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October 2, 2023

Private and confidential

Ryan Kolaski, Chief Financial Officer
Manitoba Public Insurance Corporation
820-234 Donald Street
Winnipeg MB R3C 4A4

Subject: Applicability of International Financial Reporting Standard (“IFRS”) 14

Dear Ryan,

Scope of Engagement

Deloitte LLP (“**Deloitte**” or “**we**” or “**us**” or “**our**”) was retained by Manitoba Public Insurance Corporation (“**MPI**”) to provide an evaluation on the application of IFRS 14, *Regulatory Deferral Accounts*, (“**IFRS 14**”) as issued by the Canadian Accounting Standards Board (“**AcSB**”) for regulatory filings with the Manitoba Public Utilities Board (the “**PUB**” or “**Board**”). Specifically, MPI has requested we report on the appropriateness of the application of IFRS 14 in response to information requests made by the PUB to permit the use of deferral accounts in MPI’s 2024 General Rate Application (the “**GRA**”).

This engagement was performed in accordance with Section 7600, *Reports on the Application of Accounting Principles* (“**Section 7600**”) of the CPA Canada Handbook, Assurance, Other Canadian Standards. When preparing this Report (“**the Report**”) we have met the following professional standards:

1. The work and this Report was performed by individuals who have adequate technical training, are proficient in the subject matter, who exercised due care, and had an objective state of mind.
2. The work was adequately planned and properly executed, and assistants, when employed, were properly supervised.
3. Sufficient appropriate information was obtained to afford a reasonable basis to support the content of this Report.

Information Relied Upon

In performing our analysis, we have relied upon information contained in three chief sources:

1. Accounting literature cited.
2. Documents listed in Appendix A.
3. The facts, circumstances and assumptions listed below.

Accounting Question Posed by MPI

MPI has asked Deloitte to respond to the following question (the “Question”):

- Can MPI apply the guidance in IFRS 14 and begin recognizing regulatory deferral accounts for its rate-regulated activities associated with MPI 2024 GRA filed with the PUB?

Relevant Facts, Circumstances, and Assumptions

When rendering our opinion on the application of IFRS 14, we relied on the following facts, circumstances and assumptions obtained from public records or/and provided by MPI management:

- MPI is a Crown corporation that operates an automobile insurance division. The automobile insurance division is subject to rate regulation under *The Crown Corporations Public Review and Accountability Act*. The PUB is the regulator of MPI and has the authority to review and approve Basic Insurance rates, premiums, and service fees charged with respect to compulsory driver and vehicle insurance provided by MPI.¹
- MPI adopted IFRS, as endorsed by the AcSB and published in Part I of the CPA Canada Handbook, for the first time in their 2011 consolidated financial statements. Previously MPI reported under Canadian generally accepted accounting principles (“GAAP”) as issued by CPA Canada.²
- Prior to the adoption of IFRS, MPI did not apply rate regulated accounting under Canadian GAAP, ‘AcG-19 Disclosures by entities subject to rate regulation’ and therefore did not recognize regulatory deferral accounts.
- In January 2014, the International Accounting Standards Board issued IFRS 14 Regulatory Deferral Accounts. IFRS 14 permits a first-time adopter of IFRS Standards that is within its scope to continue to recognize and measure its regulatory deferral account balances in its first and subsequent IFRS financial statements in accordance with its previous GAAP.³ The AcSB endorsed the standard at it was incorporated into Part I of the CPA Canada Handbook in April 2014.
- In the 2019 GRA, MPI reported that it was assessing their legacy system to determine if they were eligible for system modernization. MPI conducted a legacy systems modernization (the “LSM”) assessment where the purpose was to:⁴

- 1. Perform a detailed assessment of our core systems and their associated business processes.*
- 2. Perform an industry survey of available technologies in both the Property & Casualty Insurance policy issuance and claims administration, and in the Driver and Vehicle Administration domain.*
- 3. Create a set of recommendations and guidelines defining how to transform MPI’s legacy systems to meet long term business needs and close identified gaps in business and IT capabilities.*
- 4. Create an Application Strategy that outlines how MPI will address the proposed recommendations for transforming MPI’s legacy systems to meet long term business needs.*
- 5. Create a detailed comprehensive Business Case that outlines the costs, benefits, and risks for implementing and then operationalizing the solution defined by the Application Strategy.”*

¹ Manitoba Public Insurance Corporation, 2011 Annual Report and Annual Financial Statements

² Manitoba Public Insurance Corporation, 2011 Annual Report and Annual Financial Statements

³ CPA Canada Handbook, Part I – IFRS Standards, IFRS 14: Regulatory deferral accounts, paragraph 3

⁴ 2023_02_11_review and Vary_4_23

MPI also noted, “Some of the drivers of this assessment are the evolving customer expectations on service delivery, product and service flexibility and agility, and application risk. Given the pervasiveness of our legacy systems within our technology infrastructure, the outcome of this assessment may have a significant impact on our IT roadmap and how IT capabilities are created for the next several years.”

