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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application Of CALIFORNIA-AMERICAN WATER COMPANY (U-210-W), CALIFORNIA WATER SERVICE COMPANY (U-60-W), GOLDEN STATE WATER COMPANY (U-133-W), PARK WATER COMPANY (U-314-W) AND APPLE VALLEY RANCHOS WATER COMPANY (U-346-W) to Modify D.08-02-036, D.08-06-002, D.08-08-030, D.08-09-026, D.08-11-023, D.09-05-005, D.09-07-021, and D.10-06-038 regarding the Amortization of WRAM-Related Accounts.	Application 10-09-017

PREHEARING CONFERENCE STATEMENT

OF CALIFORNIA WATER SERVICE COMPANY (U-60-W)

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Dated: November 29, 2010

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OF THE STATE OF CALIFORNIA

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PREHEARING CONFERENCE STATEMENT
OF CALIFORNIA WATER SERVICE COMPANY (U-60-W)

I. INTRODUCTION

Pursuant to Rule 7.2 of the Commission's Rules of Practice and Procedure ("Rules") and the November 22, 2010 Administrative Law Judge's Ruling Setting a Prehearing Conference and Requesting Additional Information ("Ruling"), California Water Service Company (U-60-W) ("Cal Water") respectfully submits this Prehearing Conference Statement.

Cal Water provides the information requested in the Ruling as follows:

(1) A table containing information about the Water Revenue Adjustment Mechanisms ("WRAM") and Modified Cost Balancing Accounts ("MCBAs") for each Cal Water district.

(2) Cal Water's response to the Financial Accounting Standards Board's ("FASB's") Exposure Draft on proposed updates to Revenue Recognition (Topic 605) ("ED"), and the related October 22, 2010 comments of the Edison Electric Institute on that Exposure Draft.

Cal Water appreciates the opportunity to consider the impact of possible changes to accounting guidance, but strongly urges the Commission to move forward with the Application without delay. As discussed below, the nature and timing of potential relevant changes to the current accounting guidance under which Applicants[1] must rely will continue to be under consideration over the next several years, and in any event ***will become effective no earlier than*** 2015.

II. DISCUSSION

A. Both Ratepayers and Shareholders Share the Need for Timely Resolution of the Application

Cal Water first emphasizes that, until relevant changes to current accounting guidance are adopted and become effective, Cal Water and the other Applicants must continue to operate and issue financial reports that are consistent with current accounting guidance. As the Application discusses in detail, the implementation of the new WRAM/MCBA mechanisms, in conjunction with the historical amortization periods allowed for typical balancing accounts, have raised significant accounting concerns.[2] Whether these concerns would continue under future revised accounting guidance is a subject for future consideration.

If the Commission agrees with the general principle underlying the Application – that adoption of the WRAM/MCBA mechanisms, with no changes in allowed amortization periods, has had unforeseen accounting consequences that the Commission should rectify – <u>both Cal Water and its ratepayers have a very strong interest in resolving the Application quickly.</u> This is because consistency with current accounting guidance requires Cal Water to collect its outstanding 2009 WRAM/MCBA revenues by December 31, 2011, and therefore every month closer to that deadline is one fewer month over which the balance in a particular district may be amortized.[3]

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[1] The Applicants in this proceeding are California-American Water Company (U-210-W) ("Cal Am"), California Water Service Company (U-60-W) ("Cal Water"), Golden State Water Company (U-133-W) ("Golden State"), Park Water Company (U-314-W) ("Park"), and Apple Valley Ranchos Water Company (U-346-W) ("Apple Valley").

[2] Application at Section II (pages 5-19).

[3] As discussed in the Application, the WRAM/MCBA mechanisms were adopted to remove a company's disincentive to encourage conservation by helping to stabilize certain revenue streams – those revenue streams that that would otherwise be at risk under a conservation rate design. Application at 9-10. Cal Water accordingly books both the WRAM and non-WRAM revenue for a given calendar year in that year for financial accounting purposes, even though

As Attachment 1 reflects, the net WRAM/MCBA balance for calendar year 2009 that must be collected from the ratepayers in each district is a fixed amount that has already been calculated, with additional interest as the only variable. Thus, until a Commission decision resolving the Application becomes effective, each passing month unfortunately increases the monthly customer surcharge that will have to be imposed to collect to collect the revenue by December 31, 2011, consistent with the current accounting standards.

B. Table with Cal Water's WRAM and MCBA Data

Cal Water provides the table requested in Question 1 of the Ruling, and identifies the column that is responsive to each sub-part of the question. A narrative description of each column is also provided below the table.

> (1) Each Utility should prepare a table, in a format similar to the table at page 18 of the application, that provides the following information columns for each water district with an authorized Water Revenue Adjustment Mechanism and Modified Cost Balancing Account ("WRAM/MCBA"):

a. The current quantity charge rate

   Please refer to columns "E" and "F" in the table shown below.

b. 2009 WRAM MCBA Balance

   Please refer to column "B" in the table shown below.

c. Estimated 2010 WRAM/MCBA Balance

   Please refer to column "G" in the table shown below.

d. Estimated 2011 Surcharges under existing authorization

   Please refer to columns "J" and "K" in the table shown below.

e. Estimated 2011 Surcharges under proposed changes

   Please refer to columns "M" and "N" in the table shown below.

