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Comments on the Exposure Draft *Regulatory Assets and Regulatory Liabilities*

1. The Accounting Standards Board of Japan (“the ASBJ” or “we”) welcome the opportunity to provide our comments on the International Accounting Standards Board (“the IASB”)’s Exposure Draft (ED/2021/1) *Regulatory Assets and Regulatory Liabilities* (hereinafter referred to as “the ED”), issued in January 2021.
2. We share the IASB's concern that the application of other IFRS Standards alone does not provide users of financial statements with sufficient information to assess future cash flows for entities subject to rate regulation. However, we disagree with the scope, accounting and presentation proposed in the ED.
3. The right to increase (or the obligation to decrease) the regulated rate (unit price) based on a regulatory agreement is a conditional right (or obligation) that results in different amounts of cash flows depending on whether the goods or services will be provided in the future and the quantity of those goods or services when they are provided. In recognising a conditional right (or obligation) as an asset (or liability), our understanding is that there are two general approaches: (a) one is to recognise the asset (or liability) regardless of the degree of the probability and incorporate the probability of the inflow or outflow of the economic benefits (outcome uncertainty) into the measurement, as in the case of financial instruments, and (b) the other is to recognise an asset (or liability) only when it satisfies the probability threshold, as in the case of contingent assets (or contingent liabilities).
4. The ED proposes that the right to increase (or the obligation to decrease) a regulated rate (unit price) based on a regulatory agreement be recognised regardless of the degree of probability of an inflow or outflow of economic benefits, and that the

uncertainty be reflected in measurement (paragraph BC126 of the ED). Accordingly, our understanding is that the proposal in the ED is consistent with approach (a) above.

5. The ED states that the purpose of the ED is to supplement the information provided by applying IFRS 15 *Revenue from Contracts with Customers* and other IFRS Standards (paragraph BC30 of the ED). We are of a view that approach (b) in paragraph 3 of this comment letter is appropriate from the perspective of ensuring consistency with the IFRS Standards that the ED purports to supplement. Accordingly, we comment mainly on the scope, accounting and presentation proposed in the ED on this basis.
6. As we explain in detail in the following paragraphs, we propose that transactions with a more limited scope than those proposed in the ED be recognised on the face of the financial statements. However, some ASBJ board members have expressed their views stating that issues related to rate regulation should be addressed by enhancing disclosures, rather than recognising and presenting regulatory assets or regulatory liabilities on the face of the financial statements, for the following reasons:
 - (a) Due to the existence of various regulations and the different stages of deregulation in each jurisdiction, the effects of rate regulation vary on a global basis. Under these circumstances, it would be difficult to develop accounting standards, due to challenging issues, including how to distinguish between rate regulated activities that should be recognised and those that should not and when rate regulated activities should be recognised how to ensure consistency in the accounting treatment on a global basis.
 - (b) It is inappropriate that only entities that are subject to rate regulation reflect their rights to increase (or obligations to reduce) the future regulated rate (unit price) on the face of the financial statements, because entities that are not subject to rate regulation may have similar rights to increase (or obligations to decrease) the future price (unit price) that does not arise from rate regulation.

(Scope)

7. The ED proposes that an entity be included in the scope of the ED if it is party to a regulatory agreement and the regulatory agreement determines the regulated rate (paragraph 6 of the ED). We are of a view that the following clarification is necessary because this proposal may make it difficult to determine whether or not an entity is included in the scope.

Characteristics of the transaction subject to the proposal

8. First, we propose that the term "regulatory framework" be used instead of the term "regulatory agreement" as used in the ED, and that the rights and obligations of an entity arising from a regulatory framework be included in the scope of the ED. We further propose clarifying that a regulatory framework may include a contract between the entity and the regulator, as well as any law or regulation that becomes applicable by performing an act that is subject to that law or regulation. We are of a view that the term "framework" is more appropriate because, as the ED acknowledges, there may be cases where there is no regulatory body, but the term "agreement" implies the existence of multiple parties.¹
9. Next, we propose that the transactions subject to the ED be clarified by specifying the characteristics of customers and transactions that are affected by the regulatory agreement and that the transaction would be subject to the ED, in addition to IFRS 15.

