



IFRS® Foundation

Exposure Draft *Regulatory Assets and Regulatory Liabilities*

Emerging Economies Group meeting

EEG Agenda ref 1
May 2021

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Purpose of this session

Agenda ref 1

Background

- Exposure Draft *Regulatory Assets and Regulatory Liabilities* published in January 2021
- Comment period of 180 days ending on 30 July

Purpose

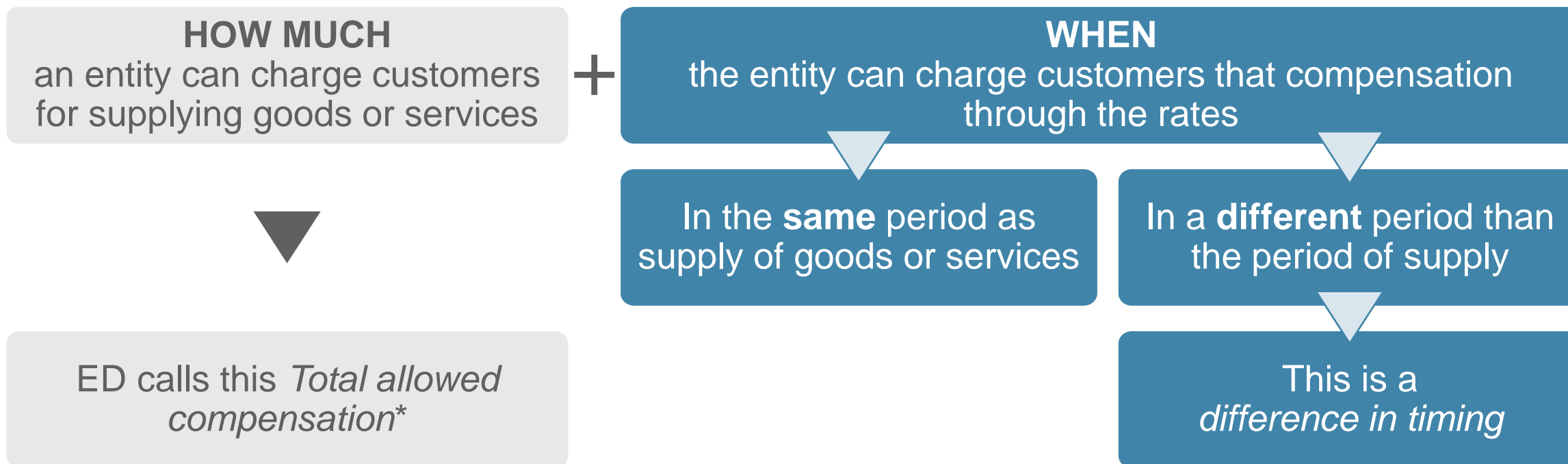
- The staff are seeking feedback on the main proposals in the Exposure Draft
- Questions for EEG members are on slides 13, 19, 23, 26, 29, 33, 37, 40, 43 and 46

A grayscale world map is the background for the slide. Overlaid on the map are several thick, light gray curved lines that sweep across the continents. Additionally, there are several dotted lines that form a grid-like pattern across the map, intersecting the curved lines.

Problem definition

What is the problem? (1/3)

A regulatory agreement establishes



* See Appendix for the full definition of *total allowed compensation* for goods or services supplied

What is the problem? (2/3)

Illustration

- Entity A charges a regulated rate, for goods supplied in Year 1, set based on estimated input costs of CU100*
- Actual input costs for Year 1 were CU120
- Estimated and actual input costs for Year 2 were CU100
- Entity A has a right given by regulatory agreement to add under-recovery of CU20 of input costs of Year 1 in regulated rate for Year 2

Total allowed compensation for goods or services supplied in the two years would include:

	Year 1 CU	Year 2 CU
Total allowed compensation	120	100

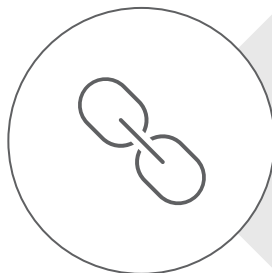
Applying IFRS Standards, Entity A's Statement of profit or loss would include:

	Year 1 CU	Year 2 CU
Revenue	100	120
Input costs	(120)	(100)
Profit (loss)	(20)	20

* Monetary amounts are denominated in 'currency units' (CU).

What is the problem? (3/3)

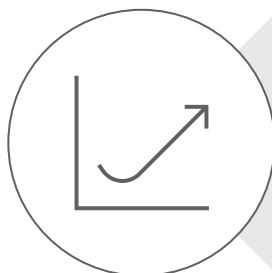
Without information about *differences in timing* users of financial statements have *insufficient basis*—



To understand revenue-expenses relationship



To analyse financial performance



To make projections of future cash flows

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Proposed solution

How does the Board propose to solve the problem? (1/2)

Agenda ref 1

When the regulatory agreement requires an entity to charge compensation in a different period (a difference in timing), a regulatory asset or regulatory liability arises

Regulatory asset is a right to add amount in future rates because of goods or services already supplied*

Regulatory liability is an obligation to deduct amount in future rates because of compensation already charged*

An entity would report:

- regulatory assets and regulatory liabilities in statement of financial position
- regulatory income and regulatory expense in statement of financial performance



Reflect *total allowed compensation for goods or services supplied as part of reported financial performance for the period in which those goods or services are supplied*

* See Appendix for a summary of the proposed model and full definitions of *regulatory asset* and *regulatory liability*

How does the Board propose to solve the problem? (2/2)

Agenda ref 1

Illustration

(Amounts in CU)

Statement of profit or loss

	Year 1	Year 2
Revenue	100	120
Regulatory income minus regulatory expense	20	(20)
Input costs	(120)	(100)
Profit (loss)	-	-