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the WRAM revenue for that year (offset by the MCBA) will not be collected until surcharges (or surcredits if consumption is high) begin to be applied to bills in the following calendar year.

A	B	C	D	E	F	G	H	I	J	K	L	M	N
Calwater District	12/2009 WRAM/MCBA Balance	% of Recorded RR	Current Charge Rate			Annualized 2010 WRAM/MCBA Balance	% of Recorded RR	Estimated 2011 Surcharges Existing			Estimated 2011 Surcharges Proposed		
	Adopted RR for Previous Year		# Mos. Amort	Metered-rate (per Ccf.)	Flat-rate (per Ccf.)	Adopted RR for 2011		# Mos. Amort	Metered-rate (per Ccf.)	Flat-rate (per Ccf.)	# Mos. Amort	Metered-rate (per Ccf.)	Flat-rate (per Ccf.)
ANTELOPE VALLEY	$ 74,285	4.2%	12	$ 0.1507		$ 112,985	4.9%	12	$ 0.2196		12	$ 0.2196	
	$ 1,784,400					$ 2,298,178							
BEAR GULCH	$ 1,121,365	4.0%	12	$ 0.1900		$ 1,910,987	6.1%	24	$ 0.1553		18	$ 0.2068	
	$ 27,960,700					$ 31,289,158							
BAKERSFIELD	$ (1,315,736)					$ (924,877)	-1.5%				12	$ (0.0288)	$ (1.2136)
						$ 62,915,198							
CHICO-HAM CITY	$ 283,471					$ 572,677	2.9%	12	$ 0.0621	$ (0.3059)	12	$ 0.0621	$ (0.3059)
						$ 19,554,043							
DIXON	$ 182,978	10.1%	36	$ 0.0871		$ 260,953	11.1%	36	$ 0.1274		18	$ 0.2539	
	$ 1,810,900					$ 2,350,478							
DOMINGUEZ SOUTH-BAY	$ 478,126					$ 3,370,653	6.6%	24	$ 0.0956		18	$ 0.1273	
						$ 51,327,199							
EAST LOS ANGELES	$ 569,995					$ 759,886	2.4%				12	$ 0.0918	
						$ 31,262,821							
HERMOSA-REDONDO	$ 2,123,170	8.5%	24	$ 0.1774		$ 2,544,446	9.9%	24	$ 0.2131		18	$ 0.2832	
	$ 24,906,300					$ 25,573,415							
KERN RIVER VALLEY	$ 629,676	12.7%	36	$ 0.3970		$ 774,412	14.4%	36	$ 0.5857		18	$ 1.1676	
	$ 4,976,700					$ 5,389,703							
KING CITY	$ 56,334	2.6%	12	$ (0.0714)		$ 41,888	1.5%				12	$ 0.0504	
	$ 2,138,500					$ 2,830,840							
LIVERMORE	$ 493,894	2.7%	12	$ (0.1006)		$ 500,211	2.5%	12	$ 0.0958		12	$ 0.0958	
	$ 18,581,400					$ 20,340,202							
LOS ALTOS-SUBURBAN	$ 490,221					$ (854,184)	-3.5%	12	$ (0.1343)		12	$ (0.1343)	
						$ 24,351,719							
MARYSVILLE	$ 121,460	4.6%	12	$ 0.2125	$ (0.3667)	$ 135,007	4.2%	12	$ 0.2046	$ (0.3627)	18	$ 0.2046	$ (0.3627)
	$ 2,629,300					$ 3,203,504							
MID PENINSULA	$ 1,055,731	3.3%	12	$ 0.1642		$ 1,934,591	5.6%	24	$ 0.1302		18	$ 0.1735	
	$ 32,172,900					$ 34,706,107							
OROVILLE	$ 315,613	9.1%	24	$ 0.1253	$ 0.4616	$ 306,365	7.6%	24	$ 0.1054	$ (0.7115)	18	$ 0.1404	$ (0.9477)
	$ 3,472,100					$ 4,028,129							
PALOS VERDES	$ 1,691,473	4.7%	12	$ 0.1403		$ 3,150,002	8.2%	24	$ 0.1598		18	$ 0.2128	
	$ 35,884,200					$ 38,382,933							
REDWOOD VALLEY - COAST SPRINGS	$ 18,879	7.2%	24	$ 1.3169		$ 23,064	5.2%	24	$ 1.4491		18	$ 1.9301	
	$ 260,600					$ 441,663							
REDWOOD VALLEY - LUCERNE	$ 192,991	14.9%	36	$ 0.5079		$ 242,883	13.8%	36	$ 0.6133		18	$ 1.2225	
	$ 1,291,100					$ 1,759,434							
REDWOOD VALLEY - UNIFIED	$ 109,526	19.6%	36	$ 0.7708		$ 119,334	19.6%	36	$ 1.0546		18	$ 2.1023	
	$ 558,800					$ 609,114							
SALINAS	$ 1,526,860	6.1%	24	$ 0.1044		$ 2,571,459	10.1%	36	$ 0.1142		18	$ 0.2276	
	$ 25,119,500					$ 25,356,975							
SELMA	$ 102,828	2.9%	12	$ 0.0673	$ (0.0160)	$ 190,366	4.3%	12	$ 0.1084	$ 0.0468	12	$ 0.1084	$ 0.0468
	$ 3,518,400					$ 4,410,068							
SO. SAN FRANCISCO	$ 187,822					$ 468,697	2.9%	12	$ 0.1179		12	$ 0.1179	
						$ 16,230,573							
STOCKTON	$ 913,376	3.0%	12	$ 0.0837		$ 1,578,252	4.7%	12	$ 0.1204		18	$ 0.1204	
	$ 30,821,800					$ 33,831,604							
VISALIA	$ 998,249	4.9%	24	$ 0.0493	$ 0.0552	$ 797,193	3.4%	12	$ 0.0594	$ 0.0598	12	$ 0.0594	$ 0.0598
	$ 20,451,100					$ 23,514,456							
WESTLAKE	$ 348,531	2.3%	12	$ 0.1294		$ 839,196	5.5%	24	$ 0.1022		18	$ 0.1362	
	$ 15,049,200					$ 15,385,164							
WILLOWS	$ (31,727)					$ 7,827	0.4%				12	$ 0.0206	$ (0.5831)
						$ 2,031,159							

