UKEB UK Endorsement Board

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30 July 2021

Dear Dr Barckow

Invitation to Comment: Exposure Draft ED/2021/1 *Regulatory Assets and Regulatory Liabilities*

The UK Endorsement Board (UKEB) is responsible for endorsement and adoption of International Financial Reporting Standards (IFRS) for use in the UK and therefore is the UK's National Standard Setter for IFRS. The UKEB also leads the UK's engagement with the IFRS Foundation on the development of new standards, amendments and interpretations. This letter forms part of those influencing activities and is intended to contribute to the International Accounting Standards Board's (IASB) due process. The views expressed by the UKEB in this letter are separate from, and will not necessarily affect the conclusions in, any endorsement and adoption assessment on new or amended International Accounting Standards undertaken by the UKEB.

We welcome the opportunity to respond to Exposure Draft ED/2021/1 *Regulatory Assets and Regulatory Liabilities*.

We support the proposals in the Exposure Draft as their implementation will lead to an improvement to financial reporting by entities within scope. We consider that information that explains the effect a regulatory agreement has on the timing of revenue, profit and cash flows of companies that undertake rate regulated activities will assist investors' decision making as well as their assessment of management's stewardship of such companies.

Our main recommendations to enhance the proposals in the Exposure Draft are outlined below. For detailed responses to the questions in the Exposure Draft please see Appendix 1.

1. The proposed standard should be explicit that the agreements intended to be included in the scope of the definition "regulatory agreement" are a small subset of regulatory agreements. We also recommend that the title of the definition is amended, e.g. by using the term "specified regulatory agreement" to clarify the scope (see our detailed response at paragraphs A3–A8 in Appendix 1).

2. The proposed standard should explicitly exclude service concession arrangements from its scope unless there is clear evidence that users would gain additional information from the application of both IFRIC 12 and the proposed standard to such arrangements. We have not been able to identify any such evidence in our outreach (see detailed response at paragraphs A8–A12 in Appendix 1).

3. The proposed standard should require an entity's regulator to be an independent third-party. This can be achieved by defining what is meant by a regulator in the context of the standard (see detailed response at paragraphs A13–A16 in Appendix 1).

4. The proposed requirement to exclude regulatory returns relating to assets not yet available for use in Total Allowable Compensation (TAC) does not reflect the economic substance of that return. We have heard from preparers in the UK that their regulators take a very high-level approach that does not require the granularity of information implied by the proposed requirements. Instead, UK regulators focus on an overview of an entity's operations and future requirements for goods or services, and thus the investment required to produce that level of goods or services. We therefore recommend that regulatory returns relating to assets not yet available for use in TAC should follow the economic substance of the requirements in the regulatory agreements (see detailed response at paragraphs A26–A31 in Appendix 1).

If you have any questions about this response, please contact the project team at UKEndorsementBoard@endorsement-board.uk

Yours sincerely

Pauline Wallace
Chair
UK Endorsement Board

Appendix 1 Questions on ED/2021/1 *Regulatory Assets and Regulatory Liabilities*

UKEB UK Endorsement Board

Appendix 1: Questions on ED/2021/1 *Regulatory Assets and Regulatory Liabilities*

Question 1: Objective and scope
Paragraph 1 of the Exposure Draft sets out the proposed objective: an entity should provide relevant information that faithfully represents how regulatory income and regulatory expense affect the entity's financial performance, and how regulatory assets and regulatory liabilities affect its financial position. Paragraph 3 of the Exposure Draft proposes that an entity apply the [draft] Standard to all its regulatory assets and all its regulatory liabilities. Regulatory assets and regulatory liabilities are created by a regulatory agreement that determines the regulated rate in such a way that part of the total allowed compensation for goods or services supplied in one period is charged to customers through the regulated rates for goods or services supplied in a different period (past or future).[1] The [draft] Standard would not apply to any other rights or obligations created by the regulatory agreement—an entity would continue to apply other IFRS Standards in accounting for the effects of those other rights or obligations. Paragraphs BC78–BC86 of the Basis for Conclusions describe the reasoning behind the Board's proposals. They also explain why the Exposure Draft does not restrict the scope of the proposed requirements to apply only to regulatory agreements with a particular legal form or only to those enforced by a regulator with particular attributes. a) Do you agree with the objective of the Exposure Draft? Why or why not? b) Do you agree with the proposed scope of the Exposure Draft? Why or why not? If not, what scope do you suggest and why? c) Do you agree that the proposals in the Exposure Draft are clear enough to enable an entity to determine whether a regulatory agreement gives rise to regulatory assets and regulatory liabilities? If not, what additional requirements do you recommend and why? d) Do you agree that the requirements proposed in the Exposure Draft should apply to all regulatory agreements and not only to those that have a particular legal form or those enforced by a regulator with particular attributes? Why or why not? If not, how and why should the Board specify what form a regulatory agreement should have, and how and why should it define a regulator? e) Have you identified any situations in which the proposed requirements would affect activities that you do not view as subject to rate regulation? If so, please describe the situations, state whether you have any concerns about those effects and explain what your concerns are. f) Do you agree that an entity should not recognise any assets or liabilities created by a regulatory agreement other than regulatory assets and regulatory liabilities and other assets and liabilities, if any, that are already required or permitted to be recognised by IFRS Standards? [1] A regulatory agreement is defined in the Exposure Draft as a set of enforceable rights and obligations that determine a regulated rate to be applied in contracts with customers.