- **Regulatory income CU20 in Year 1** to reflect compensation for goods supplied in Year 1
- **Regulatory expense CU20 in Year 2** to reflect compensation in rates of Year 2 for goods of Year 1

Statement of financial position

	Year 1	Year 2
Assets		
...		
Regulatory asset	20	-

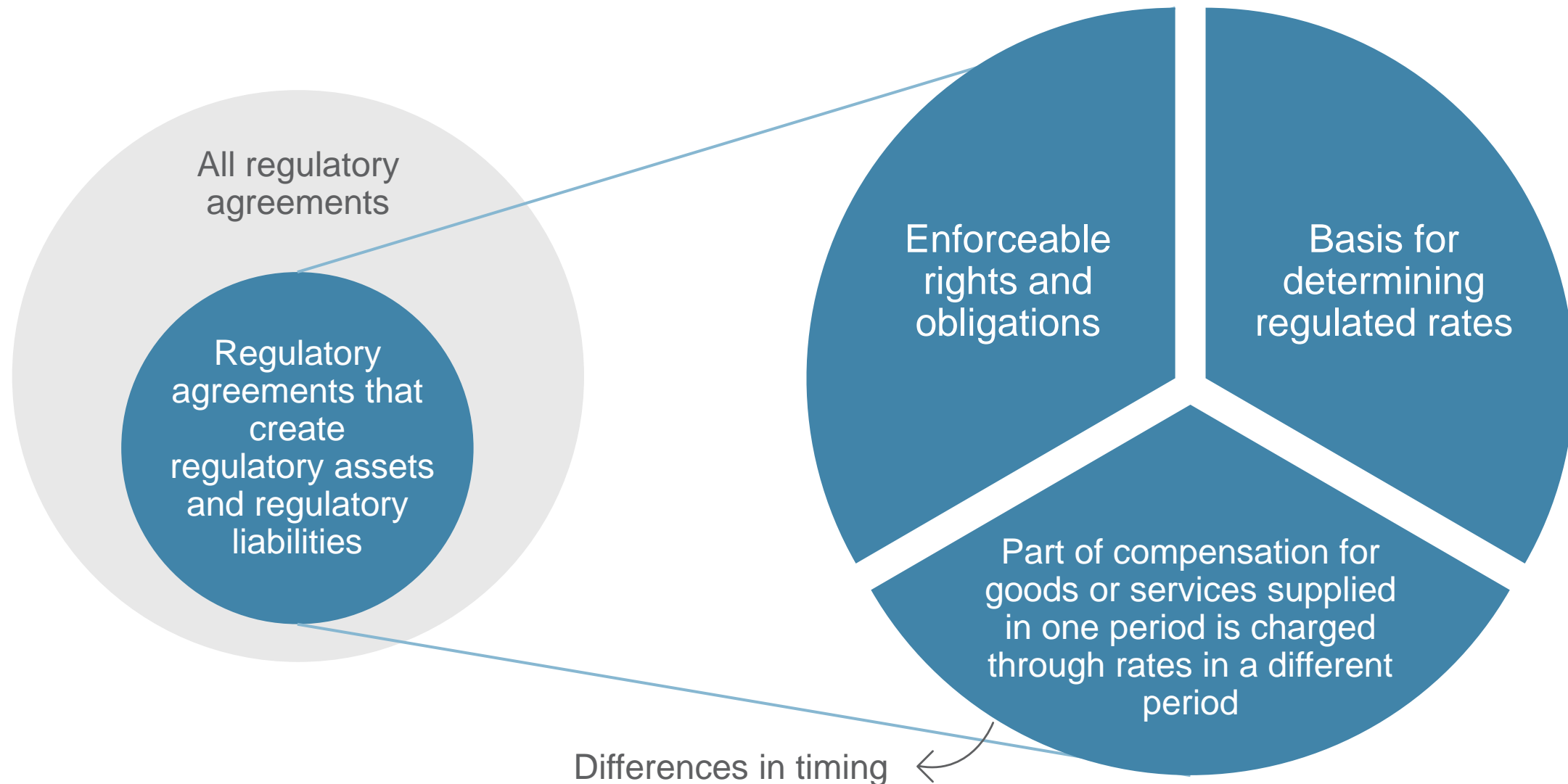
- **Regulatory asset of CU20 in Year 1** to reflect right to increase regulated rates in Year 2
- **No regulatory asset in Year 2** because rates increased to recover under-recovered CU20 of Year 1



Board's proposals

Scope

Regulatory agreements that create...



Questions for EEG—Scope

Agenda ref 1

1

Do you agree with the proposed scope?

2

Are the scope proposals clear enough to enable an entity to determine whether a regulatory agreement gives rise to regulatory assets and regulatory liabilities?

3

Do you foresee assessing whether rights and obligations are enforceable would be challenging? If so, what are the circumstances that make such assessment challenging?