- In 2020, MPI rebranded LSM as “Project Nova” and introduced it to the PUB within its 2020 GRA.
- Project Nova was the largest transformation project in the history of MPI.⁵ MPI continues to depreciate these costs over time, in accordance with IFRS.⁶ The total cost associated by Project Nova by Line of Business are as follows:⁷

'000s	'18/'19A	'19/'20A	'20/'21A	'21/'22A	'22/'23A	'23/'24F	'24/'25F	'25/'26F	'26/'27F	'27/'28F
Basic	99	2,043	10,546	23,801	7,658	13,709	10,008	3,678	342	503
Extension	8	172	877	1,959	7,658	13,709	10,008	3,678	206	303
SRE	6	125	683	1,610	16,592	9,509	6,686	2,838	430	632
DVA	23	914	6,749	27,043	20,493	20,843	5,258	919	325	478
Total	136	3,254	18,855	54,413	52,402	57,771	31,960	11,113	1,303	1,916

- On January 11, 2023, the PUB issued Order 4/23 directing MPI to defer expenses for (1) certain initiatives related to Project Nova and (2) other expenses unrelated to Project Nova until Project Nova is fully in-service.⁸ More specifically, these expenses included initiatives related to the implementation of Generalized Linear Modelling.⁹ Order 4/23 included the following specific directives:
- Directive 12.1(d):¹⁰

“There shall be an overall 3.8% rate decrease in compulsory vehicle insurance premiums for the 2023/24 insurance year, effective April 1, 2023, for all major classes combined. This rate decrease is, as derived in accordance with Accepted Actuarial Practice in Canada, based on a Naïve interest rate forecast taking into account interest rates as at August 31, 2022. This rate decrease is a combination of the 0.05% rate decrease as requested by MPI, along with the additional impact on the AAP rate indication of the following items:

d. The expense forecast for 2023/24 and 2024/25 for rate-setting purposes is to be adjusted by the removal of all initiative expenses.”¹¹
- Directive 12.1 also instructed MPI to defer all integration costs related to Project Nova through a regulatory deferral account for rate setting purposes and included the following:¹²

“Based on MPI Exhibit #96, the total for 2023/24 is \$21.6 million, and is \$25.7 million for 2024/25, or an average of \$23.7 million[...]. The Board therefore directs MPI to defer these integration costs, through a regulatory deferral account for rate-setting purposes. The account will accumulate the integration costs and will be recovered when Project Nova is fully in-service. The period of recovery will be established in

⁵ Part_02_04_OV_01_Overview_Chapter

⁶ 2023_02_11_review and Vary_4_23

⁷ 2024 GRA https://apps.mpi.mb.ca/Rate-Application/2024/GRA/2024_GRA.pdf

⁸ Order No.4/23

⁹ 2023_02_11_review and Vary_4_23

¹⁰ The PUB provides Board Orders which are the Board’s decisions, recommendations and reasoning (The Public Utilities Board, Board Orders). Directives are instructions by the Board within Board Orders

¹¹ Order No.4/23

¹² 2023_02_11_review and Vary_4_23

the 2024 General Rate Application, when MPI is expected to provide an updated timeline for the delivery of Project Nova.”

- On February 10, 2023 as part of MPI’s 2023 GRA, MPI requested that Directive 12.1(d) be varied to allow MPI to:¹³

*“1. Continue to defer expenses related to its initiatives as per its existing methodology.¹⁴
2. Recover from ratepayers in the 2024 GRA, the average amount the PUB directed it to defer in the 2023 GRA (i.e., \$23.7 million).”*

- On June 15, 2023, the PUB reaffirmed that MPI defer all costs, from all improvement initiatives including but not limited to Project Nova through a regulatory deferral account in their 2024 GRA.¹⁵ MPI notes within their 2024 GRA that, *“MPI intends to adjust its financial forecasts (for the regulatory purposes) taking in consideration the deferral account for the purposes of GRAs. However, MPI is not eligible to apply International Financial Reporting Standards (IFRS) 14, impacting its financial statements. As a result, this will create a misalignment between rates approved by the PUB (based on forecasts) and MPI financial statements.”*¹⁶
- On August 2, 2023, in its 2024 General Rate Application, MPI affirmed that its rate regulated activities cannot be accounted in accordance with IFRS 14 for the following reasons:¹⁷
 - 1. MPI did not report regulatory deferral account balances¹⁸ under previous GAAP.¹⁹*
 - 2. MPI did not apply IFRS 14 in its first IFRS financial statements issued for the fiscal year ended March 31, 2011.²⁰*
- Following MPI’s response on their inability to adopt IFRS 14, the PUB is requesting MPI provide their assessment and analysis on why they believe MPI cannot adopt IFRS 14.