Column B identifies (1) the net WRAM/MCBA balance for calendar year 2009, which in this case is the “under-collection” to be recovered from ratepayers through surcharges, and (2) the total recorded revenue requirement for that ratemaking unit for the previous year.

Column C provides the net WRAM/MCBA balance as a percentage of the previous year’s recorded revenue requirement. This is the percentage that is used to determine whether the amortization "trigger" has been met, and what the appropriate period for amortization should be. (Note that the Applicants' Settlements state that this percentage should be calculated based on the "recorded" revenue requirement, while the proposal in the Application would use the "adopted" revenue requirement, a modification suggested by DRA that Applicants do not oppose.)

Column D identifies the amortization periods directed by Standard Practice U-27. The Standard Practice directs Utilities to implement a surcharge over a twelve (12) month period for increases between zero and less than five percent (0 to < 5%). For increases between five and less than ten percent, the Standard Practice directs Utilities to implement a surcharge over a twenty-four (24) month period. For increases greater than ten percent (10%), the Standard Practice directs Utilities to amortize the increase over a period of thirty-six (36) months.

Column G shows (1) the net WRAM/MCBA balance for calendar year 2010 (since only nine (9) months of data are available, this amount has been annualized using the prior year's balance for the remaining three (3) months); and (2) the total revenue requirement in the Proposed Decision in Cal Water's pending general rate case (A.09-07-001) ("GRC PD"), and scheduled to be effective January 2011.[4]

Column H provides the net WRAM/MCBA balance as a percentage of the adopted revenue requirement for 2011 in the GRC PD. This revenue requirement is scheduled to become effective in January 2011. On the assumption that the amortization requested in the Application would not begin until January 2011 or later, this table uses the 2011 revenue requirement in the GRC PD to determine whether the amortization "trigger" has been met, and what the appropriate period for amortization should be.

Column I notes the amortization period for the 2010 WRAM/MCBA net balance based on Standard Practice U-27.

Columns J and K depict the amortization amounts for each of Cal Water's District's net balance for 2010 based on Standard Practice U-27.

Column L identifies the amortization period for the 2010 WRAM/MCBA net balance based on the proposed policy to amortize all balances over a period of twelve (12) months (whether or not they meet the "trigger") or, for balances greater than five percent (5%) of the revenue requirement, over a period of eighteen (18) months.

Columns J and K show the amortization amounts for each of Cal Water's District's net balance for 2010 based on the treatment for the WRAM and MCBA net balance proposed in the Application.

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[4] A Proposed Decision issued in A.09-07-001 is on the Commission's December 2, 2010 Agenda as Item 42.

C. The Application Should be Resolved Based on Current Accounting Guidance that Will Continue to be in Effect for the Near Future

The Exposure Draft on Revenue Recognition referenced in the Ruling is part of the work plan by FASB and the International Accounting Standards Board ("IASB") to impose international financial reporting standards ("IFRS") on U.S. companies.[5] At the forefront of this discussion, it is important to note that adoption of IFRS for U.S. companies is subject to approval of the Securities and Exchange Commission ("SEC") and will occur no earlier than 2015.[6] Adoption of, or FASB convergence with, IFRS could also be delayed.

Cal Water notes that the specific exposure draft brought to our attention by the Ruling has, on the surface, little to do with revenue recognition for alternative revenue programs. In fact, the only mention of these programs is among other revenue recognition standards the IASB intends to roll into the proposed standard or delete as a result of adopting a new standard. Decoupled utilities, as well as the Edison Electric Institute ("EEI") referenced in your Ruling, have commented on the ED and urged the inclusion of accounting guidance for alternative revenue programs in any new IFRS. This provision is related to the larger issue of accounting for rate-regulated industries.

