

STAFF PAPER

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Purpose of this paper

1. The purpose of this paper is to seek advice from the Accounting Standards Advisory Forum (ASAF) members on identifying disclosure objectives and related disclosure requirements for defined rate regulation.
2. The disclosure objectives and requirements in this paper are the staff's work in progress and have not been discussed with the Board yet. We will consider the advice provided by the ASAF members when discussing this matter with the Board at a future meeting.

Structure of the Paper

3. The structure of the paper is as follows:
 - (a) staff's initial views on presentation requirements (paragraphs 5–6);
 - (b) work done on the Disclosure Initiative—Targeted Standards-level Review of Disclosures project (paragraphs 7–8);
 - (c) disclosure objectives (paragraphs 9–23);
 - (d) level of aggregation (paragraphs 24–32);
 - (e) disclosure requirements (paragraph 33–38); and

(f) illustrative disclosures and usefulness of the resulting information (paragraphs 39–49).

4. Agenda Paper 4C includes a case study that provides background information about how the regulatory items shown in the illustrative disclosures in paragraphs 39–49 arose. The illustrative examples are designed to ‘stand-alone’ so we believe that ASAF members will not need to read Agenda Paper 4C. The paper is provided for those who wish to see more detailed information about the mechanics of the model.

Staff’s initial views on presentation requirements

5. This section provides a brief overview of the staff’s initial views on the presentation requirements for the model so that ASAF members have a better context within which to provide us with advice on the disclosure objectives and disclosure requirements.

6. Regulatory assets and regulatory liabilities have a distinct nature that does not fit neatly into any of the defined categories of assets and liabilities accounted for using existing IFRS Standards. Consequently, the staff’s initial view is that the Board should require presentation of additional line items beyond those required by IAS 1 *Presentation of Financial Statements*. The staff will discuss the number, location and naming of line items with the Board at a later meeting. As a minimum, the staff are likely to recommend separate line items as follows:¹

(a) In the statement of financial position:

- (i) regulatory assets;
- (ii) regulatory liabilities;

¹ IFRS 14 *Regulatory Deferral Accounts* requires similar line items to those proposed for the model. However, those line items are isolated from the assets, liabilities, income and expenses presented using other IFRS Standards by use of sub-totals. IFRS 14 is a temporary Standard that permits particular first-time adopters of IFRS Standard to continue to apply, with some limitations, their previous GAAP accounting policies for the recognition and measurement of particular regulatory rights and obligations described as ‘regulatory deferral account balances’. When the Board issued IFRS 14, it had not decided whether regulatory deferral account balances met the definitions of asset and liability in the *Conceptual Framework for Financial Reporting*. While developing the model in this project, the Board has decided that the regulatory rights and regulatory obligations identified as being within the scope of the model do meet those definitions of asset and liability. Consequently, the staff’s initial view is not to propose the use of sub-totals to isolate regulatory assets, regulatory liabilities and related regulatory income or expense from other assets, liabilities, income or expense.

- (b) In the profit or loss section of the statement of profit or loss and other comprehensive income, regulatory income or regulatory expense recognised in profit or loss (possibly just as a single net amount).
- (c) In the other comprehensive income section of the statement of profit or loss and other comprehensive income, regulatory income or regulatory expense recognised in other comprehensive income (possibly with income netted against expenses). In addition, this item should be disaggregated and presented in separate lines to distinguish:
 - (i) items that will be reclassified subsequently to profit or loss when specified conditions are met; and
 - (ii) items that will not be reclassified subsequently to profit or loss.

Disclosure Initiative—Targeted Standards-level Review of Disclosures project

7. The Board considered the feedback received from its Discussion Paper *Disclosure Initiative—Principles of Disclosure* at its meeting in March 2018 and tentatively decided to perform a [targeted Standards-level review of disclosure](#) requirements. As part of this review, the Board tentatively decided, at its May 2018 meeting,² that when developing and drafting disclosure requirements in future, it will:
- (a) continue to use high-level or overall disclosure objectives within individual IFRS Standards.
 - (b) base all disclosure requirements on one or more specific disclosure objectives. The specific disclosure objectives should provide a more granular application of the overall disclosure objective. These objectives should explain why the information is useful to the primary users of financial statements, and what the Board expects primary users of financial statements will be able to do with the information.