Please refer to paragraph 5 of the Appendix to this comment letter for details.

Unit of account

10. The ED proposes that the right or obligation arising from each individual difference in timing be accounted for as a separate unit of account (paragraph 24 of the ED). Our understanding is that this proposal is intended to require entities to account for each of the factors specified in the regulatory agreement as triggering adjustments to future rates, and we are of a view that this should be clarified. In addition, although the unit of account is described in the ED immediately before the provisions related to recognition, we are of a view that this unit of account should also be considered in the determination of the scope and therefore propose that it be included in the provisions related to scope.

Probability of the inflow or outflow of economic benefits from the transaction subject to rate regulation

11. Because the scope is not necessarily clear and the ED proposes the recognition of regulatory assets or regulatory liabilities regardless of the degree of the probability,

¹ Although we propose changing the term to "regulatory framework," the remainder of this comment letter will continue to use the term "regulatory agreement" for the ease of reading.

we are concerned that the proposal in the ED may result in the recognition of items for which an inflow or outflow of economic benefits is not probable.

12. We do not support such proposal. Instead, we propose that the following requirements be established to ensure that only the items for which an inflow or outflow of economic benefits is probable will be recognised.
 - (a) The degree of probability that the future regulated rate will increase (or decrease) based on the regulatory agreement if sales are lower (or higher) or costs of goods sold are higher (or lower) than expected (or both) is sufficiently high. Although this requirement is described in the ED as a requirement for recognition in the context of existence uncertainty of the regulatory asset and the regulatory liability, we propose that this be a requirement in the context of scope.
 - (b) Sufficient demand exists for the goods or services subject to rate regulation such that the recovery of the regulatory asset and the fulfilment of the regulated liability can be expected when the future regulated rate is increased (or decreased) (in determining whether sufficient demand exists, the impact on demand of future price adjustments shall also be considered).

(Accounting and presentation)

13. We are of a view that regulatory assets and regulatory liabilities included in the scope based on our proposal should be accounted for and presented in the following manner.

Assets

14. A regulatory asset arising from the right to increase the regulated rate (unit price) typically arises when sales are lower than expected or costs of goods sold are higher than expected (or both). Regulatory assets typically arise from the excess of the costs of goods sold that have actually incurred, not from the sales that have not yet occurred.
15. Regarding the measurement of the right to increase the future regulated rates, in addition to considering the consistency with IFRS 15, which the ED is intended to supplement, and the consistency with the measurement requirements in IAS 36 *Impairment of Assets*, the best estimate should be made for the amount of excess costs of goods sold that have incurred and that is expected to result in an inflow of economic benefits from future increases in regulated rates, taking into account the future demand risks and credit risks of the customer group.
16. When the asset is recovered over a long period of time, we agree that it is necessary to adjust for the time value of money. However, the discount rate to be used in this

case should not be the regulatory interest rate as proposed in the ED, but a rate that reflects the time value of money and the current market valuation of risks inherent in the asset (demand risks and credit risks), such as the discount rate used in IAS 36. As stated in IAS 36, the discount rate shall not reflect risks for which the future cash flow estimates have been adjusted; otherwise, the effect of some risks will be double-counted.

17. If the regulatory agreement only prescribes the right to recovery and the scope of that right, but does not specify the timing of such recovery, we propose not to discount. In addition, in our view, a practical expedient should be provided so that the entity can choose not to discount if the time to recovery is less than one year.
18. When a regulatory asset is recognised based on our proposal, a regulatory asset typically arises from the excess of costs of goods sold. Accordingly, we are of a view that the changes (including changes arising from the unwinding of the discount on the regulatory asset) should be accounted for as an adjustment to costs of goods sold, rather than as an adjustment to sales as proposed in the ED. In this case, instead of directly adding (or deducting) the adjustment amount to (or from) the costs of goods sold, we propose that the adjustment amount be presented as a separate line item so that the costs of goods sold can be adjusted indirectly.

Please refer to paragraphs 11 through 16, 28 and 29 of the Appendix to this comment letter for details.