More relevant to this proceeding is the most recent exposure draft for another portion of the accounting rules, "Accounting for Rate-Regulated Industries," which would have far-reaching effects on all utilities if adopted with no provisions for regulatory assets and liabilities. All regulated industries are actively engaged in an effort to retain regulatory accounting provisions in future IFRS accounting rules. Recent open meetings with the IASB have shown the continued controversy surrounding IFRS rules for rate-regulated industries, an indication that no decisions will be made in the near future on these matters.[7]

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[5] *See* IASB Work Plan (Attachment 1).

[6] *See* description of SEC Statement in Support of Convergence and Global Accounting Standards (Attachment 2) at 15.

[7] *See* Notes of IASB September 2010 meeting (Attachment 3).

Upon review, Cal Water's view is that the Revenue Recognition Exposure Draft has little or no nexus with the current proceeding because the existing accounting guidance will not be changed for the foreseeable future, and potentially may not change at all. The Applicants' requests specifically relate to compliance with current revenue recognition guidance adopted under GAAP and affect calendar years 2009 and 2010 in addition to future years that will be covered by existing rules and guidance.

Further, Cal Water management believes it will be appropriate for the Commission to consider, for all industries, the policy implications of IFRS once final rules are published and adopted by the SEC if such rules require changes to regulated utility accounting. Any future change to revenue recognition standards which affect the Applicant utilities' alternative revenue programs should be considered in that potential rulemaking proceeding.

As background, Cal Water is enclosing:

Attachment 1 – IASB Work Plan (as of October 2010) containing the projected timetable for IFRS

Attachment 2 – Description of SEC Statement in Support of Convergence and Global Accounting Standards

Attachment 3 – Notes of IASB September 2010 meeting

III. CONCLUSION

As discussed above, it is in the interests of both ratepayers and shareholders that the Commission move forward with the Application based on the current accounting guidance under which Applicants must operate over the next several years. The Commission should therefore refrain from delay based on concerns that the relevant financial accounting rules may change after 2014.

Respectfully Submitted,

___/s/ THOMAS F. SMEGAL______

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California Water Service Company

Dated: November 29, 2010

CERTIFICATE OF SERVICE

I hereby certify that on this date I served the foregoing **PREHEARING CONFERENCE STATEMENT OF CALIFORNIA WATER SERVICE COMPANY (U-60-W)** by electronic mail or U.S. Mail delivery on the Service List for **A.10-09-017** below:

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By U.S. Mail Delivery:

Christine M. Walwyn
California Public Utilities Commission
Division of Administrative Law Judges
505 Van Ness Avenue
San Francisco, CA 94102-3214

Executed this **29th day of November 2010**, at San Jose, California.

______/s/ LONG NGUYEN___
Long Nguyen

Attachment 1 to CWS PHC Statement

IFRS

IASB work plan - projected timetable as of 12 October 2010

The timetable (also available to **download in PDF format**) shows the current best estimate of document publication dates. The effective date of amendments and new standards is usually 6-18 months after publication date, although in setting an effective date the Board considers all relevant factors. In appropriate circumstances, early adoption of new standards will be allowed.

The work plan anticipates the completion of several projects in 2010 and 2011. The Board will consider staggering effective dates of standards to help entities that apply IFRSs undertake an orderly transition to any new requirements. The Board understands the difficulties some entities, and jurisdictions that must pass our Standards into law, could have coping with several major changes to IFRSs as we complete the projects on the MoU. The Board plans to publish in October a paper outlining possible ways to reduce that burden. The Board will seek comments on that paper.

The Board undertakes this work using its established due process, including consultation with interested parties. The timetable for completion is subject to change depending on input received throughout a project's development.

<table>
<tr><td></td><td colspan="4">Estimated publication date</td><td colspan="2"></td></tr>
<tr><td>Financial Crisis related projects</td><td>2010 Q4</td><td>2011 Q1</td><td>2011 Q2</td><td>2011 H2+</td><td>MoU</td><td>Joint</td></tr>
<tr><td>Financial instruments (IAS 39 replacement)</td><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td>Classification and measurement – financial liabilities</td><td>IFRS</td><td></td><td rowspan="4">IFRS</td><td></td><td>✓</td><td>✓</td></tr>
<tr><td>Impairment</td><td></td><td></td><td></td><td>✓</td><td>✓</td></tr>
<tr><td>Hedge accounting</td><td>ED</td><td></td><td></td><td>✓</td><td>✓</td></tr>
<tr><td>Asset and liability offsetting</td><td>ED</td><td></td><td></td><td>✓</td><td>✓</td></tr>
<tr><td>Consolidation</td><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td>Replacement of IAS 27</td><td>IFRS</td><td></td><td></td><td></td><td>✓</td><td>✓</td></tr>
<tr><td>Disclosures unconsolidated entities</td><td>IFRS</td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td>Investment companies</td><td>ED</td><td></td><td>IFRS</td><td></td><td></td><td>✓</td></tr>
<tr><td>Fair value measurement guidance</td><td></td><td>IFRS</td><td></td><td></td><td>✓</td><td>✓</td></tr>
<tr><td></td><td colspan="4">Estimated publication date</td><td colspan="2"></td></tr>
<tr><td>Memorandum of Understanding projects</td><td>2010 Q4</td><td>2011 Q1</td><td>2011 Q2</td><td>2011 H2+</td><td>MoU</td><td>Joint</td></tr>
<tr><td>Financial statement presentation</td><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td>Presentation of OCI</td><td></td><td>IFRS</td><td></td><td></td><td>✓</td><td>✓</td></tr>
<tr><td>Replacement of IAS 1 and IAS 7 (including Discontinued operations)</td><td></td><td>ED</td><td></td><td>IFRS</td><td>✓</td><td>✓</td></tr>
</table>

