertion that the demand (and accordingly, the price) is relatively 'inelastic.'

(d) It would be helpful if the IASB highlights the key features of a defined rate regulation. When the ASBJ reached out to our constituents, many found that distinguishing features of a defined rate regulation is the existence of 'regulatory adjustment mechanism' in which specified differences between the amount of the revenue requirement accrued to date and the amounts billed to customers is reversed within a specific timeframe.

(e) Finally, it would be important to provide sufficient guidance to support the definitions if the IASB decides to develop specific requirements for a defined rate regulation (including the effect that only relevant aspects of rate regulated activities within a rate regulated entity can be within the scope of a defined rate regulation.) The ASBJ found that the explanations given in paragraphs 4.8 to 4.79 would be essential in understanding the criteria of a defined rate regulation, and recommends that the summary paragraphs are provided as part of the application guidance.

Question 6

Paragraphs 4.62–4.72 contain an analysis of the rights and obligations that arise from the features of defined rate regulation.

(a) Are there any additional rights or obligations that you think the IASB should consider? Please specify and give reasons.

(b) Do you think that the IASB should develop specific accounting guidance or requirements to account for the combination of rights and obligations described? Why or why not?

22. The ASBJ generally thinks that paragraphs 4.62 to 4.72 of the DP sufficiently describe the analysis about rights and obligations that arise from a defined rate regulation.

Question 7

> Section 5 outlines a number of possible approaches that the IASB could consider developing further, depending on the feedback received from this Discussion Paper. It highlights some advantages and disadvantages of each approach.
>
> (a) Which approach, if any, do you think would best portray the financial effects of defined rate regulation in IFRS financial statements and is most likely to provide the information that investors and lenders consider is most relevant to help them make their investing and lending decisions? Please give reasons for your answer?
>
> (b) Is there any other approach that the IASB should consider? If so, please specify and explain how such an approach could provide investors and lenders with relevant information about the financial effects of rate regulation.
>
> (c) Are there any additional advantages or disadvantages that the IASB should consider before it decides whether to develop any of these approaches further? If so, please describe them.
>
> If commenting on the asset/liability approach, please specify, if it is relevant, whether your comments reflect the existing definitions of an asset and a liability in the *Conceptual Framework* or the proposed definitions suggested in the *Conceptual Framework* Discussion Paper, published in July 2013.

23. The ASBJ thinks that the asset-and-liability approach (possibly in combination with the approach which requires deferral of costs or revenue) and the disclosure-only approach are worthy of further consideration.

<u>*Asset and liability approach*</u>

24. When considering the needs of special accounting requirements, the ASBJ believes that it is essential to assess the nature of rights or obligations that arise from a defined rate regulation against the definitions and characteristics of an asset and a liability under the *Conceptual Framework*. This is because the term 'income' or 'expense' is basically explained as the increases or decreases in the value of an asset or a liability under the *Conceptual Framework*.

25. When evaluating the needs of special accounting requirements under the asset and liability approach as explained in the DP, the ASBJ referred to the IASB's latest tentative decisions

within the on-going *Conceptual Framework* project. Please refer to the IASB's tentative decisions with regard to definitions of an asset and liability and the threshold of recognition in Appendix-II.

26. Having assessed whether rights and obligations arising from a defined rate regulation meet the definitions of an asset or a liability and the thresholds, the ASBJ found it very challenging to conclude that such rights and obligations *do not* meet these definitions or the thresholds for recognition. Although there is some possibility that the difference between the revenue requirement accrued to date and the amounts billed to customers may not actually reverse in the future (including the possibility of future changes in the rate regulatory framework), the ASBJ thinks that the criteria set out for a defined rate regulation provides reasonable assurance that the amount will be adjusted in the future operation of the rate regulated entities. However, the ASBJ does not think that this immediately means that associated assets or liabilities should be recognised for the following reasons:

    (a) It is unclear as to what the term 'past events' refers to in the definitions of an asset or a liability. In the context of a rate regulation, the past event could mean the fact that an entity operated its activities within a rate regulatory framework (and goods or services are provided to *a class of customers*). If it is the case, assets or obligations may be created from the operation well before goods or services are provided to customers within the context of a defined rate regulation. However, others could interpret that the 'past events' means provision of goods or services to customers, and therefore conclude that assets or obligations should not be recognised until an entity provides goods or services to specific customers.

    (b) It is unclear as to whether an entity's obligation to reduce the future rate (compared to a rate without a rate regulation) is considered to fall under a present obligation to transfer an economic resource. Some argue that an entity's obligation to forgo its future opportunities meets the definition of a 'present obligation' but others argue that the act of foregoing is not a transfer of an entity's economic resource to third parties.