Question 1(a) Do you agree with the objective of the Exposure Draft? Why or why not?

A1 We agree with the objective of the Exposure Draft. We understand that this is a significant issue for entities with rate-regulated activities, many of whom consider that it is not possible at present to reflect the underlying economic reality of those activities in financial statements prepared in accordance with IFRS. We consider that the proposals in this Exposure Draft will enable these entities to provide relevant information to investors and other users helping them to understand the effect that a "regulatory agreement" (within the scope of the proposed requirements) has on their financial statements.

Question 1(b) Do you agree with the proposed scope of the Exposure Draft? Why or why not? If not, what scope do you suggest and why?

A2 We are supportive of the scope of the Exposure Draft, however, we have identified the following potential issues:

a) It is not immediately clear that many types of regulatory agreement are out of the scope.

b) The explicit inclusion of service concession arrangements in the proposed standard.

Types of "regulatory agreement"

A3 The scope in the Exposure Draft relies on the definition of "regulatory agreement", "regulatory asset" and "regulatory liability". The title of the definition of regulatory agreement is especially problematic in the UK because it is generally interpreted as relating to a wide range of agreements, most of which are not in the scope of the Exposure Draft. For stakeholders not familiar with the project, it can create an initial perception that a great many of these agreements will fall within the scope of the Exposure Draft; only when they have worked through the details in the Exposure Draft and tested them against the regulatory agreements they hold, will it become clear that the scope is limited to only a very small subset of all agreements that in common usage are referred to as "regulatory agreements".

A4 For example, there are over 90 regulators in the UK[1]. However, there are only "…five regulators … that are independent economic regulators, which promote competitive forces in industries which would otherwise be natural monopolies due to high network or infrastructure costs"[2].

A5 We recommend that the title of the definition of "regulatory agreement" should be amended to make it clear that it only applies to a very small subset of all regulatory agreements, e.g. by using the term "specified regulatory agreement".

A6 It would also be helpful to set out the types of regulatory agreements that are out of the scope, e.g. by including an example of simple price cap regulation. In the UK, price cap regulation limits the prices that can be charged on a volumetric basis. Entities regulated on a price cap basis might therefore be exposed to demand risk as prices are based on forecast volumes and shortfalls are not necessarily adjusted, or 'trued up', in following periods.

A7 We note that the IASB's Snapshot: *Regulatory Assets and Regulatory Liabilities* (page 5), indicated that not all regulatory agreements will fall within the scope of the ED. We think this should also be specified in the proposed standard so that it is immediately clear that a large number of regulatory agreements are outside the scope of the proposed standard. This will remove the need for preparers with regulatory

1 National Audit Office: "A Short Guide to Regulation", September 2017, page 4: https://www.nao.org.uk/wp-content/uploads/2017/09/A-Short-Guide-to-Regulation.pdf

2 National Audit Office: "A Short Guide to Regulation", September 2017, page 5:

agreements to perform a detailed analysis of the proposed standard before they can conclude whether they are outside its scope.

A8 Adding examples of types of regulation that are excluded from the scope of the Exposure Draft would also minimise the risk that the requirements would be inappropriately applied by analogy to other types of regulatory agreements (which is the general way accounting standards are applied). These examples would be supplementary to those in Illustrative Example 7C. We propose that they should include examples related to market-based regulatory agreements, transfer pricing agreements and where the regulator is a related party of the entity.

Service concession arrangements

A9 IFRIC 12 *Service Concession Arrangements* sets out two models of service concession arrangements: the financial asset model and the intangible asset model. We have not found evidence that users would gain additional information by applying both IFRIC 12 and the proposed standard under either model. We therefore recommend that service concession arrangements should be excluded from the scope of this standard. If they remain within scope, the proposed standard should clarify why it is necessary and what the regulatory asset and/or regulatory liability would represent over and above the amounts already recognised under IFRIC 12.

A10 Our outreach has not identified any examples in the UK where a service concession arrangement would also meet the scope of the proposed standard.

Question 1(c) Do you agree that the proposals in the Exposure Draft are clear enough to enable an entity to determine whether a regulatory agreement gives rise to regulatory assets and regulatory liabilities? If not, what additional requirements do you recommend and why?

A11 We disagree with the reasoning in paragraph BC86 that it is unnecessary to define a regulator for the purposes of the proposed standard. We consider that relying solely on the definitions of "regulatory agreement", "regulated rate", "regulatory asset", and "regulatory liability" is not sufficient.

A12 It needs to be explicit that the regulator is a third party that is independent from the entity applying the proposed requirements.

A13 Requiring the regulator to be an independent third party delivers the following advantages:

a) It mitigates against unintended consequences where situations that have not been brought to the IASB's attention are inappropriately included in the scope of the proposed requirements.

b) It ensures that self-regulated entities, such as co-operatives, are not included in the scope of the proposals.

c) It would make it clear that a transfer pricing agreement between a parent and one of its subsidiaries or a situation where an entity establishes a regulator who has

legally enforceable powers either within or outside of its group structure, is not within scope.

