IFRS Foundation

World Standard-setters Conference
2024

Learn about prospective IFRS Accounting Standard *Regulatory Assets and Regulatory Liabilities*

#WSS2024

Agenda

1. Introduction
2. Main requirements of IFRS X *Regulatory Assets and Regulatory Liabilities*
3. Next steps

Introduction

The problem—Lack of information about differences in timing

A regulatory agreement establishes

HOW MUCH an entity can charge for supplying goods or services to customers

WHEN the entity can charge that compensation to customers through regulated rates

In the period of supply

Compensation in rates

Supply goods or services

No difference in timing

In a **different period** from the period of supply

Past period

Current period

Future period

Difference in timing arises—Incomplete information about financial performance and financial position

Differences in timing—an illustration

- Entity A charges a regulated rate for goods supplied in Year 1 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.

- The regulatory agreement gives Entity A the right to add the costs under-recovered of CU20 in Year 1 to the regulated rate in Year 2.

Statement of profit or loss	Year 1 CU	Year 2 CU
Revenue from contracts with customers	100	120
Input costs	(120)	(100)
Profit (loss)	**(20)**	**20**

Without information about the difference in timing of CU20, investors would not understand:

- revenue in Year 1 excludes compensation of CU20 that relates to goods supplied in that year; and
- revenue in Year 2 includes compensation of CU20 that relates to goods supplied in Year 1.

Reflecting differences in timing

Statement of profit or loss	Year 1 CU	Year 2 CU
Revenue from contracts with customers	100	120
Regulatory income (regulatory expense)	**20**	**(20)**
Input costs	(120)	(100)
Profit (loss)	**-**	**-**

- **Regulatory income of CU20 in Year 1** to reflect compensation for goods supplied in Year 1.
- **Regulatory expense of CU20 in Year 2** to reflect amounts in revenue in Year 2 that relate to compensation for goods supplied in Year 1.

Balance sheet	Year 1 CU	Year 2 CU
Regulatory asset	**20**	**-**

- **Regulatory asset of CU20 in Year 1** to reflect the entity's right to increase regulated rates in Year 2.
- **Regulatory asset derecognised in Year 2**.

Information about regulatory income or regulatory expense helps investors to understand Entity A's financial performance—and compensation for goods supplied—in Years 1 and 2.

How does the prospective Standard solve the problem?

Problem	Without information about differences in timing, investors have an insufficient basis for understanding the effects of those differences on an entity's financial performance and financial position—and hence, the entity's prospects for future cash flows.
Objective	Provide information about the effects of regulatory income, regulatory expense, regulatory assets and regulatory liabilities on an entity's financial performance and financial position.
Principle	Reflect compensation for goods or services supplied in a period in an entity's financial performance for that period.