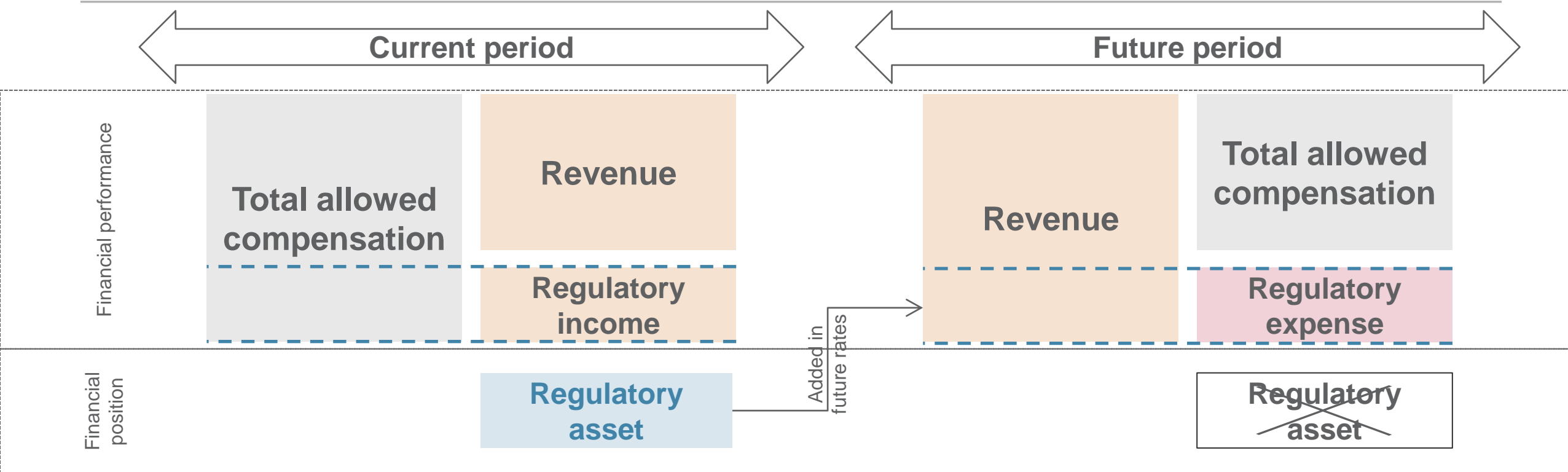


Board's proposals

Regulatory assets and regulatory liabilities

Regulatory assets (1/2)

Agenda ref 1



Regulatory asset Dr
 Regulatory income (Cr)

Under-recovery of compensation in current period creates regulatory asset



Regulatory expense Dr
 Regulatory asset (Cr)

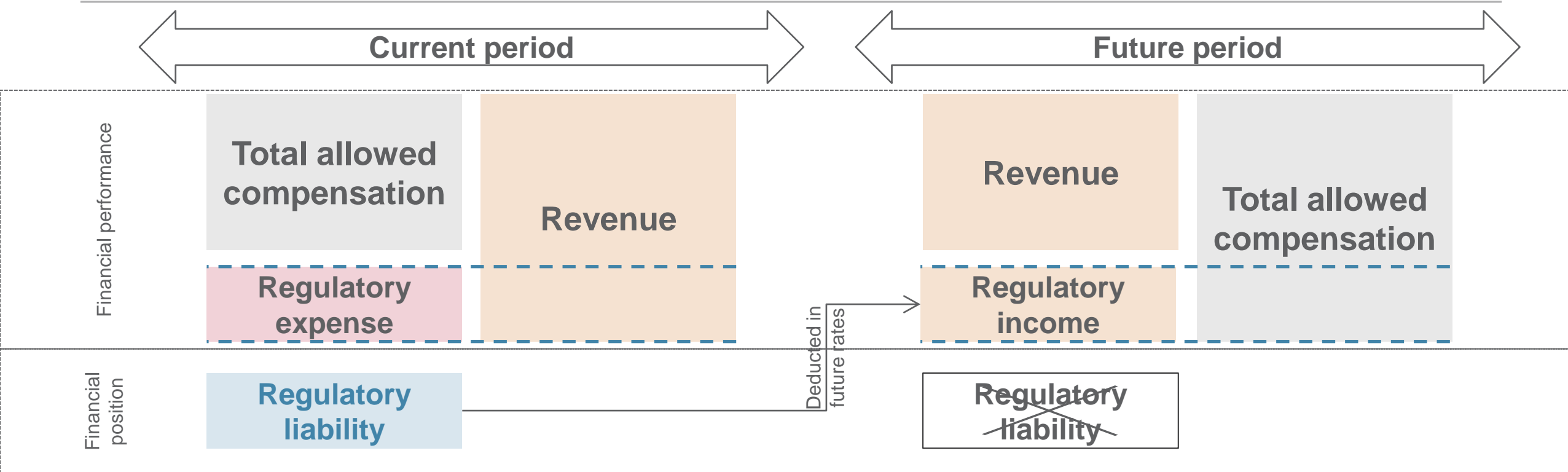
Generates cash inflows when regulated rates increased in future period

Regulatory assets (2/2)

Example RA1	Example RA2	Example RA3
<p>The rate an entity charges customers during the current period includes an estimated amount of input costs. Actual input costs incurred in that period exceeded this estimate.</p> <p>The regulatory agreement gives the entity the right to add that under-recovery of input costs in the rates to be charged to customers in the future.</p>	<p>An entity incurs an obligation for environmental clean-up costs during the current period.</p> <p>The rates charged to customers during the current period did not include the environmental costs incurred. The regulatory agreement gives the entity the right to recover those costs by adding them in the rates only when it pays the related cash in the future.</p>	<p>A regulatory agreement entitles an entity to a bonus because it met specified performance criteria in the current period.</p> <p>The rates charged to customers during the current period did not include the bonus. The regulatory agreement gives the entity the right to recover the bonus by adding it in the rates to be charged to customers in the future.</p>

Regulatory liabilities (1/2)

Agenda ref 1



Regulatory expense Dr
 Regulatory liability (Cr)

Regulatory liability Dr
 Regulatory income (Cr)

Over-recovery of compensation in current period creates regulatory liability



Generates lower cash inflows when regulated rates decreased in future period

Regulatory liabilities (2/2)

Agenda ref 1

Example RL1	Example RL2	Example RL3
<p>The rate an entity charges customers during the current period includes an estimated amount of input costs. Actual input costs incurred in that period were lower than this estimate.</p> <p>The regulatory agreement obliges the entity to deduct that over-recovery of input costs in the rates to be charged to customers in the future.</p>	<p>A regulatory agreement entitles an entity to recover part of the construction cost of an asset through the rates charged to customers ('pre-funding') in the current period. The asset was not yet available for use in the current period.</p> <p>The regulatory agreement obliges the entity to deduct the amount of the pre-funding in the rates to be charged to customers in the future.</p>	<p>A regulatory agreement imposes a penalty on an entity because it failed to meet specified performance criteria in the current period.</p> <p>The rates charged in the current period did not reflect the penalty. The regulatory agreement obliges the entity to deduct the amount of the penalty in the rates to be charged to customers in the future.</p>

4

Do you agree with the proposed definitions for regulatory assets and regulatory liabilities^(*)?