² Agenda Paper 11B discussed at the May 2018 Board meeting can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/may/iasb/ap11b-di.pdf>

(c) draft all disclosure requirements so they explicitly state the underlying objective(s) and clearly link each item of information included in disclosure requirements with the related objective(s).

8. The purpose of the overall disclosure objective and supporting specific objectives is to prompt entities to use judgement to decide what information to disclose relating to a particular topic in their financial statements and whether the information provided meets user information needs for that topic.

Disclosure objectives

9. In July 2018, the Board discussed the following initial presentation and disclosure objective being developed for defined rate regulation:³

An entity shall present and disclose information that enables users of financial statements to assess and distinguish between:

- fluctuations in revenue and expenses compensated for through the rate-adjustment mechanism; and
- fluctuations in revenue and expenses for which there is no compensation.

This information will be useful because it will allow users to assess the amounts, timing and uncertainty of future cash flows arising from regulatory assets and regulatory liabilities.

10. The Board was not asked to make decisions but Board members were asked to provide their views on that objective. Some Board members expressed the following views:

- (a) the initial disclosure objective is too broad and may unintentionally result in a ‘long-wish list’ of requirements, which would not be helpful (see paragraphs 18–20);
- (b) the disclosure objective should convey a key feature of the model, which is that it is a ‘supplementary model’ (see paragraph 20–21); and

³ Agenda Paper 9C discussed at the July 2018 Board meeting can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/july/iasb/ap09c-rra.pdf>

- (c) the disclosure objective should focus more on understanding what future rate adjustments refer to activities carried out to date, the uncertainties associated with them, how they were measured and the expected timing of their reversal (see paragraphs 20–23).
11. The following paragraphs aim to address these concerns and provide the analysis that leads to our new proposed overall disclosure objective in paragraph 22. The analysis is structured as follows:
- (a) users' information needs (paragraphs 12–14);
- (b) the disclosure objective in IFRS 14 *Regulatory Deferral Accounts* (paragraphs 15–19); and
- (c) main focus of the overall disclosure objective (paragraphs 20–21).

User information needs

12. The operation of the rate-adjustment mechanism creates timing differences when an entity fulfils service requirements in a different period than the period in which those service requirements are charged to customers through the regulated rate. Currently, users of IFRS financial statements may get an incomplete picture of the effects of defined rate regulation on an entity's financial performance during the period and the entity's financial position at the end of the period. This is because the application of current IFRS requirements (excluding IFRS 14) reports some of the effects of some transactions or other events as income or expenses in a different period than the period in which other effects of the same transactions or events are reported. The model aims to address this shortcoming by recognising the origination and recovery of regulatory assets and the origination and fulfilment of regulatory liabilities.
13. Related to the above, users of financial statements have told us that they need information about how timing differences have arisen and about how and when those timing differences will reverse. This information helps users to distinguish fluctuations in revenue and expenses compensated for through the rate-adjustment mechanism from fluctuations for which there is no compensation. The information also helps them to predict the amounts, timing and uncertainty of future cash flows arising from regulatory assets and regulatory liabilities.

14. Users have also told us that information about the regulatory environment and relationship between the regulator and the entity would enhance their understanding of the amounts, timing and uncertainty of future cash flows (see Agenda Paper 9C, discussed at the July 2018 Board meeting and paragraph 19).

Disclosure objective in IFRS 14 Regulatory Deferral Accounts

15. IFRS 14 *Regulatory Deferral Accounts* has a disclosure objective and disclosure requirements based on common practice observed when the Standard was developed. Respondents to the Discussion Paper *Reporting the Financial Effects of Rate Regulation*⁴ and, more recently, members of the Board’s Capital Markets Advisory Committee suggested that the disclosure objective in IFRS 14 would be a good starting point for developing the disclosure requirements of the model.⁵

16. The disclosure objective of IFRS 14 is reproduced below:

27 An entity that elects to apply this Standard shall disclose information that enables users to assess:

- (a) the nature of, and the risks associated with, the rate regulation that establishes the price(s) that the entity can charge customers for the goods or services it provides; and
- (b) the effects of that rate regulation on its financial position, financial performance and cash flows.