Attachment 1 to CWS PHC Statement

Leases [ED, comments due 15 December 2010]	RT 17, 20 Dec & 5, 6 Jan		IFRS		✓	✓
Revenue recognition [ED, comments due 22 October 2010]	RT 4,8,10,23 Nov		IFRS		✓	✓
Joint ventures	IFRS				✓	
Post-employment benefits (incl. pensions)		IFRS			✓	
FI with characteristics of equity		ED		IFRS	✓	✓
Effective dates and transition	RV					✓
	Estimated publication date					
Other Projects	**2010 Q4**	**2011 Q1**	**2011 Q2**	**2011 H2+**	**MoU**	**Joint**
Insurance contracts [ED, comments due 30 November 2010]	RT 9,16,20 Dec		IFRS			✓
Emissions trading schemes				ED		✓
Liabilities (IAS 37 amendments)				ED		
Management commentary	PS					
Narrow-scope improvements						
Annual improvements 2009-2011	ED		IFRS			
Amendments to IFRS 1 – Removal of Fixed Dates for First-time Adopters [ED, comments due by 27 October 2010]		IFRS				
Amendments to IFRS 1 – Severe Hyperinflation [ED, comments due by 30 November 2010]	IFRS					
Deferred tax: recovery of underlying assets [ED, comments due by 9 November 2010]	IFRS					
Income taxes		ED				
	Estimated publication date					
Conceptual Framework **Documents currently being developed**	**2010 Q4**	**2011 Q1**	**2011 Q2**	**2011 H2+**	**MoU**	**Joint**
Phase B: Elements and recognition	TBD					✓
Phase C: Measurement	DP			ED		✓
Phase D: Reporting entity		Final chapter				✓
Phase A was completed in September 2010. The IASB and the FASB will amend sections of their conceptual frameworks as they complete individual phases of the project. *Phases E to H Presentation and disclosure, Purpose and Status, Application to not-for-profit entities and Remaining issues have not yet started.*						
	Estimated publication date					
Agenda consultation	**2010**	**2011**	**2011**	**2011**	**MoU**	**Joint**

Attachment 1 to CWS PHC Statement

	Q4	Q1	Q2	H2+		
Three-yearly public consultation	RV					

Abbreviations	
AD Agenda Decision (to add the topic to the active agenda)	**PS** IFRS Practice Statement
DP Discussion Paper	**ED** Exposure Draft
IFRS International Financial Reporting Standard	**RT** Roundtables
RV Request for Views	**TBD** To be determined

Research and other projects
In 2009 the Board published an exposure draft addressing **rate-regulated activities**. In September 2010 the Board concluded that it could not resolve the matter quickly and decided to develop an agenda proposal for consideration for its future agenda in 2011.
In October 2010 the Board began considering comments received in relation to a Discussion Paper on **extractive activities** prepared for it by national standard-setters from Australia, Canada, Norway and South Africa. The Board will use this feedback to help it assess whether to add a project to its agenda when it considers its future agenda in 2011.
Common control was added to the agenda in December 2007. The Board will consider whether to restart the project when it considers its future agenda in 2011.
In October 2009 the Board decided to stop work on **credit risk in liability measurement** as a free-standing work stream and not to reach a general conclusion on credit risk at this time but instead to incorporate the topic in the conceptual framework measurement project. The Board is also considering the input received on this topic when it considers the measurement of liabilities in other topics.
In April 2009 the Board considered comments received in relation to proposed amendments to IAS 33 **Earnings per Share**. In the light of other priorities, the Board stopped work on the project. The Board will consider whether to restart the project when it considers its future agenda in 2011
Work on the **government grants** project has been deferred pending progress in the revenue recognition and emissions trading schemes projects. The Board will consider whether to restart the project when it considers its future agenda in 2011.
In December 2007 the IASB decided not to add a project on **intangible assets** to its active agenda. National standard-setters are carrying out research for a possible future project. The Australian Accounting Standards Board has published a discussion paper Initial Accounting for Internally Generated Intangible Assets. The Board will consider whether to restart the project when it considers its future agenda in 2011.

Recently completed projects
Derecognition – Disclosures. *Amendments to IFRS 7 Financial Instruments*: Disclosures were issued in October 2010. Those amendments improve the disclosure requirements in relation to transferred financial assets. The amendments are effective for annual periods beginning on or after 1 July 2011, with earlier application permitted.
Conceptual Framework Phase A: Objectives and qualitative characteristics. New chapters dealing with objectives and qualitative characteristics were issued on 28 September 2010, with immediate effect.
Improvements to IFRSs. Amendments issued in May 2010. The amendments are effective for annual periods beginning on or after 1 January 2011, with earlier application permitted.
Amendment to IFRIC 14: *Prepayments of a Minimum Funding Requirement* was issued in November 2009. The amendment is effective for annual periods beginning

Attachment 1 to CWS PHC Statement

on or after 1 January 2011, with earlier application permitted.
IFRS 9 *Financial Instruments* was issued in November 2009. The standard is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted.