* The Appendix includes the proposed definitions of *regulatory asset* and *regulatory liability*.

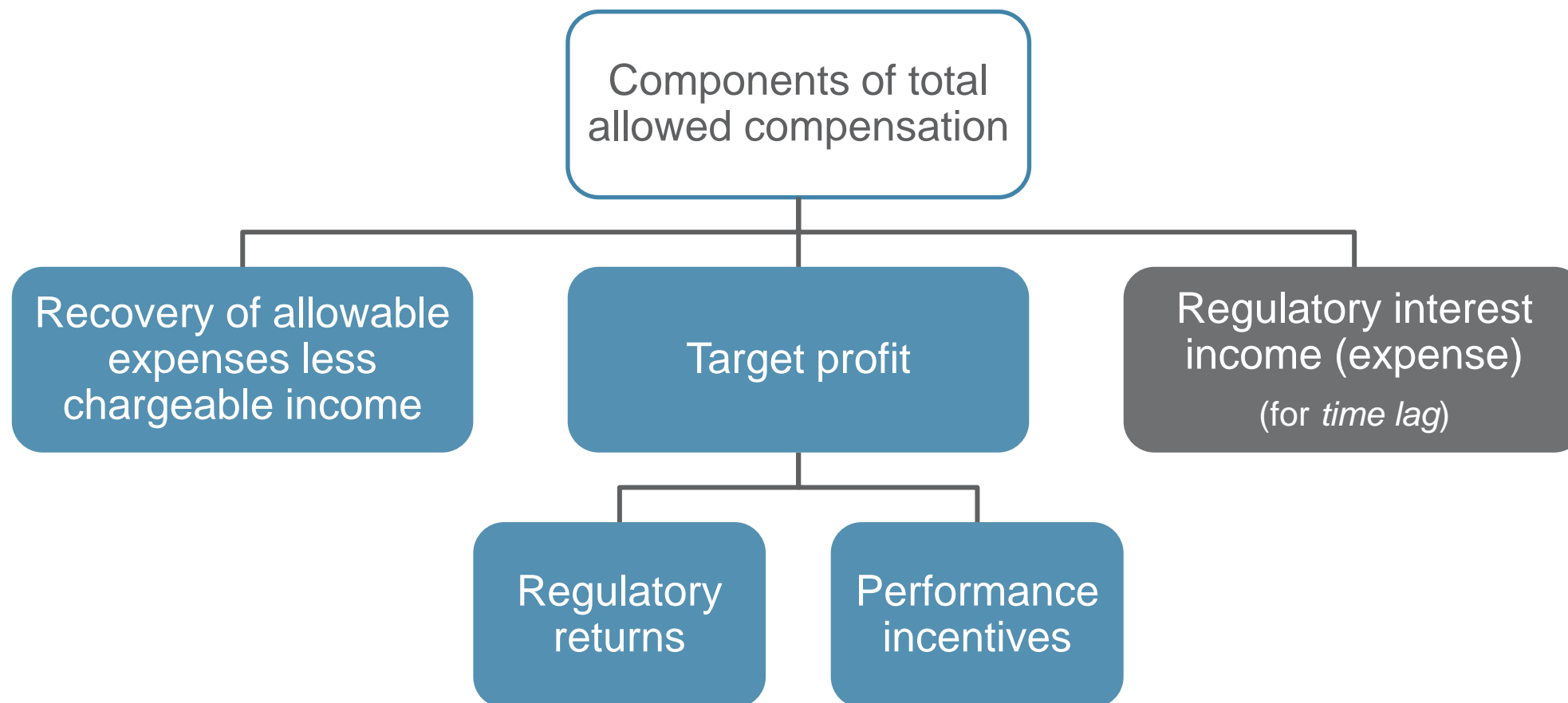
A grayscale world map is the background for the slide. Overlaid on the map are several thick, curved, light-gray lines that sweep across the continents. Additionally, there are dotted lines forming a grid-like pattern across the map, suggesting latitude and longitude.

Board's proposals

Total allowed compensation
for goods or services

Components of total allowed compensation (1/2)

Agenda ref 1



Components of total allowed compensation (2/2)

Agenda ref 1

When components of total allowed compensation affect profit

Recovery of allowable expenses less chargeable income	Target profit		Regulatory interest income (expense) (for time lag)
	Regulatory returns*	Performance incentives	
When expense or income are recognised applying IFRS Standards	When an entity is entitled to add returns in setting regulated rates	When performance gives rise to the incentive bonus or penalty	As discount unwinds until recovery of regulatory asset (or fulfilment of regulatory liability)

* Regulatory returns on an asset not available for use affect profit:

- only once the asset is available for use
- over the remaining periods in which the asset is recovered through the regulated rates

5

Do you agree with the focus of the proposals on total allowed compensation for goods or services supplied in a period?

6

Do you agree with the proposals on how an entity would determine total allowed compensation for goods or services supplied in a period?