17. We have considered this objective in the light of the work being done in the Board’s Better Communication projects, in particular its Targeted Standards-level Review of Disclosures project (see paragraph 7). We have also considered the Guidance on the objective of financial statements contained in paragraph 3.2 of the *Conceptual Framework for Financial Reporting*, which states:

⁴ The Discussion Paper can be found: <https://www.ifrs.org/-/media/project/rate-regulated-activities/published-documents/discussion-paper-reporting-financial-effects-rate-regulation-september-2014.pdf>

⁵ Agenda Paper 5 discussed at the March 2018 CMAC meeting can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/march/cmac/ap5-rate-regulated-activities-notes.pdf> and the summary meeting notes can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/march/cmac/cmac-meeting-summary-march-2018.pdf>

The objective of the financial statements is to provide financial information about the reporting entity's assets, liabilities, equity, income and expense that is useful to users of financial statements in assessing the prospects for future net cash inflows to the reporting entity and in assessing management's stewardship of the entity's economic resources [...].

18. We think the disclosure objective in IFRS 14 is too broad because it could require entities to disclose information about the general environment in which they operate, rather than focusing on the effects that transactions and other events within the scope of the model have on the entity's income, expenses, assets and liabilities. Having disclosure objectives that are too broad was identified in the Disclosure Initiative project as one of the ways stakeholders stated the drafting in IFRS Standards contributes to the 'disclosure problem', with clearer, more specific or granular disclosure objectives being more helpful.⁶
19. Although information about the general regulatory and economic environment may be helpful for users it does not contribute directly to fulfilling the objective of the financial statements. Consequently, we think that such general regulatory information should not be required in the financial statements. Users may be able to obtain the information from other sources (for example, (a) Management Commentary section of the annual report or (b) other available information on general economic conditions and expectations, political events and political climate, and industry and company outlooks).

Main focus of the overall disclosure objective

20. Considering the objective of the financial statements and the views of Board members on an earlier draft disclosure objective (paragraph 10), we think the disclosure objectives and disclosure requirements need to focus on the effects that the transactions or other events that give rise to regulatory timing differences⁷ have on the entity's financial performance and financial position. Such information will

⁶ Agenda Paper 11E discussed at the February 2018 Board meeting can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/february/iasb/ap11e-disclosure-initiative.pdf>

⁷ A regulatory timing difference is a timing difference that arises through the operation of the rate-adjustment mechanism when an entity fulfils service requirements in a different period than the period in which those service requirements are charged to customers through the regulated rate.

help users to better understand the entity's financial performance trend and help users to assess management's stewardship and the entity's prospects for future net cash inflows from its rate-regulated activities.

21. The financial information provided by the model will supplement the information that other Standards already require about other aspects of the entity's financial performance trend and the entity's prospects for future cash flow generation. For example, information about the entity's revenue from contracts with its customers is required by IFRS 15 *Revenue from Contracts with Customers*.

Overall disclosure objective

22. Consequently, considering all these matters we propose the following overall disclosure objective:

An entity shall disclose information that helps users of financial statements to understand how the origination and reversal of regulatory timing differences affect the entity's financial performance and financial position.

This information will be useful because it will help users to assess the entity's financial performance trends and the amounts, timing and uncertainty of its future cash flows.

Specific disclosure objectives

23. We propose three specific disclosure objectives to provide a more granular application of the overall disclosure objective as follows. We think the overall disclosure objective together with the specific disclosure objectives below help address the concerns from the Board in paragraph 10.

Specific disclosure objective 1—Financial performance

An entity shall disclose information about the effect of regulatory timing differences on the entity's revenues, regulatory income and regulatory expense recognised during the period and the relationship of those effects with the expenses recognised during the period.

This information will be useful because it will help users of financial statements to understand the effects of regulatory timing differences on the entities' financial performance by distinguishing between:

- fluctuations in revenue and expenses compensated for through rate-adjustment mechanisms; and
- fluctuations in revenue and expenses for which there is no compensation.

Specific disclosure objective 2—Amount, timing and uncertainty of future cash flows from regulatory assets and regulatory liabilities

An entity shall disclose information about:

- (a) the remaining time bands over which it expects to recover the carrying amounts of the regulatory assets and regulatory liabilities; and
- (b) uncertainties about the amount or timing of future cash flows from of regulatory assets and regulatory liabilities.

This information will be useful because it will help users of financial statements to understand the amount, timing and uncertainty of future cash flows that will result from the entity's regulatory assets and regulatory liabilities.