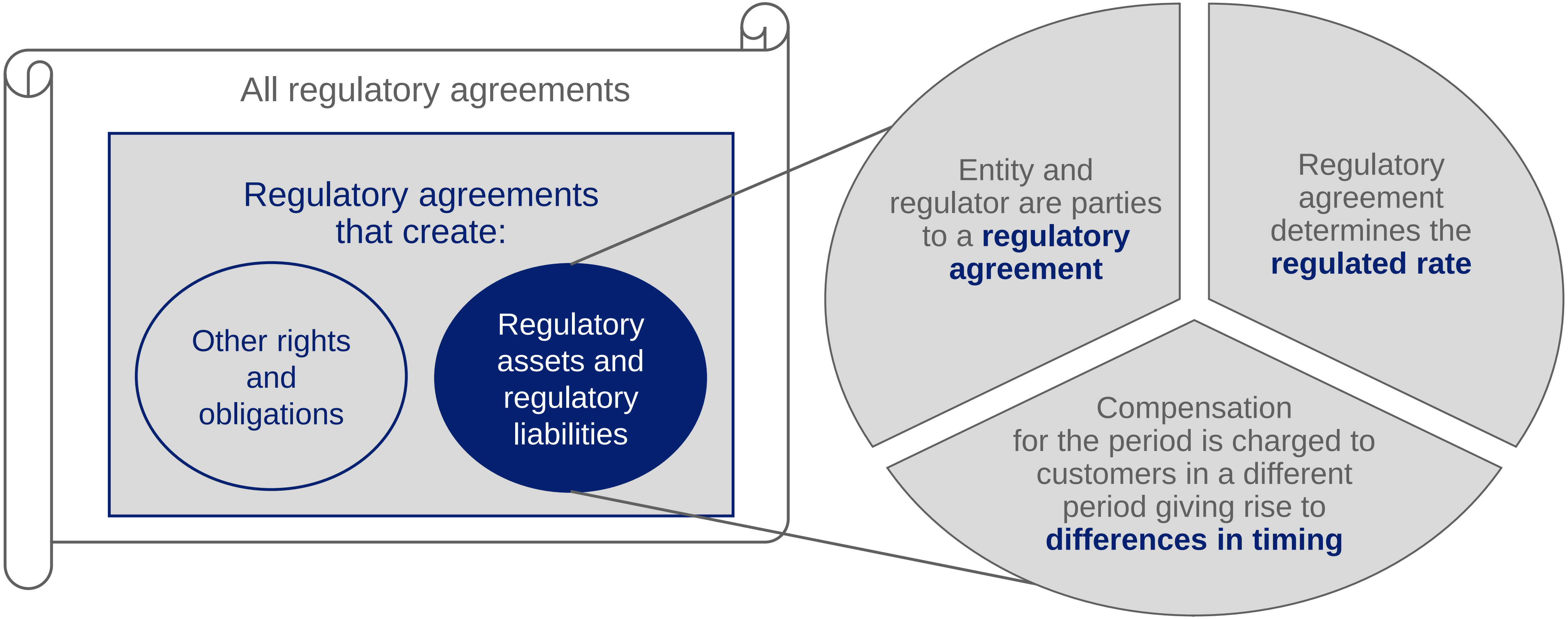
Supplement information provided by applying IFRS Accounting Standards—including IFRS 15 *Revenue from Contracts with Customers*