Liabilities

19. A regulatory liability arising from the obligation to decrease the regulated rate (unit price) typically arises when sales are higher than expected or costs of goods sold are lower than expected (or both). Regulatory liabilities typically arise from the excess of the sales that have actually occurred, not from the costs that have not yet incurred.
20. Regarding the measurement of the obligation to decrease the future regulated rates, in addition to considering the consistency with IFRS 15, which the ED is intended to supplement, and the consistency with the measurement requirements in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, the best estimate should be made for the sales that have occurred and that is expected to result in an outflow of economic benefits from future decreases in regulated rates, taking into account the future demand risks of the customer group.
21. When the liability is fulfilled over a long period of time, we agree that it is necessary to adjust for the time value of money. However, the discount rate to be used in this

case should not be the regulatory interest rate as proposed in the ED, but a rate that reflects the time value of money and the current market valuation of risks inherent in the liability (demand risks), such as the discount rate used in IAS 37. The discount rate shall not reflect risks for which the future cash flow estimates have been adjusted; otherwise, the effect of some risks will be double-counted.

22. If the regulatory agreement only prescribes the obligation to fulfilment and the scope of that obligation, but does not specify the timing of such fulfilment, we propose not to discount. In addition, in our view, a practical expedient should be provided so that the entity can choose not to discount if the time to fulfilment is less than one year.
23. When a regulatory liability is recognised based on our proposal, a regulatory liability typically arises from the excess of sales. Accordingly, we are of a view that the changes (including changes arising from the unwinding of the discount on the regulatory liability) should be accounted for as an adjustment to sales, as proposed in the ED. In this case, instead of directly adding (or deducting) the adjustment amount to (or from) the sales, we propose that the adjustment amount be presented as a separate line item so that the sales can be adjusted indirectly.

Please refer to paragraphs 17-21 and 30-31 of the Appendix to this comment letter for details.

(Global convergence of accounting standards)

24. While local accounting standards in our jurisdiction do not recognise regulatory assets and regulatory liabilities, our understanding is that the dominant practice in jurisdictions that recognise regulatory assets and regulatory liabilities is based on U.S. GAAP. We note that the requirements in U.S. GAAP are closer to our proposed accounting compared to those proposed in the ED in that the scope is limited² and that regulatory assets are recognised based on the costs that have actually incurred.
25. If the ED is finalised as proposed, our understanding is that it will result in a significant change in practice, not only for entities in jurisdictions that have not previously recognised regulatory assets and regulatory liabilities, but also for entities in jurisdictions that have been recognising regulatory assets and regulatory liabilities. We have many reservations with the proposals in the ED and we are not convinced that the benefits of adopting the proposals would outweigh the costs. We urge the

² Paragraph 980-10-15-2 of the FASB Accounting Standards Codification.

IASB to develop standards that are more beneficial and less burdensome for all that are concerned, considering our proposals and the requirements in U.S. GAAP.

(Conclusion)

26. For our comments on individual questions, please refer to the Appendix of this comment letter.
27. We hope our comments contribute to the IASB's deliberations. Please contact us if you have any questions.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'A. Kogasaka'.

Atsushi Kogasaka
Chair

Accounting Standards Board of Japan

Our comments on individual questions

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).³ 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

³ 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.

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. We disagree with the proposal in the ED for the following reasons.
2. The ED proposes that an entity be included in the scope of the ED if it is party to a regulatory agreement and the regulatory agreement determines the regulated rate (paragraph 6 of the ED). We are of a view the following clarification is necessary because this proposal may make it difficult to determine whether or not an entity is included in the scope.