Specific disclosure objective 3—Changes in the carrying amounts of regulatory assets and regulatory liabilities

An entity shall disclose information that shows how the carrying amounts of regulatory assets and regulatory liabilities have changed from the beginning to the end of each reporting period presented.

This information will be useful because it will help users of financial statements to understand how the entity's financial position has been affected by transactions or other events during the period that caused changes in regulatory timing differences. Information about some changes in regulatory timing differences is already needed to meet specific disclosure objective 1. Specific disclosure objective 3 is necessary to cover other changes in regulatory timing differences, namely those changes that did not affect the amounts reported in the regulatory income/(expense) line item(s) in the statement of profit or loss and other comprehensive income.

Question for ASAF members**Overall disclosure objective and specific disclosure objectives**

1. Do ASAF members think the overall disclosure objective in paragraph 22 and specific disclosure objectives in paragraph 23 are appropriate and would:
 - (a) result in information that is useful for the users of the financial statements?
 - (b) facilitate judgement by entities in deciding what information to disclose?
2. Have ASAF members identified:
 - (a) any modifications we should consider making to the overall disclosure objective and specific disclosure objectives suggested in this section?

(b) any other specific disclosure objectives the staff should consider including?

Level of aggregation of disclosures

24. At the February 2018 meeting, the Board tentatively decided that the model will use as its unit of account the individual timing differences that create the supplementary rights and obligations arising from the regulatory agreement. In Agenda Paper 9A discussed at that meeting, the staff suggested that, for presentation and disclosure, it may be appropriate to group some timing differences with similar characteristics and risks and similar expiry patterns. The staff will ask the Board to decide about aggregation criteria for presentation and disclosure in a future meeting.⁸
25. Our views about the level of aggregation for disclosure have been informed by the following paragraphs of the *Conceptual Framework* (**emphasis added**):
- 7.7 Classification is the sorting of assets, liabilities, equity, income or expenses on the basis of shared characteristics for presentation and disclosure purposes. Such characteristics include-but are not limited to-the **nature of the item, its role (or function)** within the business activities conducted by the entity, and how it is measured.
 - 7.9 Classification is applied to the unit of account selected for an asset or liability (see paragraphs 4.48-4.55).
 - 4.49 A unit of account is selected for an asset or liability when considering how recognition criteria and measurement concepts will apply to that asset or liability and to the related income and expenses. [...] **For presentation and disclosure, assets, liabilities, income and expenses may need to be aggregated or separated into components.**

⁸ Agenda Paper 9A discussed at the February 2018 Board meeting can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/february/iasb/ap9a-rate-regulated-activities.pdf>

7.21 Aggregation makes information more useful by summarising a large volume of detail. However, aggregation conceals some of that detail. Hence, a balance needs to be found so that **relevant information is not obscured** either by a large amount of insignificant detail or by excessive aggregation.⁹

26. We also identified and considered some IFRS Standards that require disaggregation in the disclosure notes of the line items presented in the primary financial statements.¹⁰ Those Standards provide guidance about the level of disaggregation needed by identifying criteria that an entity could use, such as:¹¹

- (a) nature, characteristics and use;
- (b) how the item is measured; and
- (c) risks and degree of uncertainty.

27. We also considered current practice for entities applying IFRS 14, which requires disclosures about recognised amounts for each type of rate-regulated activity and for each class of regulatory balance. The Standard does not define what is meant by type of rate-regulated activity or class of regulatory balance but paragraph 30(c) of IFRS 14 states that a class of regulatory balance is a ‘type of cost or income’. We have observed that some rate-regulated entities have applied these requirements by grouping regulatory balances in the following categories:

- (a) by project or actions taken (eg ‘site restoration’, ‘dam safety’);
- (b) automatic rate adjustments (eg ‘fuel price adjustment’, ‘variance account’);

⁹ The requirements in paragraph 30A of IAS 1 *Presentation of Financial Statements* are also aligned to this paragraph.

¹⁰ Some of the IFRS Standards requiring disclosure by classes of assets or liabilities are as follows: IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*, IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, IFRS 13 *Fair Value Measurement* and IFRS 15 *Revenue from Contracts with Customers*.