Authoritative Support

The established practice in IFRS has been that rate-regulated entities do not recognize regulatory deferral accounts in IFRS financial statements.²¹ This is because some regulatory deferral account balances are specifically prohibited from being recognized as assets and liabilities by other IFRS standards.²²

In 2008, the IASB added a project on rate-regulated activities to its agenda and subsequently, in July 2009, published an Exposure Draft Rate-regulated Activities (the ‘2009 ED’) to consider whether rate regulated accounting can be applied under the IFRS framework. In September 2010, the IASB decided that the complex technical issues could not be resolved quickly, and suspended the project until it had considered whether to include rate-regulated activities in its future agenda.

¹³ 2023_02_11_review and Vary_4_23

¹⁴ 2023_02_11_review and Vary_4_23 indicates MPI’s existing methodology to depreciate administrative capital costs over time, in accordance with IFRS

¹⁵ Part_02_04_OV_01_Overview_Chapter

¹⁶ Part_02_04_OV_01_Overview_Chapter

¹⁷ PUB1_014

¹⁸ IFRS 14, Appendix A defines Regulatory deferral account balances as “[t]he balance of any expense (or income) account that would not be recognised as an asset or a liability in accordance with other Standards, but that qualifies for deferral because it is included, or is expected to be included, by the rate regulator in establishing the rate(s) that can be charged to customers”

¹⁹ Manitoba Public Insurance Corporation, 2011 Annual Report and Annual Financial Statements

²⁰ Manitoba Public Insurance Corporation, 2011 Annual Report and Annual Financial Statements

²¹ IFRS 14, Paragraph BC28

²² IFRS 14, Paragraphe BC30

In September 2012 the IASB decided to add to its agenda a comprehensive project on rate-regulated activities to investigate these complex issues. It also decided, in December 2012, to develop an interim Standard on the accounting for regulatory deferral accounts that would apply until the completion of the comprehensive project. IFRS 14 is the interim Standard issued as a result of that decision.

The sole objective of the issuance of IFRS 14 was to **permit eligible first-time adopters of IFRS to continue** to account for regulatory deferral account balances **in accordance with their previous GAAP**, both on initial adoption of IFRS and in subsequent financial statements.²³

This objective is stated in the scope section of IFRS 14 in paragraph 5 (emphasis added):

*"An entity is permitted to apply the requirements of this Standard in its first IFRS financial statements **if and only if** it:"²⁴*

a. Conducts rate-regulated activities.²⁵

*b. Recognized amounts that **qualify as regulatory deferral account balances in its financial statements in accordance with its previous GAAP.**"*

Furthermore, IFRS 14.6 states that (emphasis added): *"An entity shall apply the requirements of this Standard in its financial statements for subsequent periods **if and only if, in its first IFRS financial statements, it recognised regulatory deferral account balances** by electing to apply the requirements of this Standard."²⁶*

Therefore, the following points should be considered as they relate to MPI's eligibility to adopt IFRS 14 in any period after the issuance of the first IFRS financial statements:²⁷

- An entity that adopts IFRS and is eligible but elects to not apply IFRS 14 in those first IFRS financial statements is not allowed to adopt IFRS 14 in subsequent periods.
- An entity that adopted IFRS for the first time prior to the issuance of IFRS 14, in January 2014, cannot apply IFRS 14.

²³ Deloitte iGAAP, Volume A, Section A42, 1.1

²⁴ IFRS 14, paragraph 5

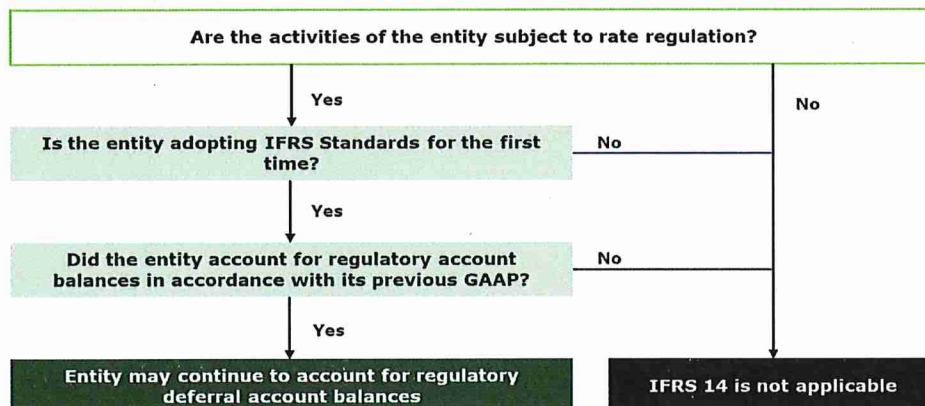
²⁵ IFRS 14, Appendix A defines Rate-regulated activities balances as "[a]n entity's activities that are subject to rate regulation" which in turn is defined as "[a] framework for establishing the prices that can be charged to customers for goods or services and that framework is subject to oversight and/or approval by a rate regulator"