7

Is there a need for further guidance on how to apply the concept of total allowed compensation for goods or services?



Board's proposals

Recognition

An entity shall recognise

- All regulatory assets and all regulatory liabilities **existing** at the end of the reporting period.

If it is *uncertain* whether a regulatory asset or a regulatory liability exists, an entity shall recognise the regulatory asset or regulatory liability if it is **more likely than not** that it exists.

Consider all relevant facts and circumstances to determine existence

- Confirmation from the regulator
- Regulatory decisions or court rulings interpreting regulatory agreement
- Entity's experience with regulator's interpretation of the regulatory agreement in similar circumstances
- Experience of other entities regulated by the same regulator
- Preliminary views expressed by the regulator...

8

Do you agree that a 'more likely than not' recognition threshold should apply when it is uncertain whether a regulatory asset or regulatory liability exists?



Board's proposals

Measurement

Cash-flow-based measurement

Agenda ref 1

	Future cash flows	Discount rate
Initial measurement	<p>Include all future cash flows</p> <ul style="list-style-type: none">• if uncertain, estimate using ‘most likely amount’ method or ‘expected value’ method• the cash flows include those from regulatory interest	<p>Discount estimated future cash flows</p> <ul style="list-style-type: none">• using the <i>regulatory interest rate</i>• unless this rate for a regulatory asset is insufficient*
Subsequent measurement	<p>Update estimates of future cash flows</p> <ul style="list-style-type: none">• to reflect recovery of regulatory asset or fulfilment of regulatory liability• for changes in estimates	<p>Continue to use discount rate</p> <ul style="list-style-type: none">• as determined at initial recognition• unless regulatory agreement changes the regulatory interest rate


* For a regulatory asset only, if the regulatory interest rate compensates an entity insufficiently for the time value of money and uncertainty, the discount rate would instead be the **(minimum) rate** that would be sufficient to provide that compensation.

9 Do you agree with the proposed cash-flow-based measurement technique?

10 Do you agree with the proposals that an entity should estimate uncertain future cash flows using whichever of the two methods ('most likely amount' or 'expected value') the entity expects to better predict the cash flows?

11 Do you agree with the proposals for discounting the estimated future cash flows using the regulatory interest rate, except in specified circumstances?

12 Do you agree with the proposals for cases when the regulatory interest rate provided for a regulatory asset is insufficient?



Board's proposals

Presentation and Disclosure

In statement of financial position

- Separate line items for regulatory assets and regulatory liabilities
- Classified as current and non-current

In statement of financial performance

- Regulatory income minus regulatory expense immediately below revenue line item
 - net movement between opening and closing balances of regulatory assets and regulatory liabilities

Presentation—Statement of profit or loss

Agenda ref 1

Illustration

(Amounts in CU)

Statement of profit or loss	Year 1	Year 2
Revenue	100	120
Regulatory income minus regulatory expense	20	(20)
Input costs	(120)	(100)
Profit (loss)	-	-

1

Mostly includes compensation for goods or services supplied in the year, but:

- may not include part of that compensation that is charged in other years (past or future)
- can also include compensation for goods or services supplied in other years (past or future)

2

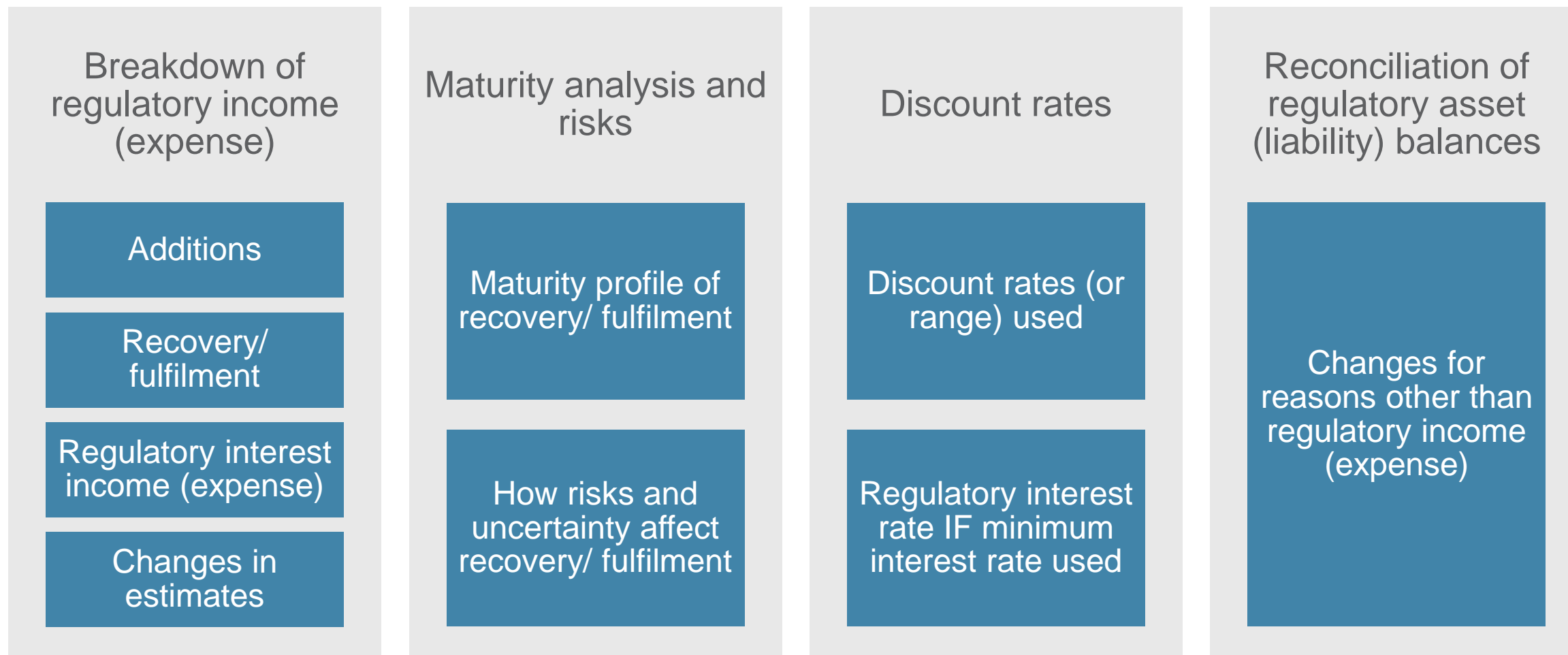
- Compensation included in revenue of other years (past or future) for goods or services supplied in the year; less
- Compensation included in revenue for the year for goods or services supplied in other years (past or future)