Terms & Conditions
Sitemap

Attachment 2 to CWS PHC Statement

Deloitte.

Energy & Resources 2010 Accounting, Financial Reporting, and Tax Update

Section 3
International Financial Reporting Standards

IFRSs are on the minds of many at P&U sector companies as we continue to monitor the ongoing international debate, the continued efforts of the SEC to conduct its work plan (see below) activities leading up to a decision about whether to mandate IFRSs for U.S. companies, and the convergence efforts of the IASB and FASB (the "boards").

SEC Update

In November 2008, the SEC issued its proposed IFRS Roadmap ("Roadmap") outlining milestones that, if achieved, could lead to mandatory transition to IFRSs, potentially as early as December 2014. In exposing the Roadmap for comment, the SEC sought input on a number of areas, including the use of IFRSs by U.S. issuers, the SEC's overall approach and considerations, proposed technical amendments to the SEC's rules and regulations, and the standard-setting process under IFRSs. The Roadmap also presented an opportunity for the SEC to decide, on the basis of progress measured against a set of milestones, on potential mandatory adoption of IFRSs in 2011.

Over 200 comment letters on the Roadmap were submitted to the SEC from a broad range of interested parties, including investors, issuers, regulators, standard setters, and representatives from academia and from the accounting and legal professions as well as other fields. The comments generally indicated support for the goal of a single set of high-quality globally accepted accounting standards, although views differed about the best approach going forward and were split between continuing current convergence efforts and going forward with a "big bang" wholesale adoption of IFRSs. Respondents also raised other concerns about the structural and operational issues involved in making the transition to IFRSs and about areas similar to those the SEC itself had identified as milestone considerations, such as the maturity and completeness of IFRSs, the independence of the global standard setter, the time frame needed for constituents to adequately prepare, and the overall costs of transition.

After considering the comments and insights it received about the Roadmap, the SEC (after much anticipation) unanimously approved at its open meeting on February 24, 2010, a public statement expressing the SEC's strong commitment to the development of a single set of high-quality globally accepted accounting standards. The SEC noted that as the activities of investors, companies, and markets become increasingly global, use of a single set of high-quality global standards will facilitate cross-border capital formation and help give investors the comparable financial information they need to make informed decisions about investment opportunities around the world. The Commissioners also affirmed that IFRSs are "best positioned" to be that set of standards for the U.S. market and outlined the SEC's next steps to determine whether to incorporate IFRSs into the financial reporting system for U.S. issuers. The statement also emphasized the importance of the boards' convergence efforts (discussed below).

In recognition of the other structural, operational, and transitional issues raised in the comment letters, the statement directed the SEC staff to execute a "work plan" to provide the SEC with appropriate information to make a well-informed decision about the use of IFRSs. After completing the work plan's activities, and in recognition of the status of the ongoing convergence projects, the SEC will reconsider whether to incorporate IFRSs into the U.S. financial reporting system. The statement indicates that the SEC will make this determination in 2011, in line with the timeline in the Roadmap. The statement notes that if in 2011 the SEC votes to incorporate IFRSs into the financial reporting system for U.S. issuers, sufficient transition time would be allowed, with U.S. issuers reporting under such a system no earlier than 2015.

While the SEC did not provide definitive dates for the U.S. adoption of IFRSs, the February 2010 statement marked another step toward the use of IFRSs, and the work plan itself demonstrates the SEC's level of commitment to moving forward with IFRSs for U.S. issuers.

A few developments that took place after the SEC's February 2010 open meeting are also worth noting. On May 18, 2010, in her presentation to the annual conference of the CFA Institute, SEC Chairman Mary Schapiro countered several "myths" about the SEC and IFRSs and further reaffirmed the SEC's commitment to developing a "single set of high-quality, globally-accepted accounting standards which will benefit U.S. investors and investors around the world."

Chairman Shapiro responded to the myth that the "SEC's commitment to global accounting standards is not as strong as it should be" by stating:

> Let's put this one to rest, right away. And, I can do that by citing the official text of our Commission Statement in Support of Convergence and Global Accounting Standards. In February we clearly stated: "The Commission continues to believe that a single set of high-quality globally accepted accounting standards will benefit U.S. investors and that this goal is consistent with our mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation."

She also responded to the myth that the "U.S. may be committed, but it's dragging its feet regarding adoption of IFRS" by noting:

> This too is wrong. To be clear, while I strongly believe in our commitment to high quality accounting standards, I believe just as strongly that this commitment is only the beginning of the discussion, not the end. The convergence process is critical to the incorporation of IFRS into the U.S. market. . . . While redoubling efforts to achieve the goal of convergence in a timely manner is important, a convergence effort that fails to take into account the due processes of the standard setting bodies will not serve investors well in the long run. . . . We are committed to convergence. But we are committed, above all, to a convergence exercise that yields high-quality improvements to accounting standards. And the fact is, we are moving forward. We are executing on a comprehensive work plan, dedicating significant resources to it and providing periodic progress reports on it.