Characteristics of the transaction subject to the proposal

3. First, we propose that the term "regulatory framework" be used instead of the term "regulatory agreement" as used in the ED, and that the rights and obligations of an entity arising from a regulatory framework be included in the scope of the ED. We further propose clarifying that a regulatory framework may include a contract between the entity and the regulator, as well as any law or regulation that becomes applicable by performing an act that is subject to that law or regulation. We are of a view that the term "framework" is more appropriate because, as the ED acknowledges, there may be cases where there is no regulatory body, but the term "agreement" implies the existence of multiple parties.⁴
4. The conditions of the regulatory agreement should be objective and sufficiently clear in order to serve as the basis for determining the existence of regulatory assets and regulatory liabilities. In this respect, we are of a view that the scope proposed in paragraph 6 of the ED alone, which sets forth the requirements for the existence of a regulatory asset or regulatory liability, is not clear, and that the examples in paragraph 27 of the ED, which illustrate whether a regulatory asset or regulatory liability exists, are too broad.
5. Next, we propose that the transactions subject to the ED be clarified by specifying the characteristics of customers and transactions that are affected by the regulatory agreement and that the transaction would be subject to the ED, in addition to IFRS 15. We are of a view that the transactions subject to the ED would have all of the following characteristics.

⁴ Although we propose changing the term to "regulatory framework," the remainder of this comment letter will continue to use the term "regulatory agreement" for the ease of reading.

- (a) A group of customers (such as customers living in a certain area) can be identified. The individual customers that comprise the group of customers may vary from period to period.
- (b) Uniform goods and services are provided on a continuous basis to the group of customers, and a uniform regulated rate structure is applied. The regulated rate structure is determined by the regulatory agreement and may vary from period to period.
- (c) The uniform regulated rate structure is established for each period and is enforced on the customers. The regulated rate structure is adjusted for any amount overcharged or undercharged to the group of customers.

Unit of account

- 6. The ED proposes that the right or obligation arising from each individual difference in timing be accounted for as a separate unit of account (paragraph 24 of the ED). Our understanding is that this proposal is intended to require entities to account for each of the factors specified in the regulatory agreement as triggering adjustments to future rates, and we are of a view that this should be clarified. In addition, although the unit of account is described in the ED immediately before the provisions related to recognition, we are of a view that this unit of account should also be considered in the determination of the scope and therefore propose that it be included in the provisions related to scope.

Probability of the inflow or outflow of economic benefits from the transaction subject to rate regulation

- 7. Because the scope is not necessarily clear and the ED proposes the recognition of regulatory assets or regulatory liabilities regardless of the degree of the probability, we are concerned that the proposal in the ED may result in the recognition of items for which an inflow or outflow of economic benefits is not probable.
- 8. We do not support such proposal. Instead, we propose that the following requirements be established to ensure that only the items for which an inflow or outflow of economic benefits is probable will be recognised.
 - (a) The degree of probability that the future regulated rate will increase (or decrease) based on the regulatory agreement if sales are lower (or higher) or costs of goods sold are higher (or lower) than expected (or both) is sufficiently high. Although this requirement is described in the ED as a requirement for recognition in the

context of existence uncertainty of the regulatory asset and the regulatory liability, we propose that this be a requirement in the context of scope.

- (b) Sufficient demand exists for the goods or services subject to rate regulation such that the recovery of the regulatory asset and the fulfilment of the regulated liability can be expected when the future regulated rate is increased (or decreased) (in determining whether sufficient demand exists, the impact on demand of future price adjustments shall also be considered).

9. The proposal in the previous paragraph would limit the types of rate regulation that would be included in the scope of accounting standards. This limitation has the advantage that by recognising only those for which the probability is high (that is, not recognising those for which the probability is low), typical types of rate regulation would be covered, and the usefulness of financial information provided by entities subject to such rate regulation would be enhanced. On the other hand, it has the disadvantage that rate regulations that otherwise would have been covered would no longer be covered. Limiting the scope would cause such trade-off, but we are of a view that the advantages of limiting the scope would be greater than the disadvantages.

<p>Question 2—Regulatory assets and regulatory liabilities</p> <p>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.</p> <p>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.</p> <p>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.</p> <ul style="list-style-type: none"> (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?

10. We disagree with the proposal in the ED. We are of a view that regulatory assets and regulatory liabilities included in the scope based on our proposal should be accounted for in the following manner.