13 Do you agree that an entity should present all regulatory income minus all regulatory expense as a separate line item immediately below revenue?

14 Do you agree with the proposed inclusion of regulatory interest income or regulatory interest expense within regulatory income minus regulatory expense?

Proposed objective

- Focus on financial performance
- Information provided by applying ED together with all other information provided in financial statements would enable users of financial statements
 - *to understand the relationship between an entity's revenue and expenses as completely as they can when no regulatory assets or regulatory liabilities exist*
- That understanding would provide users with better insights into the entity's prospects for future cash flows



Disclosure (3/3)

Note X Regulatory income minus regulatory expense

	Year 1 CU	Year 2 CU
Amounts for goods or services supplied in current year:		
—to be included in revenue in future years	20	XX
—already included in revenue in prior years	XX	XX
Amounts included in revenue in current year:		
—for future goods or services	(XX)	(XX)
—for goods or services in prior years	(XX)	(20)
Regulatory interest income on regulatory assets less regulatory interest expense on regulatory liabilities	XX	XX
Changes in estimates	XX	XX
Regulatory income minus regulatory expense	20	(20)

Addition to regulatory assets

Fulfilment of regulatory liabilities

Addition to regulatory liabilities

Recovery of regulatory assets

15 Do you agree with the proposed disclosure objectives and disclosure requirements?

16 Are the proposals worded to make it possible for preparers, auditors, regulators and enforcement bodies to assess whether information disclosed is sufficient to meet the disclosure objectives?



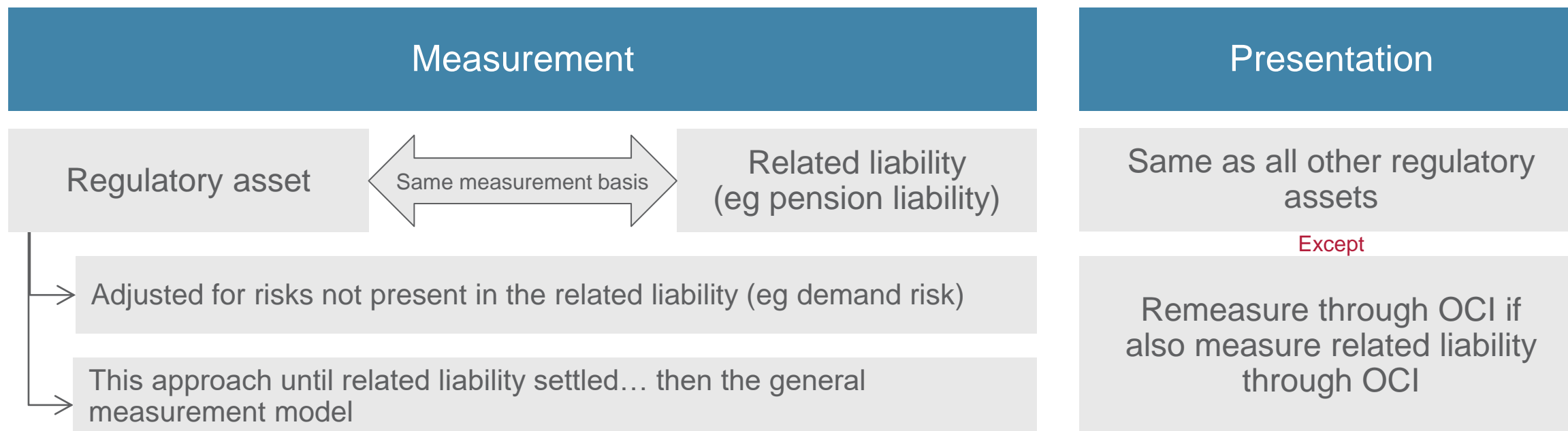
Board's proposals

Measurement and Presentation in one situation

Measurement and Presentation in one situation

Agenda ref 1

Compensation for allowable expenses (eg pension costs) that is included in the regulated rates only when or after related cash is paid*



* Proposals apply equally to chargeable income and any associated regulatory liability

17

Do you agree with the measurement and presentation proposals for regulatory assets and regulatory liabilities discussed on slide 39?



Board's proposals

Interaction with IFRIC 12

- Service concessions within the scope of IFRIC 12 are subject to some form of rate regulation, because the grantor regulates the price to be charged for the services.
- A service concession arrangement may be the form that a regulatory agreement takes.
- Service concession arrangements may create regulatory assets and regulatory liabilities.

18 Do you think some service concession arrangements in your jurisdiction may create regulatory assets and regulatory liabilities? Why?