In addition, in August 2010, the SEC released two Requests for Comment on a number of topics related to its ongoing work plan activities, in which it asked for views on the following topics:

Investor and logistics perspectives (Release No. 33-9133):

- Investors' current knowledge of IFRSs and preparedness for incorporation of IFRSs.
- Investors' education processes on changes in accounting standards and timeliness of such education.
- Extent of, logistics for, and estimated time necessary to undertake any necessary changes.

Impacts on other arrangements and requirements (Release No. 33-9134):

- Contractual arrangements (e.g., financial covenants, lease contracts, employee compensation, earn-out provisions).
- Corporate governance — stock exchange listing requirements.
- Statutory distribution restrictions and other legal standards tied to financial reporting standards.

On October 29, 2010, the SEC staff issued its first public progress report on the staff's efforts and observations to date under the work plan.

The Modified Convergence Strategy

Convergence remains a key goal of the boards, as reaffirmed by a number of public statements over the past year. The boards' November 2009 Joint Statement reaffirmed the boards' commitment to improve both IFRSs and U.S. GAAP and to converge these two accounting frameworks. The boards also committed to monthly joint meetings and agreed to publish quarterly updates on progress toward convergence. Their Joint Statement also reaffirmed the boards' Memorandum of Understanding (MoU), originally issued in 2006 and updated in 2008, and set an aggressive timetable for completing the MoU projects by June 2011.

In February 2010, the Trustees of the Financial Accounting Foundation (FAF), the FASB's oversight body, issued a statement acknowledging "the SEC's leadership regarding its consideration of global accounting standards, including its continued support for the goal of a single set of high quality globally accepted accounting standards" and noting that the FAF and the FASB "support the SEC's view that a single set of high-quality globally accepted accounting standards will benefit U.S. investors."

In June 2010, the boards announced a modified strategy for the convergence of IFRSs and U.S. GAAP. The modified plan was in response to a period of unprecedented standard-setting activity that would have resulted in the issuance of a significant number of proposals for comment in a very short period. The aggressive schedule prompted concerns by constituents about their ability to provide meaningful input on these proposals given both their number and complexity. Constituents also voiced concerns about ultimately implementing such a large number of new standards in a short period. Accordingly, the boards modified their convergence strategy to:

- Revise the MoU to give higher priority to projects that would result in significant improvements to current IFRSs and U.S. GAAP and in achieving convergence.
- Commit the boards to no more than four significant or complex EDs outstanding for comment in any one quarter, to allow for full stakeholder participation in due process.
- Issue a separate document requesting constituent input on the proposed effective date and transition methods for the projects covered under the modified convergence agenda.

The joint projects on financial instruments, revenue recognition, leases, offsetting, and fair value measurements were given priority, and the timelines were extended for (1) the projects on derecognition and financial instruments with characteristics of equity and (2) the main project on financial statement presentation.

SEC Chairman Schapiro issued a statement on the modified convergence strategy in which she outlined her support for the boards' view that increased time to allow stakeholders the ability to contribute quality feedback would be time well invested. In her statement, Ms. Schapiro noted that she did believe that the change in the boards' strategy would affect the SEC's 2011 date for determining whether to incorporate IFRSs into the U.S. capital markets for domestic issuers.

Therefore companies should continue to think about the potential effect of IFRSs, including potential differences between IFRSs and U.S. GAAP that may remain even after convergence. As U.S. practitioners know, the guidance in U.S. GAAP is often rules based, while that under IFRSs is generally more principles based. This may prove to be an interesting challenge as U.S. accounting and finance professionals reconsider the role of judgment rather than rely on guidance that is often highly prescriptive. Professional judgment will become more important by necessity, and practitioners will need to fully consider and document the facts and circumstances they relied on in reaching an accounting conclusion.

IFRSs also present particular technical accounting challenges to P&U sector companies, as discussed below.

Regulatory Assets and Liabilities

IFRSs do not presently provide specific guidance on regulatory assets and liabilities or on the recognition of revenues and expenses covered by future increases and decreases in regulated tariffs. However, on July 23, 2009, the IASB issued an ED of a proposed standard on rate-regulated activities (RRAs). In contrast to ASC 980, this ED requires:

- That a probability-weighted cash flow approach be used to initially measure and record regulatory assets and liabilities in each subsequent reporting period on the basis of the expected present value as opposed to their being recognized in their entirety if recovery is probable.

- That an impairment evaluation be performed in accordance with IAS 36 when it is reasonable to assume that sufficient revenues cannot be collected to recover the entity's costs. (Under U.S. GAAP, inability to collect sufficient revenues to cover an entity's costs and earn a reasonable return is a matter of scope that would require the utility to cease regulatory accounting.)

- More extensive disclosures than those currently required by U.S. GAAP, including a tabular reconciliation of each category of regulatory asset or liability from the beginning of the period to the end.

The comment period on the ED ended on November 20, 2009. The IASB received 155 comment letters with diverse views, both supporting and opposed to the proposed RRA standard.