Assets

11. A regulatory asset arising from the right to increase the regulated rate (unit price) typically arises when sales are lower than expected or costs of goods sold are higher than expected (or both).
12. Regulatory assets typically arise from the excess of the costs of goods sold that have actually incurred, not from the sales that have not yet occurred. The right to increase the regulated rate arises from goods or services already provided in accordance with the terms of the regulatory agreement, but does not constitute the consideration for those goods or services already provided, and no sales of goods or services for which the regulated rate is increased have occurred. In other words, this right is triggered by the excess of the costs of goods sold of the goods or services that have already been provided.
13. Regarding the measurement of the right to increase the future regulated rates, in addition to considering the consistency with IFRS 15, which the ED is intended to supplement, and the consistency with the measurement requirements in IAS 36 *Impairment of Assets*, the best estimate should be made for the amount of excess costs of goods sold that have incurred and that is expected to result in an inflow of economic benefits from future increases in regulated rates, taking into account the future demand risks and credit risks of the customer group.

14. When the asset is recovered over a long period of time, we agree that it is necessary to adjust for the time value of money. However, the discount rate to be used in this case should not be the regulatory interest rate as proposed in the ED, but a rate that reflects the time value of money and the current market valuation of risks inherent in the asset (demand risks and credit risks), such as the discount rate used in IAS 36. As stated in IAS 36, the discount rate shall not reflect risks for which the future cash flow estimates have been adjusted; otherwise, the effect of some risks will be double-counted.
15. If the regulatory agreement only prescribes the right to recovery and the scope of that right, but does not specify the timing of such recovery, we propose not to discount. In addition, in our view, a practical expedient should be provided so that the entity can choose not to discount if the time to recovery is less than one year.
16. U.S. GAAP, which requires the capitalisation of incurred costs that meet certain criteria, does not require discounting. However, in our proposal, we propose recognising future recoveries and, in principle, to discount them.

Liabilities

17. A regulatory liability arising from the obligation to decrease the regulated rate (unit price) typically arises when sales are higher than expected or costs of goods sold are lower than expected (or both).
18. Regulatory liabilities typically arise from the excess of the sales that have actually occurred, not from the costs that have not yet incurred. The liability to reduce the regulated price is a liability to reimburse a portion of the revenue that have arisen from contracts with customers.
19. Regarding the measurement of the obligation to decrease the future regulated rates, in addition to considering the consistency with IFRS 15, which the ED is intended to supplement, and the consistency with the measurement requirements in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, the best estimate should be made for the sales that have occurred and that is expected to result in an outflow of economic benefits from future decreases in regulated rates, taking into account the future demand risks of the customer group.
20. When the liability is fulfilled over a long period of time, we agree that it is necessary to adjust for the time value of money. However, the discount rate to be used in this case should not be the regulatory interest rate as proposed in the ED, but a rate that

reflects the time value of money and the current market valuation of risks inherent in the liability (demand risks), such as the discount rate used in IAS 37. The discount rate shall not reflect risks for which the future cash flow estimates have been adjusted; otherwise, the effect of some risks will be double-counted.

21. If the regulatory agreement only prescribes the obligation to fulfilment and the scope of that obligation, but does not specify the timing of such fulfilment, we propose not to discount. In addition, in our view, a practical expedient should be provided so that the entity can choose not to discount if the time to fulfilment is less than one year.

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?

22. We disagree with the accounting model proposed in the ED that adjusts revenue for all changes in regulatory assets and regulatory liabilities. However, if this accounting model were to be applied, we are of a view that Question 3(a)(ii) "regulatory returns on a balance relating to assets not yet available for use" would need to be modified to treat such returns as part of total allowed compensation in the same manner as other regulatory returns. The reasons are as follows:

- (a) Regulatory returns, including regulatory returns on balances relating to assets not yet available for use, are not of the nature that claiming those returns in one

period would result in the need to return a portion of those returns in a different period. Therefore, it would be more appropriate to treat those returns as total allowed compensation in the period in which the entity is entitled to charge those returns (and thus not to subsequently adjust those returns as regulatory income or regulatory expense) because doing so would better reflect the substance of the regulation.