Board's proposals

Transition

Transition

	Comparative	Date of initial application 1 Jan 20X2
	20X1	20X2
<i>Statement of profit or loss</i>	CU	CU
Revenue	XX	XX
Regulatory income minus regulatory expense	XX	XX
Expenses	(XX)	(XX)
Profit (loss)	XX	XX

← Full retrospective application →

- Full restatement of comparatives
- Data comparable across time periods and entities

19

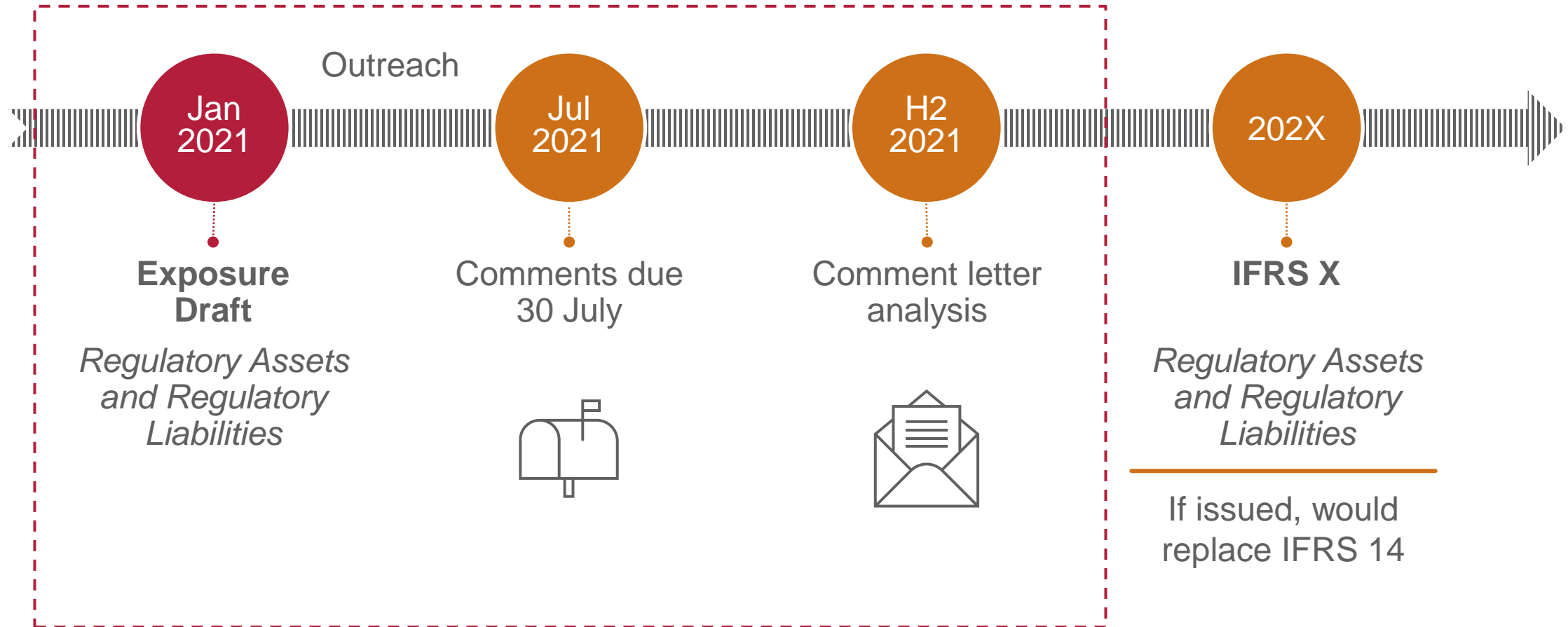
Do you agree with the transition proposals?

A grayscale world map is the background for the slide. Overlaid on the map are several thick, light gray curved lines that sweep across the continents. Additionally, there are several dotted lines that form a grid-like pattern across the map, intersecting the curved lines.

Next steps

Next steps

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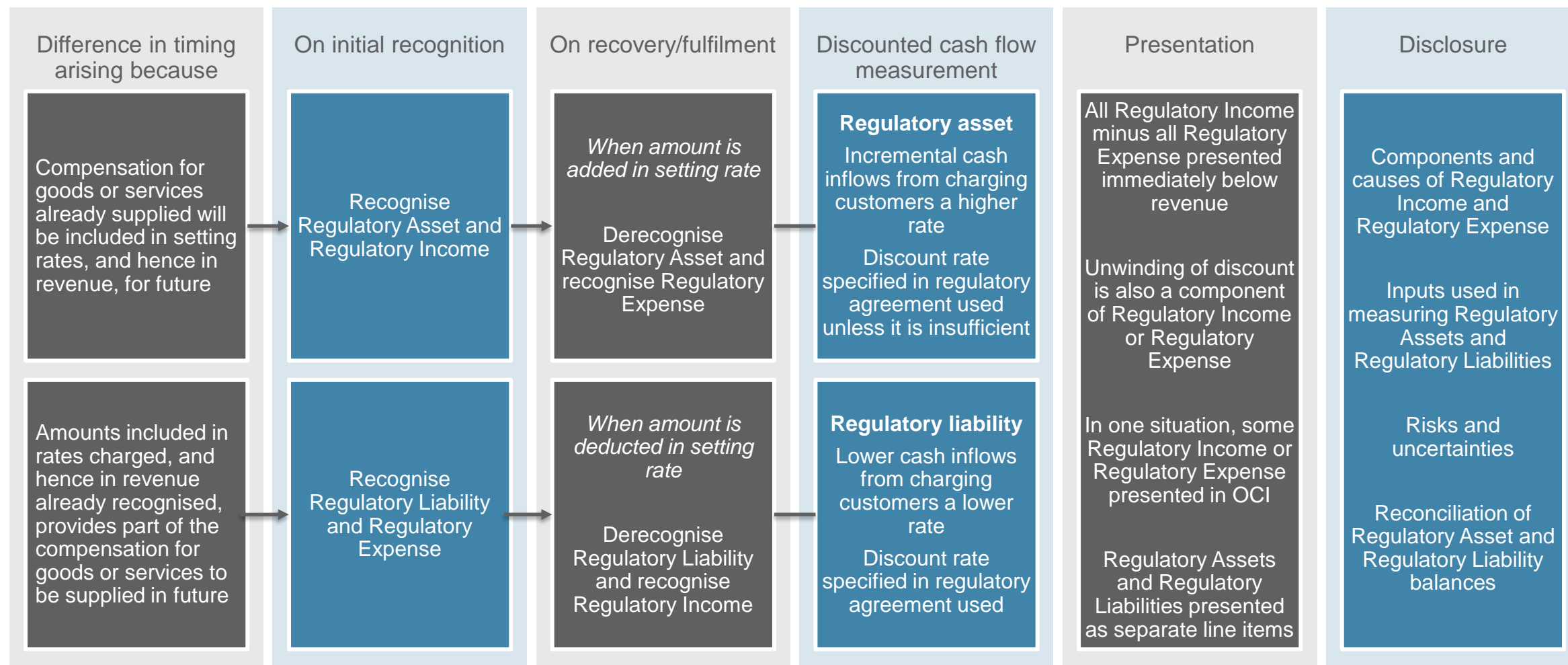
For more information, please refer to the following materials on www.ifrs.org:

- [Webinar](#): Explaining the Exposure Draft Regulatory Assets and Regulatory Liabilities
- [Exposure Draft *Regulatory Assets and Regulatory Liabilities*](#)
- [Illustrative Examples](#) on *Regulatory Assets and Regulatory Liabilities*
- [Basis for Conclusions](#) on Exposure Draft *Regulatory Assets and Regulatory Liabilities*
- [Snapshot](#): *Regulatory Assets and Regulatory Liabilities*

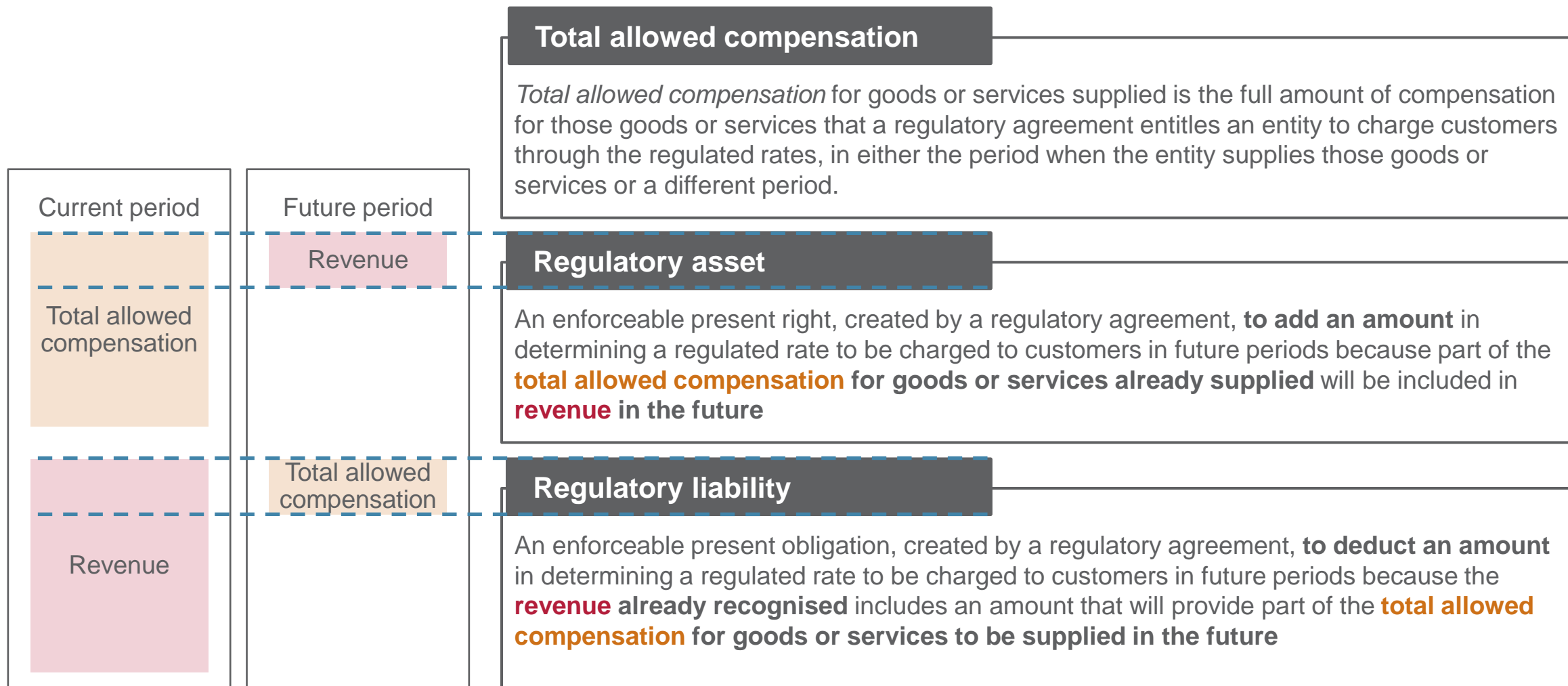
A grayscale world map is the background for the top half of the slide. Overlaid on the map are several thick, light gray curved lines that sweep across the continents. A network of thin, dotted lines is also visible, connecting various points across the map, suggesting a global network or data flow.

Appendix

Summary of the model



Definitions of key terms



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