Main requirements

Topics

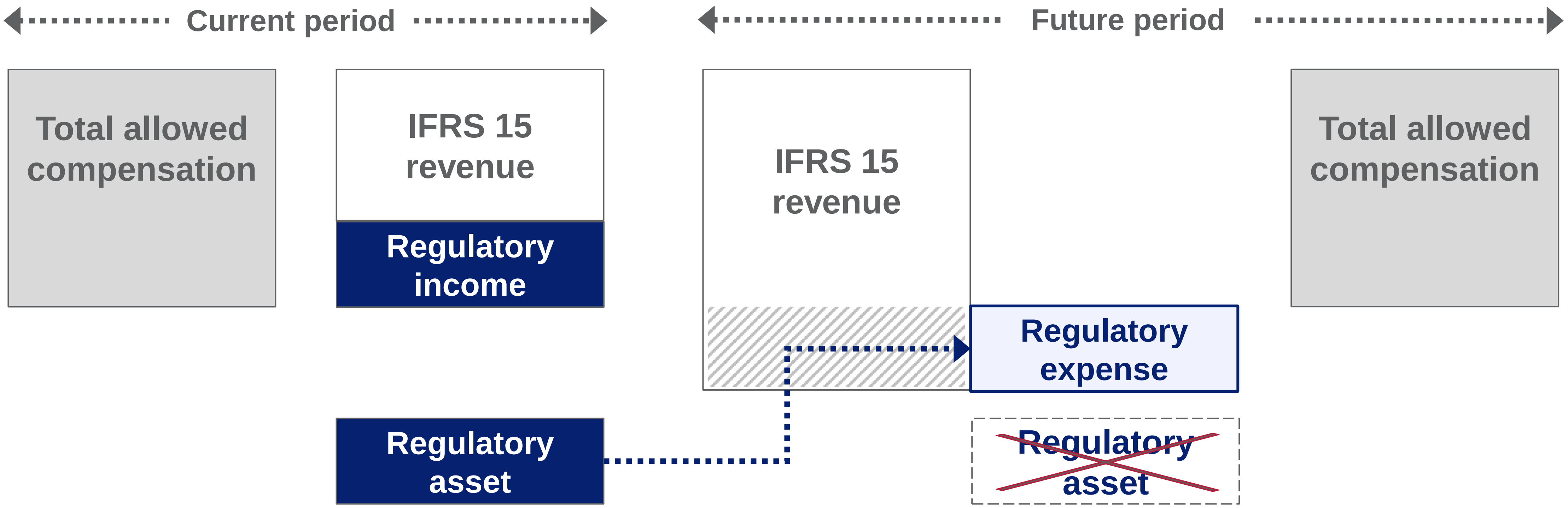
Scope

An entity applies IFRS X to all its **regulatory assets** and **regulatory liabilities**



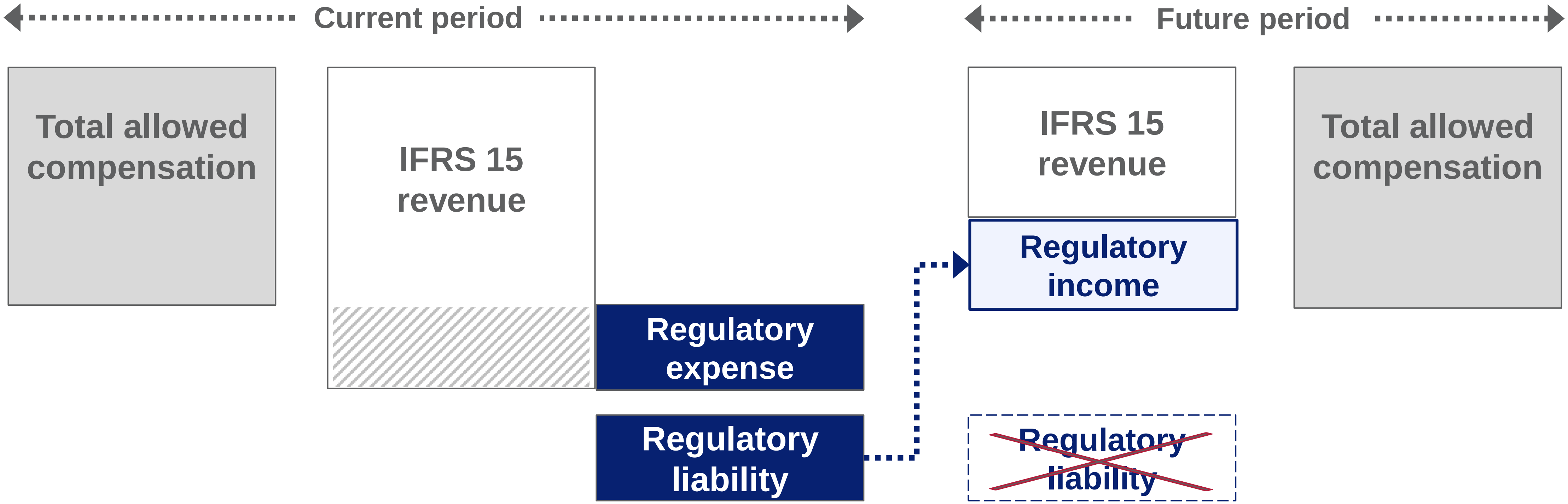
Regulatory asset

An **enforceable present right**, created by a regulatory agreement, to **add an amount** in determining a regulated rate to be charged to customers in future periods because all or part of the **total allowed compensation** for goods or services already supplied will be included in **IFRS 15 revenue** in the **future**



Regulatory liability

An **enforceable present obligation**, created by a regulatory agreement, to **deduct an amount** in determining a regulated rate to be charged to customers in future periods because the **IFRS 15 revenue** already recognised includes an amount that will provide all or part of the **total allowed compensation** for goods or services to be supplied in the **future**



Main components of the regulated rate

Regulated rate

Components unrelated to RCB(*)			Components related to RCB		
Allowable expenses	Volume variances	Performance incentives	Regulatory depreciation	Returns on RCB	Other items
				▪ Returns on assets in use ▪ Returns on assets not yet in use	▪ Allowable expenses ▪ Performance incentives ▪ Inflation (real approach)

(*): Regulatory capital base—a base that includes an entity's investment in operating assets. The regulator uses the RCB to determine compensation for the recovery of the investment (regulatory depreciation) and a return on the investment (regulatory returns).