¹¹ As part of the Primary Financial Statements project, work is currently being developed on proposals for improving disaggregation in the financial statements. The most recent discussion of the Board on this matter was at its May 2018 meeting (Agenda Paper 21A discussed at the May 2018 Board meeting can be found: <https://www.ifrs.org/-/media/feature/meetings/2018/may/iasb/ap21a-pfs.pdf>). We will monitor any progress so that any requirements we develop for the model are aligned to these proposals. Please note that Appendix B of Agenda Paper 21A includes an overview of characteristics for aggregation and disaggregation in IFRS Standards.

- (c) incentive mechanism (eg ‘incentive mechanism variance account’); and
- (d) timing differences that arise when the regulatory agreement uses a different basis for recognition of costs incurred than is used for IFRS purposes (eg IFRS uses accrual basis but the regulatory agreement may use cash basis—as is often the case for, for example, asset retirement obligations, pension obligations, or deferred tax).

Initial views on level of aggregation

28. Much of the work being done in the projects within the Board’s theme of ‘Better Communication in Financial Reporting’ is focused on helping entities apply better judgement about disclosures and communicate information more effectively to users of the financial statements.¹² Based on this work, our view is that the model should require entities **to apply judgement** when assessing how to aggregate regulatory assets and regulatory liabilities into groups of like items for disclosure. When assessing the level of aggregation, an entity should also consider materiality (ie the level of aggregation should not reduce the understandability of the financial statements by aggregating material items that have different characteristics).¹³ We think that different levels of aggregation may be appropriate for meeting different specific disclosure objectives.
29. We think that an entity could justify aggregating information about the total amounts of regulatory assets and of regulatory liabilities, perhaps with some supporting narrative when appropriate. This is because the features of the entity’s regulatory assets and regulatory liabilities (for example, characteristics, risks and degree of uncertainty etc) may be similar for the entire population of regulatory balances. However, an entity may consider disaggregating its regulatory assets and regulatory liabilities further if it concludes that further disaggregation would result in more relevant information for users of the financial statements.
30. For the statement(s) of financial performance, as stated in paragraph 6, we are likely to recommend that entities should present the following line items:

¹² ‘Better Communication in Financial Reporting’ highlights the importance and common themes of a number of the Board’s projects. More information on the projects is available on the Board’s website at <https://www.ifrs.org/projects/better-communication/#about>.

¹³ See paragraphs 30–31 of IAS 1.

- (a) regulatory income or regulatory expense recognised in profit or loss (possibly just as a single net amount); and
- (b) regulatory income or regulatory expense recognised in other comprehensive income (possibly with income netted against expenses).

31. However, to help users understand how and when regulatory timing differences affect revenue and expenses reported in the statement(s) of financial performance, we are likely to recommend that an entity should be required to disaggregate the regulatory income/(expense) line items into the following components, if material:¹⁴

- (a) amounts that an entity has a right to include in rates in a future period(s) as a result of rate-regulated activities carried out in the current period (ie origination of regulatory assets);
- (b) amounts already included in revenue in the current period for rate-regulated activities that the entity will carry out in a future period(s) (ie origination of regulatory liabilities);
- (c) amounts included in revenue relating to rate-regulated activities carried out in previous period(s) (ie recovery of regulatory assets);
- (d) amounts included in regulatory income as a result of rate-regulated activities carried out in the current period for which the entity had already charged customers in previous period(s) (ie fulfilment of regulatory liabilities); and
- (e) changes in the carrying amount of regulatory assets and regulatory liabilities due to changes in accounting estimates.

32. In addition, we think that entities should disaggregate the regulatory income/(expense) line item sufficiently to help users of financial statements to understand information that is disclosed for each reportable segment, if the entity applies IFRS 8 *Operating Segments*.¹⁵

¹⁴ These components are aligned to the disaggregation of the regulatory income/(expense) line item(s) in the disclosure requirement DR1 in paragraph 34.

¹⁵ Similarly, paragraph 115 of IFRS 15 requires entities to disclose sufficient information to enable users of financial statements to understand the relationship between the disclosure of disaggregated revenue and revenue information disclosed for each reportable segment applying IFRS 8.