A14 See also our response to Question 1(b).

Question 1(d) Do you agree that the requirements proposed in the Exposure Draft should apply to all regulatory agreements and not only to those that have a particular legal form or those enforced by a regulator with particular attributes? Why or why not? If not, how and why should the Board specify what form a regulatory agreement should have, and how and why should it define a regulator?

A15 Subject to our responses to Questions 1(a)–(c), we are content that the proposed requirements should apply to all regulatory agreements within scope.

Question 1(e) Have you identified any situations in which the proposed requirements would affect activities that you do not view as subject to rate regulation? If so, please describe the situations, state whether you have any concerns about those effects and explain what your concerns are.

A16 We have undertaken outreach to endeavour to identify situations where we would consider it inappropriate to apply the proposed requirements to those activities. To date we have not identified any specific cases.

Question 1(f) Do you agree that an entity should not recognise any assets or liabilities created by a regulatory agreement other than regulatory assets and regulatory liabilities and other assets and liabilities, if any, that are already required or permitted to be recognised by IFRS Standards?

A17 We agree that applying the proposed requirements to regulatory assets and regulatory liabilities only is appropriate as this is consistent with the approach of applying a supplementary model to pre-existing IFRS requirements.

Question 2: Regulatory assets and regulatory liabilities
The Exposure Draft defines a regulatory asset as 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 part of the total allowed compensation for goods or services already supplied will be included in revenue in the future. The Exposure Draft defines a regulatory liability as 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 revenue already recognised includes an amount that will provide part of the total allowed compensation for goods or services to be supplied in the future. Paragraphs BC36–BC62 of the Basis for Conclusions discuss what regulatory assets and regulatory liabilities are and why the Board proposes that an entity account for them separately. a) Do you agree with the proposed definitions? Why or why not? If not, what changes do you suggest and why?

b)	The proposed definitions refer to total allowed compensation for goods or services. Total allowed compensation would include the recovery of allowable expenses and a profit component (paragraphs BC87–BC113 of the Basis for Conclusions). This concept differs from the concepts underlying some current accounting approaches for the effects of rate regulation, which focus on cost deferral and may not involve a profit component (paragraphs BC224 and BC233–BC244 of the Basis for Conclusions). Do you agree with the focus on total allowed compensation, including both the recovery of allowable expenses and a profit component? Why or why not?
c)	Do you agree that regulatory assets and regulatory liabilities meet the definitions of assets and liabilities within the Conceptual Framework for Financial Reporting (paragraphs BC37–BC47)? Why or why not?
d)	Do you agree that an entity should account for regulatory assets and regulatory liabilities separately from the rest of the regulatory agreement (paragraphs BC58–BC62)? Why or why not?
e)	Have you identified any situations in which the proposed definitions would result in regulatory assets or regulatory liabilities being recognised when their recognition would provide information that is not useful to users of financial statements?

Question 2(a), (c), (d) and (e) Regulatory Assets and Regulatory Liabilities

A18 We agree with the proposed definitions of regulatory assets and regulatory liabilities and consider that they are consistent with the *Conceptual Framework for Financial Reporting*, as set out in paragraphs BC37–BC47 of the Basis for Conclusions.

A19 We also agree that an entity should account for regulatory assets and regulatory liabilities separately from the rest of the regulatory agreement as this is a supplementary model, applied after an entity has applied other IFRS.

A20 Our outreach with stakeholders did not identify situations in which the proposed definitions would result in regulatory assets or regulatory liabilities being recognised when it would not be useful to users of financial statements.

Question 2(b) Total Allowed Compensation

A21 We agree with the focus on total allowed compensation (TAC) and how it is related to the supply of goods and services to customers, either to goods or services supplied in the same period, or to goods or services supplied in a different period. We also agree that the TAC should include a profit component although we have some comments on aspects of the TAC, set out in our response to Question 3.

Question 3: Total allowed compensation	
Paragraphs B3–B27 of the Exposure Draft set out how an entity would determine whether components of total allowed compensation included in determining the regulated rates charged to customers in a period, and hence included in the revenue recognised in the period, relate to goods or services supplied in the same period, or to goods or services supplied in a different period. Paragraphs BC87–BC113 of the Basis for Conclusions explain the reasoning behind the Board's proposals.	
a)	Do you agree with the proposed guidance on how an entity would determine total allowed compensation for goods or services supplied in a period if a regulatory agreement provides:
	(i) regulatory returns calculated by applying a return rate to a base, such as a regulatory capital base (paragraphs B13–B14 and BC92–BC95)?
	(ii) regulatory returns on a balance relating to assets not yet available for use (paragraphs B15 and BC96–BC100)?
	(iii) performance incentives (paragraphs B16–B20 and BC101–BC110)?

b)	Do you agree with how the proposed guidance in paragraphs B3–B27 would treat all components of total allowed compensation not listed in question 3(a)? Why or why not? If not, what approach do you recommend and why?
c)	Should the Board provide any further guidance on how to apply the concept of total allowed compensation? If so, what guidance is needed and why?