- (b) In addition, considering that the regulatory returns has an aspect of recovering the financing costs, if the regulatory agreement allows recovery through the regulated rate even before the operation begins, it would be a faithful representation of the substance to account for it as such (that is, no adjustment in the regulatory accounts).
- (c) Assets subject to regulatory returns often consist of multiple assets, and in such cases, it would be practically cumbersome to separately treat only those assets that are not yet available for use.

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?

23. We disagree with the proposal in the ED. Our view is provided in our responses to question 1.

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?

24. Our view is provided in our responses to question 2.

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?

25. We disagree with the proposal in the ED. Our view is provided in our responses to question 2.

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?

26. Our view is provided in our responses to question 2. Because the model in the ED and our proposal use different assumptions regarding the discount rate, we refrain from answering these questions.

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. Paragraphs BC178–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?

27. We disagree with the proposal in the ED. We are of a view that regulatory assets and regulatory liabilities included in the scope based on our proposal should be presented in the following manner.

Assets

28. When a regulatory asset is recognised based on our proposal, a regulatory asset typically arises from the excess of costs of goods sold. Accordingly, we are of a view that the changes (including changes arising from the unwinding of the discount on the regulatory asset) should be accounted for as an adjustment to costs of goods sold, rather than as an adjustment to sales as proposed in the ED.
29. The change in the regulatory asset is recognised to provide supplementary information regarding the expected amount of benefits to inflow in the future based on regulatory agreements, for costs recognised in accordance with other IFRS Standards. Therefore, instead of directly adding (or deducting) the adjustment amount to (or from) the costs of goods sold, we propose that the adjustment amount be presented as a separate line item so that the costs of goods sold can be adjusted indirectly.

Liabilities

30. When a regulatory liability is recognised based on our proposal, a regulatory liability typically arises from the excess of sales. Accordingly, we are of a view that the changes (including changes arising from the unwinding of the discount on the

regulatory liability) should be accounted for as an adjustment to sales, as proposed in the ED.

31. The change in the regulatory liability is recognised to provide supplementary information regarding the expected amount of benefits to outflow in the future based on regulatory agreements, for revenue recognised in accordance with IFRS 15. Therefore, instead of directly adding (or deducting) the adjustment amount to (or from) the sales, we propose that the adjustment amount be presented as a separate line item so that the sales can be adjusted indirectly.

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?

32. Our view is provided in our responses to question 8.

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.

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| <p>(a) Do you agree with these proposals?</p> <p>(b) Do you have any comments you wish the Board to consider when it sets the effective date for the Standard?</p> |
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33. We disagree with the accounting model proposed in the ED that adjusts revenue for all changes in regulatory assets and regulatory liabilities, and therefore refrain from answering these questions.

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.

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| <p>(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?</p> <p>(b) Do you have any comments on the proposed amendments to other IFRS Standards?</p> |
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34. We disagree with the accounting model proposed in the ED that adjusts revenue for all changes in regulatory assets and regulatory liabilities, and therefore refrain from answering these questions.

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.

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| <p>(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?</p> <p>(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?</p> <p>(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?</p> |
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35. We disagree with the accounting model proposed in the ED that adjusts revenue for all changes in regulatory assets and regulatory liabilities, and therefore refrain from answering these questions.

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?
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36. While local accounting standards in our jurisdiction do not recognise regulatory assets and regulatory liabilities, our understanding is that the dominant practice in jurisdictions that recognise regulatory assets and regulatory liabilities is based on U.S. GAAP. We note that the requirements in U.S. GAAP are closer to our proposed accounting compared to those proposed in the ED in that the scope is limited⁵ and that regulatory assets are recognised based on the costs that have actually incurred.
37. If the ED is finalised as proposed, our understanding is that it will result in a significant change in practice, not only for entities in jurisdictions that have not previously recognised regulatory assets and regulatory liabilities, but also for entities in jurisdictions that have been recognising regulatory assets and regulatory liabilities. We have many reservations with the proposals in the ED and we are not convinced that the benefits of adopting the proposals would outweigh the costs. We urge the IASB to develop standards that are more beneficial and less burdensome for all that are concerned, considering our proposals and the requirements in U.S. GAAP.

⁵ Paragraph 980-10-15-2 of the FASB Accounting Standards Codification.