Questions for ASAF members

Level of disaggregation of disclosures

3. Do ASAF members agree that the regulatory income/(expense) line item(s) should be disaggregated into:
 - a) originations of regulatory assets and of regulatory liabilities;
 - b) recoveries of regulatory assets and fulfilments of regulatory liabilities; and
 - c) changes in estimates
4. Do ASAF members think that an entity should be allowed to apply judgement to determine the level of aggregation of regulatory assets and regulatory liabilities needed to satisfy the disclosure objectives? If not, what criterion would you propose to determine the level of aggregation required?

Disclosure requirements

33. This section includes our initial views on the disclosure requirements (DR). In the Disclosure Initiative—Targeted Standards-level Review of Disclosures project the Board thinks that associating particular disclosure requirements with specific disclosure objectives prompts entities to apply judgement as to whether the information is material to their financial statements and whether the information provided meets user information needs. The symbol (✓) in Table 1 shows the associations between the disclosure requirements and each specific disclosure objective (SDO) in paragraph 23 (ie which disclosure requirements help fulfil which specific disclosure objectives):

Table 1—Linking disclosure requirements with specific disclosure objectives (SDO)			
Disclosure requirement (DR)	SDO— Financial performance	SDO—Amount, timing and uncertainty of future cash flows	SDO—Changes in the carrying amounts of regulatory assets and regulatory liabilities
DR1	✓		
DR2		✓	
DR3	✓	✓	
DR4			✓
DR5	✓	✓	✓

Disclosure requirement DR1

34. An entity shall consider disclosing:

- (a) a breakdown of the regulatory income / (expense) line item(s) in the statement(s) of financial performance into the following components:¹⁶
 - (i) amounts that an entity has a right to include in rates in a future period(s) as a result of rate-regulated activities carried out in the current period (ie origination of regulatory assets);
 - (ii) amounts already included in revenue in the current period for rate-regulated activities that the entity will carry out in a future period(s) (ie origination of regulatory liabilities);
 - (iii) amounts included in revenue relating to rate-regulated activities carried out in previous period(s) (ie recovery of regulatory assets);
 - (iv) amounts included in regulatory income as a result of rate-regulated activities carried out in the current period for which

¹⁶ These components are aligned to the disaggregation of the regulatory income/(expense) line item(s) described in paragraph 31.

the entity had already charged customers in previous period(s) (ie fulfilment of regulatory liabilities); and

- (v) changes in the carrying amount of regulatory assets and regulatory liabilities due to changes in estimates.
- (b) the breakdown in (a) for each reportable segment disclosed.
- (c) the reasons for the changes in estimates in (a) (v).

Disclosure requirement DR2

35. An entity shall consider disclosing:

- (a) a maturity analysis showing the remaining time bands over which the entity expects to recover the carrying amount of regulatory assets or to fulfil the carrying amount of regulatory liabilities. In preparing the maturity analyses an entity uses its judgement to determine an appropriate number of time bands. For example, an entity might determine that the following time bands are appropriate:
 - (i) not later than one year;
 - (ii) later than one year and not later than five years; and
 - (iii) later than five years.
- (b) how the future recovery of regulatory assets or the future fulfilment of regulatory liabilities is affected by risks and uncertainty, for example:
 - (i) regulatory risk (for example, the submission or approval of a rate-setting application or the entity's assessment of the expected future regulatory actions); and
 - (ii) demand risk (for example, changes in consumer attitudes, the availability of alternative sources of supply or the level of competition).¹⁷

Disclosure requirement DR3

36. An entity shall consider disclosing:

- (a) the discount rate or ranges of discount rates (expressed in the form of weighted averages or relatively narrow ranges) used to discount the

¹⁷ Part of this proposed requirement is captured in paragraph 33 (c) of IFRS 14.

estimated cash flows reflected in the carrying amounts of regulatory assets and the carrying amounts of regulatory liabilities at the end of the period.

- (b) any differences between the rate or range of rates used to discount any regulatory assets or regulatory liabilities and the interest or return rate or range of rates approved by the regulator to compensate or charge the entity for the time lag between the origination and recovery of regulatory assets or the origination and fulfilment of regulatory liabilities, and the reason for such differences.