Question 3(a)(i) regulatory returns calculated by applying a return rate to a base; and (iii) performance incentives

A22 We agree with the proposed guidance relating to: (i) regulatory returns calculated by applying a return rate to a base; and (iii) performance incentives.

Question 3(a) Do you agree with the proposed guidance on how an entity would determine total allowed compensation for goods or services supplied in a period if a regulatory agreement provides:

(ii) regulatory returns on a balance relating to assets not yet available for use (paragraphs B15 and BC96–BC100)?

A23 We do not agree with the proposed guidance relating to regulatory returns on a balance relating to assets not available for use as the guidance does not reflect the economics substance of the requirements in the regulatory agreements. We recommend that regulatory returns relating to assets not yet available for use in TAC should follow the economic substance of the requirements in the regulatory agreement.

A24 In our outreach we heard that regulatory returns relating to assets not yet available for use should be included in Total Allowable Compensation (TAC)[3] as the return is not dependent on the assets becoming operational. Rather it is a component of regulatory returns calculated by applying a return rate to a total regulatory capital base. These preparers have stated that this component of the regulatory return is a part of the return on the capital invested even if the construction of the asset is not continued in the future.

A25 This situation is alluded to in paragraph B15 which states that it "…might be a separate base or part of a larger base…". However, that paragraph ignores that, in many instances, it is a component of the return on investment for the entity and that it is not foregone even if the asset is not completed. For example, where an entity decides not to build an asset, it does not have to return the amount allocated for a regulatory return on an asset not yet available for use where the intended outcome regarding the provision of services is achieved. A preparer likened this to the fact that the regulator is focused on outcomes from the total investment and does not allocate returns on an asset-by-asset basis.

A26 We have heard from preparers in the UK that their regulators take a very high-level approach which does not require the granularity of information inferred by the proposed

[3] Total allowed compensation (for goods and services) is defined as: "The full amount of compensation for goods or services supplied that a regulatory agreement entitles an entity to charge customers through the regulated rates, in either the period when the entity supplies those goods or services or a different period." Appendix A of the Exposure Draft.

requirements. Rather, the regulator focuses on the overview of an entity's operations and future requirements for goods or services, and thus the investment required to produce that level of goods or services.

A27 The proposals of the ED would require entities to create and maintain records of returns on an asset-by-asset basis that previously have not been necessary and are unlikely to be necessary in the future as the regulator is focused on a high-level overview. In the UK, we think these requirements could be costly and require extensive effort from entities as the information required to prepare such records would need to be created specifically for financial reporting purposes.

A28 Moreover, we consider that the reasoning in paragraph BC98 is not consistent with the model that is being proposed in that:

a) Goods and services will be provided in the future when the assets not yet available for use are available for use (or the equivalent assets are available for use) as the regulator is focusing on the provision of a specified level of future goods or services instead of whether a specific asset is built.

b) Where a regulatory agreement includes regulatory returns on assets not yet available for use, we consider that that is economically different from regulatory agreements that do not include this type of return. Consequently, we do not believe that there is an issue with comparability.

Question 3(b) Do you agree with how the proposed guidance in paragraphs B3–B27 would treat all components of total allowed compensation not listed in question 3(a)? Why or why not? If not, what approach do you recommend and why?

A29 We agree with the proposed guidance relating to components of total allowed compensation not listed in question 3(a).

Question 3(c) Should the Board provide any further guidance on how to apply the concept of total allowed compensation? If so, what guidance is needed and why?

A30 We have no comment with regards to any further guidance on applying the concept of total allowed compensation. However, we have concerns about the interaction between the various components of total allowed compensation. In our outreach we have heard that, in practice, there may be an overlap between these components, which the ED does not appear to address. To provide an example, allowable expenses could be forecast at the beginning of a price control period using an assumed level and be recovered as part of the rates charged during the period subject to a true-up at the end of the price control period to reflect the actual inflation. To the extent that true inflation differs from that which was assumed at the beginning of the price control period, the true-up could be recovered through the rates charged by being added or deducted from the regulatory base on which regulatory returns for future periods are calculated.

A31 We therefore recommend that the standard should address these interactions by providing guidance and or illustrative examples to reflect how these interactions should be treated by preparers.

Question 4: Recognition
Paragraphs 25–28 of the Exposure Draft propose that: • an entity recognise all its regulatory assets and regulatory liabilities; and • if it is uncertain whether a regulatory asset or regulatory liability exists, an entity should recognise that regulatory asset or regulatory liability if it is more likely than not that it exists. It could be certain that a regulatory asset or regulatory liability exists even if it is uncertain whether that asset or liability will ultimately generate any inflows or outflows of cash. Uncertainty of outcome would be addressed in measurement (Question 5). Paragraphs BC122–BC129 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you agree that an entity should recognise all its regulatory assets and regulatory liabilities? Why or why not? b) 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? Why or why not? If not, what recognition threshold do you suggest and why?

A32 We agree that an entity should recognise all its regulatory assets and regulatory liabilities and that a 'more likely than not' recognition threshold should apply when it is uncertain whether a regulatory asset or regulatory liability exists, as set out in paragraphs BC122–BC129 of the Basis for Conclusions.