During the first half of 2010, the IASB staff conducted additional research and analysis on the key issue of the recognition of regulatory assets and liabilities. At the IASB's July and September 2010 meetings, the staff reported that the results of the additional research and analysis had not provided a clear direction for the project. Furthermore, in the staff's opinion, (1) regulatory assets did not meet the requirements for separate recognition as specified in IAS 38 and (2) regulatory liabilities did not meet the definition of a provision in IAS 37 or the definition of financial assets or liabilities. In accordance with the staff's recommendations, the IASB considered whether to finalize the project by issuing a final standard that confirms that IFRSs do not permit the recognition of regulatory assets or liabilities and require specific disclosures about the impact of regulations on an entity's activities. The IASB further considered a proposal to incorporate into future comprehensive projects, either as part of the conceptual framework project or as part of a review of the accounting for intangible assets, the issue of how the effects of rate regulation should be accounted for. It was observed that RRAs clearly are a difficult area and that it was possible to make a case in any direction. Several IASB members noted that further analysis was required related to the broader question of accounting for intangible assets.

The IASB Chairman summarized the discussion, observing that the IASB was split and that there were a number of considerations that could be added to the staff's analysis. The Chairman was adamant that the IASB could not continue doing further analysis on the matter indefinitely and suggested that the IASB consider the following alternatives:

- A disclosure-only standard on RRAs.

- An interim standard (similar to IFRS 4 or IFRS 6) in which to grandfather previous GAAP accounting practices with some limited improvements.

- A medium-term project to add to the post-2011 agenda, focused only on the effects of rate regulation.
- A comprehensive project on the accounting for intangible assets.

The IASB did not decide on any alternative but rather chose to include in its public consultation on its future agenda a request for views on what form a future project might take, if any, to address RRAs.

PP&E

Asset Componentization

IAS 16 requires entities to identify the significant components of an asset and then depreciate those components separately from the larger asset if they have differing patterns of benefits. This components approach means that different depreciation periods will be used for different components of a fixed asset. For example, a power plant may consist of a number of separate components with different useful lives (e.g., turbine rotor, turbine blades, boiler, electronic equipment) so that its total book value would be allocated to these separate components. These individual components would then be depreciated over their respective useful lives. Significant parts of an asset with similar useful lives and patterns of consumption may be grouped together as long as an entity can separately identify components for potential impairment or retirement purposes.

Entities that currently recognize plant assets as one overall item depreciated over a single 20- or 30-year useful life may find componentization to be a challenging process, especially if the PP&E ledger under U.S. GAAP is not sufficiently detailed or lacks certain key data necessary to specifically identify components. This may be particularly true for old plants, for plants owned by joint ventures (on which data access may be limited), or for acquired assets for which legacy preacquisition data may be limited. Consequently, entities may need to involve plant managers and engineers to review the available asset data, including overhaul and replacement schedules, to complete the componentization process.

The following are other potentially significant effects of asset componentization:

- Group deprecation methods that are commonly used by P&U sector companies will not be permitted, so all gains and losses on retirements must be recognized in earnings.
- Assets related to planned major maintenance activities need to be identified as separate components if they meet the asset recognition requirements in IAS 16. For example, entities would need to identify the costs of estimated major maintenance or overhaul that is scheduled to be performed every five years that would typically be expensed under U.S. GAAP as a separate component upon acquisition of an asset and depreciate such costs separately rather than depreciate the entire cost of the asset over the longer useful life of the asset. When the major maintenance is performed, that component would be retired and the major maintenance cost incurred would be capitalized as a new component.

Revaluation Option

IFRSs allow entities to choose to account for PP&E under either the historical cost model (in a manner similar to the required model under U.S. GAAP) or a revaluation model. Although the revaluation model is not widely used under IFRSs, if it is elected, entities would remeasure PP&E at fair value and record changes in value directly to equity (to the extent that a net revaluation surplus remains) on a recurring

Attachment 3 to CWS PHC Statement

IASB September 2010

At its September 2010 meeting, the Board continued its discussions on rate-regulated activities. The Board received papers that focused on:

- whether the effect of regulators should be analysed in the context of IAS 38 *Intangible Assets* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.
- whether the effect of regulators should be recognised in financial statements that are prepared in accordance with existing IFRSs.
- the status of the Rate-regulated Activities project as a stand-alone project.
- whether IFRSs should be amended to require specific disclosure requirements related to the impact of regulations on an entity that is subject to regulations.

The Board did not reach conclusions on any technical issues at this meeting.

The Board reconfirmed its earlier view that the matter could not be resolved quickly. Accordingly the Board decided that the next step should be to consider whether to include rate regulated activities in its future agenda.

The Board therefore decided to include in its public consultation on its future agenda a request for views on what form a future project might take, if any, to address rate-regulated activities. The feedback received will assist the Board in setting its future agenda. The potential future steps include, but are not limited to:

- a disclosure only standard
- an interim standard, similar to IFRS 4 *Insurance Contracts* or IFRS 6 *Exploration for and Evaluation of Mineral Resources*, to grandfather previous GAAP accounting practices with some limited improvements
- a medium term project focused on the effects of rate-regulation
- a comprehensive project on intangible assets.

Location: **London UK**

Date: **16/09/2010**

Observer Notes

- Zip of agenda papers 12 to 12D: Rate-regulated Activities: Cover note, summary and questions for the Board