Disclosure requirement DR4

37. An entity shall consider disclosing a reconciliation¹⁸ of the carrying amount of regulatory assets and the carrying amount of regulatory liabilities at the beginning and the end of the period, in a table unless another format is more appropriate. The entity shall apply judgement in deciding the level of detail provided but should consider disclosing the following components:
- (a) the amount(s) included in the regulatory income/(expense) line item(s) in the statement(s) of financial performance; and
 - (b) other amounts, separately identified, that affect the carrying amounts of regulatory assets and regulatory liabilities, such as items acquired or assumed in a business combination, items disposed of, or the effect of changes in foreign exchange rates.

Disclosure requirement DR5

38. Where required by IAS 1, an entity shall disclose the judgements that management has made in the process of applying the model and that have the most significant effect on the amounts of regulatory assets, regulatory liabilities, regulatory income and regulatory expense recognised in the financial statements.

Illustrative disclosures and usefulness of the resulting information

39. Agenda Paper 4C contains a case study that describes the origination and reversal of various timing differences for an entity (Entity A) during the periods X0–X3. Using

¹⁸ Paragraph 33(a) of IFRS 14 also includes a reconciliation.

the data from the case study, we illustrate some of the disclosure requirements discussed in this paper. We include here some aspects of the fact pattern from the case study to aid understanding. For those interested in learning more about the application of the model, Agenda Paper 4C contains more detailed information.

40. The case study assumes a base case scenario in which Entity A has forecast operating expenses of CU9,000 in each period X0–X3. The regulator has approved a rate to charge to customers for regulated services that is forecast to generate revenue of CU10,000 each period giving Entity A an estimated annual profit margin of 10%. However, during periods X0–X1, timing differences originate due to a variety of transactions and events that create regulatory assets and regulatory liabilities. During periods X1–X3, the rate that Entity A charges to customers for delivering service requirements results in the recovery of all the regulatory assets and fulfilment of all the regulatory liabilities that originated in X0–X1. For clarity, we assume there are no other timing differences to account for during the period X0–X3.
41. The following paragraphs and figures illustrate how some of the proposed disclosure requirements in paragraphs 34–38 might be satisfied for the period ended X1, with comparative information for X0. The illustration is not intended to be exhaustive nor is it intended to be prescriptive. Figure 1 shows the amounts presented in Entity A’s statement(s) of financial performance and statement of financial position at the end of each period X0–X1.¹⁹

Figure 1		
Statement(s) of financial performance	X0	X1
Revenue	10,200	10,498
Regulatory income / (expense)	1,280	(38)
Operating expenses	(10,700)	(9,350)
Profit / (loss)	780	1,110
Statement of financial position	X0	X1
Regulatory asset	1,620	1,292
Regulatory liability	340	50

¹⁹ As mentioned in paragraph 6, we will discuss with the Board recommendations for the number and location of line items to be required in the statement(s) of financial performance for the amounts of regulatory income and regulatory expense arising during the period. In this paper, we present these amounts netted in a single line item called ‘Regulatory income/ (expense)’ for illustrative purposes.

42. Figure 2 provides a breakdown of the regulatory income/(expense) line item in the statement(s) of financial performance applying DR1. In this example, no items affect other comprehensive income. Entity A could disaggregate the amount in the regulatory income/(expense) line item using the components detailed in DR1 as follows:

Figure 2		
Regulatory income/(expense) composition	X0	X1
Origination of regulatory assets	1,620	51
Fulfilment of regulatory liabilities	-	370
Recovery of regulatory assets	-	(459)
Origination of regulatory liabilities	(340)	(50)
Changes in estimates	-	50
Regulatory income / (expense)	1,280	(38)

43. The break down of the regulatory income/(expense) line item between origination and reversal of regulatory timing differences can give a user, for example, the following information:

- (a) periods that show significant originations of regulatory assets (ie reflected as regulatory income) indicate that the related expenses have been accounted for in the expense line items in profit or loss for the period but are not yet reflected in revenue because the entity is entitled to charge customers only in a later period(s). From that information, users can see that the entity carried out service requirements in X0 for which it will be able to bill CU1,620m in future period(s). Users can use that information both to improve their assessment of the future cash flows resulting from the regulatory asset, but also to improve their analysis of the trend of revenue and expenses;
- (b) periods that show significant originations of regulatory liabilities (ie reflected as regulatory expense) indicate that the entity received funding in advance for service requirements it needs to meet in future period(s). From that information, the user can see that CU340m of the entity's revenue for X0 related to service requirements that the entity will fulfil in later period(s). Users can use that information both to improve their assessment of the future cash flows that the entity will incur in

fulfilling the regulatory liability, but also to improve their analysis of the trend of revenue and expenses.