Components of the regulated rate unrelated to RCB

Examples of differences in timing		
Allowable expenses	**Volume variances**	**Performance incentives**
• Differences between estimated and actual allowable expenses are included in future regulated rates. • Allowable expenses are recovered with a time lag (T+2). • Allowable expenses are recovered only when related cash is paid.	• Differences between allowed revenue and actual revenue due to volume variances are included in future regulated rates.	• Bonuses for current period performance are included in future regulated rates.

Components of the regulated rate related to RCB (1/3)

Examples of differences in timing

Regulatory depreciation

Returns on RCB

- Returns on assets in use
- Returns on assets not yet in use

Other items

- Allowable expenses
- Performance incentives
- Inflation (real approach)

[Grey box] Accounting depends on the **relationship** between **RCB** and **PPE**(*)

[White box] No difference in timing arises from returns on assets in use. Entities are prohibited from recognising inflation adjustment to the RCB as a regulatory asset.

(*): Property, plant and equipment

Components of the regulated rate related to RCB (2/3)

Direct relationship between RCB and PPE	No direct relationship between RCB and PPE
RCB is a tool to recover the costs of PPE.	RCB is a tool to determine allowed revenue.
▪ RCB is fundamentally the same as PPE. ▪ Recovery period of RCB is aligned with assets' useful lives. ▪ Differences between RCB and PPE can be tracked.	▪ Fundamental differences between RCB and PPE. ▪ RCB recovery period based on factors unrelated to assets' useful lives—for example, the entity's financial needs. ▪ Tracking differences between RCB and PPE can be costly and highly judgemental—or impracticable.

Components of the regulated rate related to RCB (3/3)

	Regulatory depreciation of RCB	Other items	Regulatory returns on assets not yet in use
Direct relationship	• Regulatory recovery period is longer or shorter than assets' useful lives.	• Allowable expenses and performance incentives added to RCB are included in future regulated rates.	• Regulatory returns are included in regulated rates charged during: ✓ construction—giving rise to a regulatory liability equal to the capitalised borrowing costs. ✓ operation—giving rise to a regulatory asset for the excess of the regulatory returns over the capitalised borrowing costs.
No direct	• Entities are prohibited from recognising regulatory assets or regulatory liabilities arising from these differences in timing.		• No difference in timing arises if an entity has the right to regulatory returns during construction.

Recognition

An entity recognises:

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

Recognition threshold—existence uncertainty

- An entity recognises a regulatory asset or regulatory liability if it is **more likely than not** that it exists—that is, the enforceable present right or enforceable present obligation exists.

An entity considers all relevant facts and circumstances—for example:

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

Measurement—cash-flow-based technique

	Future cash flows	Discount rate
Initial measurement	**Include all future cash flows (including regulatory interest)** • estimated using ‘most likely amount’ method or ‘expected value’ method, whichever better predicts uncertain future cash flows	**Discount estimated future cash flows** • using the regulatory interest rate • unless regulatory interest rate for a regulatory asset is insufficient (see slide 20)
Subsequent measurement	**Update estimates of future cash flows** • to reflect conditions existing at the end of reporting period **Reassess the method of estimating uncertain cash flows** • only if there is significant change in facts and circumstances	**Continue to use discount rate determined at initial recognition** • unless regulatory agreement changes the regulatory interest rate

Minimum interest rate—regulatory assets only

- Assess for any **indication** that the regulatory interest rate may be **insufficient** to compensate for **time value of money** and for **uncertainty** in future cash flows.

Not required to carry out an exhaustive search for indications.

- If there is such an **indication**:
  - **calculate** the minimum interest rate.
  - use, as the **discount rate**, the minimum interest rate if it is **higher** than the **regulatory interest rate**.