²⁶ IFRS 14, paragraph 6

²⁷ Deloitte iGAAP, Volume A, Section A42, 2.5

Figure 1 below summarizes the conditions required for an entity to be eligible to record regulatory deferral accounts under IFRS 14.

Figure 1 – IFRS 14 scope summary²⁸



Supporting Rationale

There are two reasons why MPI is unable to recognize regulatory deferral accounts in its current or future financial statements:

1. IFRS 14 is explicit that it can only be applied by an entity when it issues its first IFRS financial statements. IFRS defines the first IFRS financial statements as the first annual financial statements in which an entity adopts International Financial Reporting Standards (IFRSs), by an explicit and unreserved statement of compliance with IFRSs.²⁹ MPI adopted IFRS and issued its first IFRS financial statements for the fiscal year ending March 31, 2011. IFRS 14 was not issued until 2014 and therefore MPI was not able to apply IFRS 14 when it prepared and issued its first IFRS financial statements. This IFRS 14 application eligibility condition is not met by MPI.
2. IFRS 14 has a very narrow and restrictive scope which also stipulates that an entity is only eligible to adopt the standard in its first IFRS financial statements if the entity had recognized regulatory deferral accounts under its previous GAAP. MPI did not meet this eligibility criteria in IFRS 14 at any time including when it issued its first IFRS financial statements, when IFRS 14 was first issued, or as of the current date because it did not recognize any regulatory deferral accounts in its last Canadian GAAP financial statements issued for the fiscal year ended March 31, 2010 or in any prior year.

²⁸ KPMG Insights into IFRS, 19th Edition 2022/23, Section 6 First time adoption of IFRS Standards, 6.2.10.20
²⁹ IFRS 1 First time adoption of International Financial Reporting Standards, Appendix A

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Opinion

The ultimate responsibility for the decision on the appropriate application of IFRS for the specific transaction described above rests with your management as preparers of the financial statements, who should consult with their financial statement auditors. Our judgment on the appropriate application IFRS for the specific transaction described above is based on the facts, circumstances and assumptions provided. Should the facts, circumstances or assumptions differ, our conclusion may change. Our views on the application of IFRS 14 are based on the accounting standards in place as of the date of this Report. We do not assume any obligation to update this Report for subsequent changes in relevant accounting standards, rules or practice.

In our opinion, MPI is not eligible to apply the guidance of IFRS 14 and begin recognizing regulatory deferral accounts for its rate-regulated activities associated with MPI's 2024 GRA filed with the PUB.

This report is intended solely for the information and use of management of Manitoba Public Insurance Corporation and Manitoba Public Utilities Board, and is not intended to be and should not be used by anyone other than these specified parties or for any other purpose. This Report is not intended for circulation or publication, nor is it to be reproduced for any purpose other than as described herein, without our prior express written permission in each specific instance.

Yours very truly,

Deloitte LLP

Chartered Professional Accountants

David Dalziel
Partner, Assurance & Advisory
Toronto, ON
October 2, 2023

Enclosure

Appendix A – Information Relied Upon

In drafting this Report, we reviewed the following documents and applicable literature:

- PUB2_012
- PUB1_014
- PUB1_014_Appendix_1_IFRS 14 Regulatory Deferral Accounts
- PUB1_054
- Order No. 4/23
- CAC1_001
- CAC1_083
- CAC2_018
- 2023_02_11_Review_and_Vary_4_23
- Part_02_04_OV_01_Overview_Chapter
- PUB1_014_Appendix_2_Exposure Draft Rate Regulated Assets and Liabilities
- IFRS 14 – Regulatory deferral accounts
- 2024 General Rate Application
- Deloitte iGAAP, Volume A – A guide to IFRS reporting, A42 Regulatory deferral accounts
- KPMG Insights into IFRS, 19th Edition 2022/23
- Manitoba Public Insurance Corporation, 2010 Annual Report and Annual Financial Statements
- Manitoba Public Insurance Corporation, 2011 Annual Report and Annual Financial Statements
- Manitoba Public Insurance Corporation, 2012 Annual Report and Annual Financial Statements
- Manitoba Public Insurance Corporation, 2022 Annual Report and Annual Financial Statements