    (c) Even if such rights or obligations could meet the definitions of an asset or a liability, it is unclear as to whether they meet the recognition threshold. Among others, the IASB's tentative decision states that it may be the case that an asset or a liability should not be recognised when the resulting information would not be relevant and provide faithful representation. However, whether information is relevant and provides faithful representation is a very subjective judgment. Thus, the ASBJ doubts if such criteria is sufficiently practical.

(d) It is also unclear how much weight should be given to respective factors, where the IASB's tentative decision regarding the recognition threshold refers to several factors to be considered (including (i) the degree of existence uncertainties, (ii) the likelihood of occurrence about future flows of economic benefits and (iii) the degree of measurement uncertainties) in deciding whether information might not be relevant. It would be more helpful if a prioritisation of the factors (or a decision-flowchart) is provided.

27. Once the Exposure Draft regarding the *Conceptual Framework* project is issued, the ASBJ would like to examine further as to whether, and if so, how matters stated in the previous paragraph should be addressed (including the level of specificity of the descriptions in the *Conceptual Framework*) by consulting with a wider group of constituents.

28. Under this approach, the ASBJ thinks that the amount that corresponds to the difference between the revenue requirement accrued to date and the amounts billed to customers (that is, the amount which includes profit margin), adjusted by the incremental costs of the provision of relevant goods or services in the future period would be recognised in the statement of financial position. However, if the IASB decides to explore this approach, the ASBJ encourages the IASB to consider the following matters:

(a) How to identify the incremental costs of providing relevant goods or services in the future period. The ASBJ preliminarily thinks that the analysis of fixed costs and variable costs would be important in identifying the incremental costs.

(b) Whether assets or liabilities should be discounted. The ASBJ preliminarily thinks that it would, at least, be difficult to discount assets or liabilities arising from rate regulation, because the timing of the future reversal is very difficult to predict.

(c) Whether the accounting requirements for interest expenses relevant to a defined rate regulation should be modified from those of IAS 23 *Borrowing Costs*.

(d) How to present the changes in assets and liabilities in the statement of profit or loss and other comprehensive income (OCI) and related notes. Reflecting on the feedback from users, the ASBJ thinks that it is essential that the effect of rate regulation be separately presented on the face of the statement of profit or loss and OCI with the relevant breakdown information disclosed in the notes to financial statements.

(e) What degree of guidance is necessary to estimate the period over which the differences between the amount of the revenue requirement accrued to date and the amounts billed to customers is expected to reverse in the future operation of rate regulated entities. Having regard to the subjectivity of estimates of the period, the ASBJ thinks that the development of sufficient guidance necessary for an entity to estimate the period is important.

Approach to recognise all or part of the rights and obligations as an intangible asset

29. Some argue that rights or obligations that arise from a defined rate regulation are similar to those of intangible assets (especially with regard to licences). However, the ASBJ thinks that it is inappropriate to recognise all or part of these rights or obligations as intangible assets (licenses), primary because the specific features of defined rate regulation is considered as a combination of rights and obligations (as opposed to a single right or obligation) give rise to unique rights or obligations that entitles or obligates an entity to recover or forgo certain amounts in its future operation. Practically, it would be significantly challenging, if not impossible, to segregate the effect of rights relevant to licenses from the rest of the rights or obligations.

Approach to recognise the package of rights and obligations as a financial asset or liability

30. Some argue that rights or obligations that arise from a defined rate regulation are similar to those of financial assets or liabilities. However, the ASBJ thinks that it is inappropriate to recognise a package of these rights or obligations as a financial asset or liability. Such rights or obligations do not meet the definitions of a financial asset or a liability as set out in paragraph 11 of IAS 32 *Financial Assets: Presentation*, because these rights or obligations are not contractual rights or obligations.

Approach to report using regulatory accounting requirements

31. The ASBJ thinks that reporting using regulatory accounting requirements is inappropriate. Some may argue that it would be most cost-effective to require or permit the use of regulatory accounting requirements, because it may eliminate the costs associated with preparing two sets of financial information. However, the ASBJ thinks that this approach would give rise to significant conflict with the objective of general purpose financial reports. Paragraph OB10 of the existing *Conceptual Framework* acknowledges the different nature of general purpose financial reports and reports prepared for the purpose of regulatory reporting.

Approach using deferral or acceleration of recognising costs and revenue or their combination

32. In principle, the ASBJ does not necessarily think that deferring or accelerating the recognition of costs and/or revenue and recognising an asset or a liability for a defined rate regulation are inconsistent in that the increase or decrease of an asset or a liability is

ordinarily recognised in income or expenses. Some may argue that the only significant difference between the two approaches might be the form of presentation.