Question 5: Measurement
Paragraph 29 of the Exposure Draft specifies the measurement basis. Paragraphs 29–45 of the Exposure Draft propose that an entity measure regulatory assets and regulatory liabilities at historical cost, modified by using updated estimates of future cash flows. An entity would implement that measurement basis by applying a cash-flow-based measurement technique. That technique would involve estimating future cash flows—including future cash flows arising from regulatory interest—and updating those estimates at the end of each reporting period to reflect conditions existing at that date. The future cash flows would be discounted (in most cases at the regulatory interest rate—see Question 6). Paragraphs BC130–BC158 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you agree with the proposed measurement basis? Why or why not? If not, what basis do you suggest and why? b) Do you agree with the proposed cash-flow-based measurement technique? Why or why not? If not, what technique do you suggest and why? If cash flows arising from a regulatory asset or regulatory liability are uncertain, the Exposure Draft proposes that an entity estimate those cash flows applying whichever of two methods—the 'most likely amount' method or 'expected value' method—better predicts the cash flows. The entity should apply the chosen method consistently from initial recognition to recovery or fulfilment. Paragraphs BC136–BC139 of the Basis for Conclusions describe the reasoning behind the Board's proposal. c) Do you agree with this proposal? Why or why not? If not, what approach do you suggest and why?

Boundary of a regulatory agreement

A33 We consider that it is unclear how to apply the proposed requirements relating to the boundary of the regulatory agreement with respect to the measurement requirements.

A34 For example, it is not clear how to deal with the very practical issue that approvals from a regulator may be given well after the end of the reporting period, e.g. more than one year after the end of the regulatory period. It may well be that entities could recognise a regulatory asset or liability based on previous interactions with the regulator, but this needs to be included in the guidance.

A35 Other issues relate to:

a) The interaction between a regulatory licence and a pricing period.

b) The interaction between paragraphs B28–B34 (boundary of a regulatory agreement) and paragraphs B35–B36 (compensation for cancellation of an agreement.

c) The length of life of an asset, e.g. the asset recovery period is longer than the period of the licence agreement.

Interaction between a regulatory licence and a pricing period

A36 The application of the proposed requirements relating to the boundary of the regulatory agreement is unclear where there exists a regulatory pricing period and the resulting determination by the regulator. For example, where an entity has a rolling 25-year licence to operate and a 5-year agreement with the regulator relating to pricing and returns, it is not clear how the standard should be applied when the true-up negotiation occurs after the end of the 5-year period and takes a year to negotiate. The proposed requirements should state that, if part of the true-up relates to a return that will take the entity 10 years to recover, that should be included in the regulatory asset.

Interaction between the boundary of a regulatory agreement and compensation for cancellation of an agreement

A37 Paragraph B30(b) sets out the criteria under which an entity's present right to increase the regulated rate at a future date is enforceable only if two conditions are met. One of those conditions is that "no party apart from the entity has a right to cancel the regulatory agreement before that date without arranging compensation for the entity to recover its regulatory asset". Paragraphs B35–B38 gives further explanation of how the compensation for cancellation of an agreement may affect the measurement of a regulatory asset or a regulatory liability.

A38 However, there is no explanation that the measurement of a regulatory asset or regulatory liability may not be affected if the regulatory agreement includes provisions for compensation for cancellation of a regulatory agreement. It needs to be explicit that there may be an interaction between whether or not, for example, the entity's present right to increase the regulated rate at a future date is enforceable and the provisions for cancellation of a regulatory agreement due to the length of time it will take to recover the regulatory asset when the recovery period is longer than the license period.

Asset recovery period is longer than the period of the licence agreement / pricing period under the regulatory agreement

A39 It seems clear from paragraph B28 that the boundary of the regulatory agreement (and consequently, its measurement) is the latest future date at which an entity has either "an enforceable present right to recover a regulatory asset by increasing the regulated rate to be charged to customers" or "an enforceable present obligation to fulfil a regulatory liability by decreasing the regulated rate to be charged to customers".

A40 This guidance does not address the situation whereby the recovery period for an asset is longer than the period of the license agreement or pricing period under the regulatory agreement, for example, where the asset recovery period is 40 years, but the regulatory license is a 25-year rolling period and the pricing period is five years.

A41 We would encourage the IASB to include Illustrative Examples that reflect these situations to ensure consistent application of the proposed requirements. These examples would be more likely to reflect situations in practice due to the long-lived nature of some of the assets.