The minimum interest rate:

- reflects the key features of future cash flows—the currency, maturity profile and uncertainty.
- does not reflect risks for which future cash flows have been adjusted.

Measurement exemptions

An entity is **exempted** from **discounting** a regulatory asset (regulatory liability) in limited situations—for example:

- if the period between its recognition and its recovery (fulfilment) is expected to be 12 months or less; or
- for the period between recognition and the date from which regulatory interest starts to accrue, if that period is expected to be 12 months or less.

Minimum interest rate requirements	
Not applicable—a regulatory asset to which an exemption from discounting is applied.	**Specific exemption**—a regulatory asset that arises from cost or volume variances, **until** the regulator determines the **final balance**.

An entity applying any of these exemptions shall disclose that fact and the carrying amount of regulatory assets (regulatory liabilities) to which the entity has applied the exemption.

Presentation

Statement of financial position	Statement (s) of financial performance	
	Profit or loss	**OCI**
• **regulatory assets** • **regulatory liabilities**	• **regulatory income** or **regulatory expense** • classified as **revenue**	• **regulatory income** or **regulatory expense** resulting from **remeasurement** of a related liability or asset **through OCI**

Presentation—an illustration

Statement of profit or loss	Year 1 CU	Year 2 CU
Revenue from contracts with customers	120	100
Regulatory income(*)	70	100
Revenue	**190**	**200**
Input costs	(120)	(100)
Pension service costs	(60)	(85)
Operating profit	**10**	**15**
Interest expenses on pension liabilities	(10)	(15)
Profit	**-**	**-**

Statement presenting comprehensive income	Year 1 CU	Year 2 CU
Profit	**-**	**-**
Income and expenses that will not be reclassified to profit or loss:		
Regulatory income (regulatory expense)(*)	(40)	25
Gains (losses) on remeasurements of pension plans	40	(25)
Other comprehensive income	**-**	**-**
Total comprehensive income	**-**	**-**

(*) Associated with pension-related expenses (income) that will be added to (deducted from) future regulated rates.

Disclosure

Overall disclosure objective	Disclose information about regulatory income, regulatory expense, regulatory assets and regulatory liabilities that would enable users of financial statements to understand an entity's future cash flow prospects		
Specific disclosure objectives	Disclose information that enable users to understand:		
	• how regulatory income and regulatory expense affected the entity's financial performance	• regulatory assets and regulatory liabilities at the end of the reporting period and their changes during the period	• whether the entity's RCB has a direct relationship with its PPE
Disclosure requirements (examples)	• components of regulatory income or regulatory expense in profit or loss and OCI	• reconciliation of regulatory assets and regulatory liabilities • maturity analysis • how risks and uncertainties affect recovery and fulfilment	• whether the relationship between RCB and PPE is direct or no direct • the reasons for the entity's conclusion on the relationship between RCB and PPE

Aggregate and disaggregate disclosures in accordance with the principles in IFRS 18 *Presentation and Disclosure in Financial Statements*

Transition and effective date

Retrospective	Modified retrospective
Require an entity to restate comparative information for the comparative period only.(*)	

Modified retrospective—reliefs

Permit an entity:

- to use hindsight.
- to use the regulatory interest rate at the beginning of the comparative period as the regulatory interest rate.
- whose RCB and PPE have a direct relationship—to limit the application of the requirements for regulatory returns on assets not yet available for use to assets not yet available for use at the beginning of the comparative period.

Effective date	Annual periods beginning on or after **1 January 2029**. Earlier application is permitted.

(*) The comparative period is the period immediately preceding the period in which IFRS X is first applied.

Next steps

Next steps

Outreach

- **Feb 2022 to Jul 2024** — Redeliberations
- **Q3 2024 to H2 2025** — Drafting
  - Meetings with IFRS Foundation bodies and consultative groups
  - Additional fieldwork on the likely effects of IFRS X
- **H2 2025** — **IFRS X** *Regulatory Assets and Regulatory Liabilities*

  Replaces IFRS 14

Effective date

- **1 Jan 2029** — **IFRS X** *Regulatory Assets and Regulatory Liabilities*

Questions?

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