33. Out of the possible alternatives, the ASBJ thinks that it would be very difficult to justify acceleration of recognition of revenue from customers. The ASBJ thinks that revenue from customers should not be recognised before goods or services are provided to customers, consistent with basic principles of IFRS 15 *Revenue from Contracts with Customers*. In addition, it would be inappropriate to accelerate recognition of costs based on the projection of anticipated costs. Due to the inherent subjectivity, the ASBJ thinks that this approach would be too challenging in ensuring a reliable estimate.

34. On the other hand, the ASBJ thinks that the approach requiring deferral of relevant costs or revenue or a combination of both is worthy of further consideration in parallel with considering whether to recognise a relevant asset and liability for a defined rate regulation. For example, when a rate regulated entity undertakes expenditure for the purchase of PPE necessary to maintain the quality of goods or services and the cost of that PPE is expected to be recovered in the future period by raising the rate, it may be the case that such costs should be allocated over the relevant future period. The ASBJ thinks that deferral of costs or revenue can be supported in the context of the matching between the cost incurred and the related earning (see paragraph 4.50 of the existing *Conceptual Framework*). In addition, if rates are set higher to ensure the recovery of the future expenditure on PPE, a portion of revenue earned during the period could be considered merely as the suspense account to be used for the future expenditure.

35. When the ASBJ Staff reached out to users of financial reports, they did not express a strong preference as to whether an asset or a liability should be recognised for rate regulatory activities. However, if a special accounting treatment were applied to such activities, they emphasised the importance of clearly segregating the effect of rate regulation in the statement of profit or loss and other comprehensive income and the statement of financial position. Having regard to such feedback, the ASBJ thinks that the effect of rate regulation (in other words, the amount of the deferral) should nevertheless be clearly disclosed in the financial statements, if the IASB decides to explore the deferral of costs or revenue.

<u>*Disclosure-only approach*</u>

36. Based on the feedback from users (as stated in paragraphs 12 and 35 of this letter), the ASBJ understands that users are most interested in information that helps them to assess the effect of rate regulation. This includes, for example, the amount that is expected to be

adjusted in the future operations of rate regulated entities. However, they did not express a strong preference as to whether the effect should be presented on the face of the financial statements or in the notes to the financial statements.

37. Consequently, considered together with our analysis as to whether an asset or liability should be recognised (as stated from paragraphs 24 to 26 of this letter), the ASBJ believes that the disclosure-only approach is worthy of further consideration.

Question 8

Does your organisation carry out activities that are subject to defined rate regulation? If so, what operational issues should the IASB consider if it decides to develop any specific accounting guidance or requirements?

38. No.

Question 9

If, after considering the feedback from this Discussion Paper and the *Conceptual Framework* project, the IASB decides to prohibit the recognition of regulatory deferral account balances in IFRS financial statements, do you think that the IASB should consider developing specific disclosure-only requirements? If not, why not? If so, please specify what type of information you think would be relevant to investors and lenders in making their investing or lending decisions and why.

39. Please see our response to Questions 1 and 4 of this letter.

Question 10

Sections 2 and 6 discuss some of the information needs of users of general purpose financial statements. The IASB will seek to balance the needs of users of financial statements for information about the financial effects of rate regulation on an entity's operations with concerns about obscuring the understandability of financial statements and the high preparation costs that can result from lengthy disclosures (see paragraph 2.27). (a) If the IASB decides to develop specific accounting requirements for all entities that are subject to defined rate regulation, to what extent do you think the requirements of IFRS 14 meet the information needs of investors and lenders? Is there any additional information that you think should be required? If so, please specify and explain how investors or lenders are likely to use that information.

(b) Do you think that any of the disclosure requirements of IFRS 14 could be omitted or modified in order to reduce the cost of compliance with the requirements, without omitting information that helps users of financial statements to make informed investing or lending decisions? If so, please specify and explain the reasons for your answer.

40. As stated in paragraph 13 of this letter, Japanese users have little experience of financial statements using IFRS 14. If the IASB decides to develop special accounting requirements for all entities that are subject to defined rate regulation, the ASBJ suggests that IFRS 14 be abolished. It would be difficult to rationalise the relevance of information in accordance with the requirements of IFRS 14, when special accounting requirements applicable to a defined rate regulation is developed.

41. Nevertheless, the ASBJ suggests that the IASB consider whether all or some part of the disclosure requirements of IFRS 14 would continue to be relevant for users when the IASB decides to develop special accounting requirements relating to some form of rate regulatory activities.

Question 11

IFRS 14 requires any regulatory deferral account balances that have been recognised to be presented separately from the assets and liabilities recognised in the statement of financial position in accordance with other Standards. Similarly, the net movements in regulatory deferral account balances are required to be presented separately from the items of income and expense recognised in the statement(s) of profit or loss and other comprehensive income.