Question 6: Discount rate
Paragraphs 46–49 of the Exposure Draft propose that an entity discount the estimated future cash flows used in measuring regulatory assets and regulatory liabilities. Except in specified circumstances, the discount rate would be the regulatory interest rate that the regulatory agreement provides. Paragraphs BC159–BC166 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you agree with these proposals? Why or why not? If not, what approach do you suggest and why? Paragraphs 50–53 of the Exposure Draft set out proposed requirements for an entity to estimate the minimum interest rate and to use this rate to discount the estimated future cash flows if the regulatory interest rate provided for a regulatory asset is insufficient to compensate the entity. The Board is proposing no similar requirement for regulatory liabilities. For a regulatory liability, an entity would use the regulatory interest rate as the discount rate in all circumstances. Paragraphs BC167–BC170 of the Basis for Conclusions describe the reasoning behind the Board's proposals. b) Do you agree with these proposed requirements for cases when the regulatory interest rate provided for a regulatory asset is insufficient? Why or why not? c) Have you identified any other situations in which it would be appropriate to use a discount rate that is not the regulatory interest rate? If so, please describe the situations, state what discount rate you recommend and explain why it would be a more appropriate discount rate than the regulatory interest rate. Paragraph 54 of the Exposure Draft addresses cases when a regulatory agreement provides regulatory interest unevenly by applying a series of different regulatory interest rates in successive periods. It proposes that an entity should translate those rates into a single discount rate for use throughout the life of the regulatory asset or regulatory liability. d) Do you agree with the proposal? Why or why not? If not, what do you recommend and why?

Question 6(a) Do you agree with these proposals? Why or why not? If not, what approach do you suggest and why?

A42 We generally agree with the proposals that an entity discount the estimated future cash flows used in measuring regulatory assets and regulatory liabilities, subject to our comments on the rest of the question.

Question 6(b) Do you agree with these proposed requirements for cases when the regulatory interest rate provided for a regulatory asset is insufficient? Why or why not?

A43 Our outreach with stakeholders did not identify any examples of situations where the regulatory interest rate for a regulatory asset is not sufficient to compensate the entity for the time value of money and uncertainty risks. An entity is required to make this assessment on initial recognition of a regulatory asset and when the regulatory interest rate changes.

A44 We would advise the IASB to simplify the requirements by making it a rebuttable presumption that the regulatory interest rate is sufficient, unless the indicators set out in paragraph 52 of the Exposure Draft are present. This would mean that entities are only required to make this assessment where there are indicators that the regulatory interest rate for a regulatory asset is insufficient. This would achieve the same outcome whilst reducing the burden on preparers.

Question 6(c) Have you identified any other situations in which it would be appropriate to use a discount rate that is not the regulatory interest rate? If so, please describe the situations, state what discount rate you recommend and explain why it would be a more appropriate discount rate than the regulatory interest rate.

A45 No, we have not identified any other situations in which it would be appropriate to use a discount rate that is not the regulatory interest rate.

Question 6(d) Do you agree with the proposal? Why or why not? If not, what do you recommend and why?

A46 We agree that an entity should translate a series of different regulatory interest rates in successive periods into a single discount rate for use throughout the life of the regulatory asset or regulatory liability.

Question 7: Items affecting regulated rates only when related cash is paid or received
In some cases, a regulatory agreement includes an item of expense or income in determining the regulated rates in the period only when an entity pays or receives the related cash, or soon after that, instead of when the entity recognises that item as expense or income in its financial statements. Paragraphs 59–66 of the Exposure Draft propose that in such cases, an entity would measure any resulting regulatory asset or regulatory liability using the measurement basis that the entity would use in measuring the related liability or related asset by applying IFRS Standards. An entity would adjust that measurement to reflect any uncertainty that is present in the regulatory asset or regulatory liability but not present in the related liability or related asset. Paragraphs BC174–BC177 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you agree with the measurement proposals when items of expense or income affect regulated rates only when related cash is paid or received? Why or why not? If not, what approach do you suggest for such items and why? When these measurement proposals apply and result in regulatory income or regulatory expense arising from remeasuring the related liability or related asset through other comprehensive income, paragraph 69 of the Exposure Draft proposes that an entity would also present the resulting regulatory income or regulatory expense in other

comprehensive income. Paragraphs BC183–BC186 of the Basis for Conclusions describe the reasoning behind the Board's proposal.

b) Do you agree with the proposal to present regulatory income or regulatory expense in other comprehensive income in this case? Why or why not? If not, what approach do you suggest and why?

A47 We agree with the measurement proposals when items of expense or income affect regulated rates only when related cash is paid or received.

A48 We also agree with the proposal to present regulatory income or regulatory expense in other comprehensive income when it arises from remeasuring the related liability or related asset through other comprehensive income.

Question 8: Presentation in the statement(s) of financial performance
Paragraph 67 of the Exposure Draft proposes that an entity present all regulatory income minus all regulatory expense as a separate line item immediately below revenue. Paragraph 68 proposes that regulatory income includes regulatory interest income and regulatory expense includes regulatory interest expense. ParagraphsBC178–BC182 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you agree that an entity should present all regulatory income minus all regulatory expense as a separate line item immediately below revenue (except in the case described in Question 7(b))? Why or why not? If not, what approach do you suggest and why? b) Do you agree with the proposed inclusion of regulatory interest income and regulatory interest expense within the line item immediately below revenue? Why or why not? If not, what approach do you suggest and why?

Question 8(a) Do you agree that an entity should present all regulatory income minus all regulatory expense as a separate line item immediately below revenue (except in the case described in Question 7(b))? Why or why not? If not, what approach do you suggest and why?

A49 We agree with the proposals in the ED for presenting separately, and immediately below revenue, the regulatory income minus the regulatory expense.

A50 The separate disclosure of non-regulatory revenue from revenue generated from regulated activities is an important distinction for users as it will allow for a clear assessment of an entity's overall performance.