44. Figure 3 illustrates the maturity analysis of regulatory assets and regulatory liabilities according to DR2(a) that Entity A could provide at the end of X1 with comparative information for X0.²⁰ In this example, it is assumed that Entity A has determined that timing differences are sufficiently homogenous to group them using the total carrying amount of regulatory assets and the total carrying amount of regulatory liabilities.

Figure 3			
Maturity of regulatory assets	Total	1 year	1-3 years
Regulatory asset in year X0	1,620	720	900
Regulatory asset in year X1	1,292	677	615
Maturity of regulatory liabilities	Total	1 year	1-3 years
Regulatory liability in year X0	340	340	-
Regulatory liability in year X1	50	50	-

45. The maturity analysis may also provide users some (perhaps limited) information about the uncertainty of future cash flows because the length of the recovery or fulfilment period may affect the degree of uncertainty.
46. According to DR3 an entity would need to disclose discount rates used to discount. The example assumes all regulatory assets and regulatory liabilities outstanding at X1 attract the same annual interest rate. Consequently, Entity A could consider providing the following disclosure:

Cash flows from the regulatory assets and the regulatory liabilities are discounted at an annual interest rate of 3%. Those assets and liabilities attract annual interest at the same rate.

47. DR1(c) requires disclosure about reasons for the changes in estimates and DR2(b) requires entities to disclose how the future recovery/fulfilments of regulatory assets/regulatory liabilities is affected by risks and uncertainty. The following illustrate how those requirements could be satisfied to complement the information reflected through the maturity analysis. In this case, uncertainty about amounts

²⁰ Paragraph A2 of Appendix of Agenda Paper 4C explains how the amounts shown in Figure 3 were derived.

included in the X0 disclosures has been resolved by the regulator confirming the rate during X1.

Example A—Regulatory asset

During X0, Entity A incurred unexpected repair costs of CU1,640m due to damage caused to our network assets by Hurricane Henry. During X1, the entity received confirmation from the regulator that it can include the full amount in rates, plus annual interest of 3%, during the period X1–X3. In year X0, the entity estimated that it would be able to include CU1,560m plus annual interest of 3% in rates during X1–X2. Consequently, during X1, the entity increased the amount of the regulatory asset by CU80m. That increase is included in regulatory income.

Example B—Regulatory liability

During X1, Entity A received confirmation that the penalty imposed for failing to meet our customer satisfaction target during X0 is CU120m, which has been deducted through rates charged to customers during X1. Regulatory income for X1 includes:

- (a) CU120m reflecting the fact that the CU120m deducted through rates charged to customers in 20X1 was already recognised as regulatory expense in X0; and
- (b) CU20m because the penalty of CU120m confirmed in X1 was less than the estimated penalty of CU140m recognised as regulatory expense in X0 and as a regulatory liability at 31 December X0.

This regulatory liability did not attract interest.

48. Figure 4 illustrates the reconciliation of the total carrying amount of the regulatory assets and the total carrying amount of the regulatory liabilities from the beginning of X1 (end of X0) to the end of X1 according to DR4.²¹

²¹ Paragraph A3 of the Appendix in Agenda Paper 4C explains the calculation of the regulatory income/(expense) balances showed in Figure 4.

Figure 4				
Reconciliation of regulatory asset	X0	Regulatory income / (expense)	Other amounts	X1
Regulatory asset	1,620	(328)	-	1,292
Reconciliation of regulatory liability	X0	Regulatory income / (expense)	Other amounts	X1
Regulatory liability	(340)	290	-	(50)
Total regulatory income/(expense)		(38)		

49. As previously mentioned, according to DR1, Entity A would have provided a breakdown of the regulatory income / (expense) line item amounting to CU(38)m as illustrated in Figure 2.

Question for ASAF members

Disclosure requirements

5. Do ASAF members think the disclosure requirements are clear, complete and balanced (ie would result in useful information to users and would not result in disclosure overload)?
6. The disclosure requirements are drafted in a way that is intended to emphasise the use of judgement and to use less prescriptive language than the drafting style currently used in disclosure requirements in IFRS Standards. Do ASAF members think the drafting achieves this objective?