If the IASB develops specific accounting requirements that would apply to both existing IFRS preparers and first-time adopters of IFRS, and those requirements resulted in the recognition of regulatory balances in the statement of financial position, what advantages or disadvantages do you envisage if the separate presentation required by IFRS 14 was to be applied?

42. The ASBJ thinks that there is no advantage to users if an entity continues to follow the separate presentation requirements of IFRS 14 if special accounting requirements applicable to a defined rate regulation are developed.

Question 12

Section 4 describes the distinguishing features of defined rate regulation. This description is intended to provide a common starting point for a more focused discussion about whether this type of rate regulation creates a combination of rights and obligations for which specific accounting guidance or requirements should be developed.

Paragraph 4.73 suggests that the existence of a rate regulator whose role and authority is established in legislation or other formal regulations is an important feature of defined rate regulation. Do you think that this is a necessary condition in order to create enforceable rights or obligations, or do you think that co-operatives or similar entities, which operate under self-imposed rate regulation with the same features as defined rate regulation (see paragraphs 7.6–7.9), should also be included within defined rate regulation? If not, why not? If so, do you think that such co-operatives should be included within the scope of defined rate regulation only if they are subject to formal oversight from a government department or other authorised body?

43. The ASBJ does not think that co-operatives or similar entities should be included in the scope of the project. The ASBJ thinks that the operations of co-operatives has some similarity to rate regulatory activities within the scope of a defined rate regulation in that both are designed to achieve the protection of a customer; thus a rate is designed to be relatively *inelastic* with a lesser profit margin.

44. However, the ASBJ thinks that there are important differences in the characteristics of their operations as follows:

(a) Unlike rate regulatory activities within a defined rate regulation that is subject to oversight by an independent regulator, customers usually have greater choice to purchase the goods or services in the case of a co-operative.

(b) Unlike goods or services provided within a defined rate regulation that is subject to oversight by an independent regulator, goods or services provided by co-operatives are not necessarily essential to customers.

(c) Unlike rate regulatory activities that is within the scope of the DP, co-operatives do not usually have an adjustment mechanism similar to a ‘regulatory adjustment mechanism’, in which it is ensured with sufficient enforceability that specified differences between the amount of the revenue requirement accrued to date and the amounts billed to customers are adjusted in the future operations of rate regulated activities. In other words, the cause-and effect relationship is usually not sufficiently clear under the operations of co-operatives.

45. The ASBJ does not necessarily think that the existence of a rate regulator whose role and authority is established in legislation or other formal document is essential for a particular rate regulatory activity to require a special accounting requirement as far as the regulatory adjustment mechanism is sufficiently enforced. Yet the ASBJ thinks that the existence of

such a rate regulator is significantly important so as to ensure the enforceability.

Question 13

Paragraphs 7.11–7.22 highlight some of the issues that the IASB may consider if it continues to progress this project. Do you have any comments or suggestions on these or any other issues that may or may not have been raised in this Discussion Paper that you think the IASB should consider if it decides to develop proposals for any specific accounting requirements for rate-regulated activities?

46. The ASBJ thinks that the IASB need to consider interactions with other relevant standards of IFRSs (especially that with IFRS 3 *Business Combinations*) when the IASB decides to develop special accounting requirements for defined rate regulation. However, the ASBJ thinks that it is unnecessary to consider such interactions when the IASB decides to develop disclosure requirements only.

Appendix-II

Excerpts from the IASB's tentative decisions in the Conceptual Framework project

1. As for definitions of an asset or a liability, the IASB tentatively decided the following matters[1]:

   (a) Asset is a present economic resource controlled by the entity, as a result of past events;

   (b) A liability is a present obligation of the entity to transfer an economic resource as a result of past events;

   (c) An economic resource is a right that is capable of producing economic benefits.

2. As for recognition, the IASB tentatively decided that the *Conceptual Framework* should not establish criteria that govern the recognition of an asset or a liability in all circumstances. The *Conceptual Framework* should instead describe factors to consider in deciding whether to recognise an asset or a liability. Those factors would include whether the resulting information would be relevant and provide faithful representation, and the costs of providing information relative to the benefits. Information might not be relevant, if, for example,

   (a) it is uncertain whether the asset or liability exists;

   (b) if it is unlikely that future flows of economic benefits will occur; or

   (c) if there is very significant measurement uncertainty associated with them.

[1] Descriptions are based on the IASB Staff Paper (November 2014), Effect of Board redeliberations on DP *A Review of the Conceptual Framework for Financial Reporting*.