A51 We believe the separate presentation is also consistent with the principles contained in IAS 1 *Presentation of Financial Statements* and the *Conceptual Framework for Financial Reporting* as it will provide information that is comparable, useful and faithfully represents the underlying economic phenomena regarding an entity's regulatory activities during the financial period while also allowing for estimations of future cash flows.

A52 We also agree with the IASB's assessment in paragraph BC179, that regulatory income and regulatory expense should not be presented as part of revenue and instead should be presented in a separate line item immediately below revenue (from IFRS 15 *Revenue from Contracts with Customers*).

Question 8(b) Do you agree with the proposed inclusion of regulatory interest income and regulatory interest expense within the line item immediately below revenue? Why or why not? If not, what approach do you suggest and why?

A53 We agree with the proposed inclusion of regulatory interest income and regulatory interest expense within the line item immediately below revenue. This will ensure the amounts relating to regulatory interest are included in determining the future regulated rates charged to customers and therefore included in revenue in future periods. Separately disclosing these items beneath revenue also allows for comparability between entities.

Question 9: Disclosure
Paragraph 72 of the Exposure Draft describes the proposed overall objective of the disclosure requirements. That objective focuses on information about an entity's regulatory income, regulatory expense, regulatory assets and regulatory liabilities, for reasons explained in paragraphs BC187–BC202 of the Basis for Conclusions. The Board does not propose a broader objective of providing users of financial statements with information about the nature of the regulatory agreement, the risks associated with it and its effects on the entity's financial performance, financial position or cash flows. a) Do you agree that the overall disclosure objective should focus on information about an entity's regulatory income, regulatory expense, regulatory assets and regulatory liabilities? Why or why not? If not, what focus do you suggest and why? b) Do you have any other comments on the proposed overall disclosure objective? Paragraphs 77–83 of the Exposure Draft set out the Board's proposals for specific disclosure objectives and disclosure requirements. c) Do you have any comments on these proposals? Should any other disclosures be required? If so, how would requiring those other disclosures help an entity better meet the proposed disclosure objectives? d) Are the proposed overall and specific disclosure objectives and disclosure requirements worded in a way that would make it possible for preparers, auditors, regulators and enforcement bodies to assess whether information disclosed is sufficient to meet those objectives?

Question 9(a) Do you agree that the overall disclosure objective should focus on information about an entity's regulatory income, regulatory expense, regulatory assets, and regulatory liabilities? Why or why not? If not, what focus do you suggest and why?

A54 We generally agree that the overall disclosure objective should focus on an entity's regulatory income, regulatory expenses, regulatory assets, and regulatory liabilities as this will provide users with the information they need to assess and understand an entity's regulated activities for the period for which financial statements have been prepared.

A55 However, we consider that information about an entity's regulatory agreement should also be included. This is because it will give an understanding of how the regulatory income, regulatory expenses, regulatory assets, and regulatory liabilities have arisen. This could include information about the length of the regulatory agreement, exit provisions and the legal form of the agreement. We think this information will be useful in helping users understand how the underlying economics of an entity's regulatory

agreements impact on the regulatory balances and amounts presented in the financial statements.

A56 We also acknowledge that an entity need not disclose sensitive information and therefore recommend that our proposals made above be considered within the context of information that may be considered sensitive.

A57 Additionally, we looked at the disclosure requirements in the ED against the proposals in *Disclosure Requirements in IFRS Standards—A Pilot Approach (Proposed amendments to IFRS 13 and IAS 19)* (Disclosure Pilot ED). We acknowledge that the Disclosure Pilot ED was published after this ED but consider it is worth looking at to see if the proposed disclosure requirements are sufficient.

A58 On looking at the Disclosure Pilot ED, we consider that the layout, with the headings relating to the overall disclosure objective and specific disclosure objectives, should be replicated in the proposed standard as this will help to distinguish between the different types of disclosure objectives and their respective purposes.

Question 9(b) Do you have any other comments on the proposed overall disclosure objective?

A59 See comments on our response to Question 9(a).

Question 9(c) Do you have any comments on these proposals? Should any other disclosures be required? If so, how would requiring those disclosures help an entity better meet the proposed disclosure objectives?

A60 We agree with the proposals in paragraphs 77–83 of the ED related to specified disclosures about regulatory income, regulatory expenses, regulatory assets, and regulatory liabilities, that these will lead to information provided by entities that are comparable and relevant to users in their decision making and understanding of future cash flows. We also think the proposals will achieve faithful representation as the revenue recognised will reflect the services rendered during the year. Additionally, the balances of regulatory assets or regulatory liabilities recognised on the statement of financial position at year end will enable users to understand an entity's rights and obligations and determine the impact of the future cash flows.

Question 9 (d): Are the proposed overall and specific disclosure objectives and disclosure requirements worded in a way that would make it possible for preparers, auditors, regulators, and enforcement bodies to assess whether information disclosed is sufficient to meet those objectives?

A61 We agree with the proposed wording for the overall and specific disclosures is simple, clear, and easy to understand. See also our response to Question 9(a) as it suggests additional clarity is possible by including further sub-headings.

Question 10: Effective date and transition
Appendix C to the Exposure Draft describes the proposed transition requirements. Paragraphs BC203–BC213 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you agree with these proposals? b) Do you have any comments you wish the Board to consider when it sets the effective date for the Standard?

A62 The Exposure Draft specifies that an entity shall apply the proposed requirements retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. The entity has an option not to apply the proposed requirements retrospectively to a past business combination and sets out a number of conditions if this option is used.

A63 We understand from stakeholders that this does not address a number of challenges associated with determining the opening balance for regulatory assets and regulatory liabilities. We encourage the IASB to engage with preparers to identify the detailed issues.

A64 The starting position for entities that are within the scope of the proposed requirements are different when they come to apply it for the first time. For example:

a) Some entities will never have recognised regulatory assets and regulatory liabilities.

b) Some other entities will be applying IFRS 14 *Regulatory Deferral Accounts*.

c) Other entities will be applying US GAAP, which has a standard for the recognition of these types of assets and liabilities.

A65 We believe that, dependent on an entity's starting position, the transition needs are likely to be different. For example, entities that have never recognised regulatory assets and regulatory liabilities may lack the records to apply the full retrospective approach. We do not consider it appropriate simply to rely on the requirements in IAS 8 relating to retrospective application and including the guidance on when it is impracticable to apply retrospective application. Incorporating specific transition requirements into the proposed standard, in acknowledgement of the fact that entities will be recognising new types of assets and liabilities, is consistent with other IFRS which include such specific transition requirements. This approach is also likely to result in a much more consistent application of the proposed requirements on transition which, in turn, will result in more understandable information for users of the financial statements.

A66 Appendix D includes proposed requirements for consequential amendments to other standards. This includes a proposed amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards*, which would permit a first-time adopter of IFRS to use carrying amounts determined under a previous GAAP to recognise regulatory assets and regulatory liabilities. It seems inconsistent that this relief is available to first-time adopters of IFRS but not to those entities that currently apply IFRS 14 or another GAAP, such as US GAAP, and that go on to apply the proposed standard in the Exposure Draft. We suggest the IASB rectify this inconsistency when finalising the standard by extending the IFRS 1 requirement to entities that currently apply IFRS 14 or another GAAP.

Question 11: Other IFRS Standards
Paragraphs B41–B47 of the Exposure Draft propose guidance on how the proposed requirements would interact with the requirements of other IFRS Standards. Appendix D to the Exposure Draft proposes amendments to other IFRS Standards. Paragraphs BC252–BC266 of the Basis for Conclusions describe the reasoning behind the Board's proposals. a) Do you have any comments on these proposals? Should the Board provide any further guidance on how the requirements proposed in the Exposure Draft would interact with any other IFRS Standards? If yes, what is needed and why? b) Do you have any comments on the proposed amendments to other IFRS Standards?

Question 11(a) Do you have any comments on these proposals? Should the Board provide any further guidance on how the requirements proposed in the Exposure Draft would interact with any other IFRS Standards? If yes, what is needed and why?

A67 We generally agree with the proposed requirements relating to the interaction with other IFRS, except for service concession arrangements (as set out in our response to Question 1).

A68 Notwithstanding our recommendation that service concession arrangements should not be included in the scope of the proposed standard, if they do remain in scope, we do not consider that the proposed requirements in paragraph B47 are detailed enough to help those preparers that have service concession arrangements that also come within the definition of regulatory agreements.

Question 12: Likely effects of the proposals
Paragraphs BC214–BC251 of the Basis for Conclusions set out the Board's analysis of the likely effects of implementing the Board's proposals. a) Paragraphs BC222–BC244 provide the Board's analysis of the likely effects of implementing the proposals on information reported in the financial statements and on the quality of financial reporting. Do you agree with this analysis? Why or why not? If not, with which aspects of the analysis do you disagree and why? b) Paragraphs BC245–BC250 provide the Board's analysis of the likely costs of implementing the proposals. Do you agree with this analysis? Why or why not? If not, with which aspects of the analysis do you disagree and why? c) Do you have any other comments on how the Board should assess whether the likely benefits of implementing the proposals outweigh the likely costs of implementing them or on any other factors the Board should consider in analysing the likely effects?

A69 Our outreach has identified some issues where preparers expect the proposals to cost more than those outlined in paragraphs BC247–BC249 of the Basis for Conclusions. These concerns relate to:

a. Not including regulatory returns on a balance relating to assets not yet available for use in the TAC; and

b. The lack of transition requirements.

A70 For regulatory returns on a balance relating to assets not yet available for use, the concern from preparers seems to be that where a regulator does not require the granularity of information implied by the proposed requirements, this information will need to be created and maintained. See our response in paragraphs A29–A33.

A71 Given the lack of transition requirements or guidance, preparers may find it difficult to establish an opening position leading to increased costs of implementation. We have suggested in our response to Question 10 that the proposed standard include guidance for different categories of entities, depending on whether the entity is already recognising regulatory balances or not.

Question 13: Other comments
Do you have any other comments on the proposals in the Exposure Draft or on the Illustrative Examples accompanying the Exposure Draft?

A72 Consistent with our response to Question 1 we consider that there should be specific examples illustrating other types of regulatory agreements that are outside the scope of the proposed standard.