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Project	**Rate-regulated Activities**
Paper topic	Illustrative disclosures

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Purpose of this paper

1. The purpose of this paper is to illustrate some of the recommended disclosure requirements in Agenda Paper 9D. That agenda paper contains questions for the Board about the usefulness and completeness of the recommended disclosure requirements. This paper contains no further questions.

2. Paragraphs 3–4 provide the main assumptions embedded in the fact pattern upon which the illustrative disclosures have been built and paragraphs 5–20 include the illustrative disclosures.

Fact pattern

3. The illustrative disclosures in this paper include the following assumptions for an entity (Entity A):

   (a) Entity A has forecast operating expenses of CU9,000 in each period X0-X3 and forecast revenue of CU10,000 each period on the basis of the regulatory rate(s) to be charged to customers (ie an estimated annual profit margin of 10%);

(b) during X0–X1, regulatory timing differences originate due to a variety of transactions and events that create regulatory assets and regulatory liabilities;

(c) during 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;

(d) there are no other regulatory timing differences to account for during the period X0–X3. None of the regulatory timing differences affect other comprehensive income in this fact pattern; and

(e) Entity A has taken into account materiality considerations when deciding what informaiton to disclose. In other words, the fact pattern assumes all illustrative disclosures correspond to material items for Entity A.

4. The illustrative disclosures in paragraphs 5–20 relate to the period ended X1, with comparative information for X0. Entity A has assessed that this information fulfils the overall disclosure objective and the specific disclosure objectives as described in Agenda Paper 9D. The illustration is not intended to be prescriptive.

Illustrative disclosures

5. 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 and X1.[1]

Figure 1		
Statement(s) of financial performance	**X0**	**X1**
Revenue	10,200	10,039
Regulatory income / (expense)	1,280	421
Operating expenses	(10,700)	(9,350)
Profit / (loss)	**780**	**1,110**
Statement of financial position	**X0**	**X1**
Regulatory asset	1,620	1,751
Regulatory liability	340	50

1 The presentation of the regulatory income/(expense) line item in the statement(s) of financial performance in this paper is aligned to the recommended presentation requirements in Agenda Paper 9C.

6. According to Disclosure Requirement 1(a) (DR1(a)), Entity A provides a breakdown of the regulatory income/(expense) line item in the statement(s) of financial performance as follows (Figure 2):

Figure 2		
Regulatory income/(expense) composition	**X0**	**X1**
Origination of regulatory assets	1,620	51
Fulfilment of regulatory liabilities	-	320
Origination of regulatory liabilities	(340)	(50)
Changes in estimates	-	100
Regulatory income / (expense)	**1,280**	**421**

7. The fact pattern assumes that there have been no recoveries of regulatory assets during the period X0–X1.

8. According to DR1(b), Entity A provides:

(a) further disaggregation of the amounts included in the origination of regulatory assets and origination of regulatory liabilities (Figure 3); and

Figure 3		
Origination of regulatory assets	**X0**	**X1**
Storm damage repair costs	1,560	49
Others	60	2
Regulatory income	**1,620**	**51**
Origination of regulatory liabilities	**X0**	**X1**
Customer prepayments	200	-
Performance penalty	140	-
Others	-	50
Regulatory expense	**340**	**50**

(b) a qualitative description of the reasons of the disaggregated amounts in bullet (a). See paragraphs 9–11.

9. For example, for the period ended X0, Entity A would have disclosed the following relating to its originations of regulatory assets (Table 1):

Table 1—Drivers for the originations of regulatory assets in X0
Storm damage repair costs[2] Included in regulatory income for the year there is an amount of CU 1,560m that has been recognised as a regulatory asset and relates to unexpected costs incurred on repairs of damage caused to our network assets by Hurricane Henry. The regulatory asset amounting to CU 1,560m is subject to the regulator’s final rate approval. The balance is expected to be recovered over a period of 2 years during X1–X2 and is assumed to carry interest of 3% on the outstanding amount at the start of each year.

10. For the period ended X0, Entity A would have disclosed the following relating to its origination of regulatory liabilities (Table 2):

Table 2—Drivers for the origination of regulatory liabilities in X0
Customer prepayments During X0, Entity A billed customers an amount of CU200m as a prepayment for services to be delivered in X1. This liability does not attract interest. All related expenses for fulfilment of the service requirements are expected to be incurred in X1. **Performance penalty** In X0, Entity A recognised an estimated performance penalty of CU140m for failing to meet a customer satisfaction target during the same period. The penalty amount will be deducted from billings to customers during X1 and the liability does not attract interest. The corresponding regulatory liability of CU140m recognised in X0 is subject to the regulator’s final rate determination.

[2] Tables 1 and 2 also provide information relating to disclosure requirements on regulatory risks according to DR2(b) and disclosure requirements on discount rate used according to DR3(a)—(see paragraphs 15 and 17). Entity A presents all the information relating to the same event or transaction (eg ‘storm damage repair costs’) together as this results in a more effective disclosure.

11. For the period ended X1, Entity A would have disclosed the following relating to its originations of regulatory assets (Table 3):

Table 3—Drivers for the originations of regulatory assets in X1
Storm damage repair costs[3] In year X0, Entity A estimated that it would be able to include CU1,560m in rates, plus annual interest of 3%, during the period X1–X2, relating to costs incurred in X0 repairing damage caused by Hurricane Henry. During X1, Entity A received confirmation from the regulator that it can include an additional CU80 of costs incurred for those repairs in rates during the period X2–X3, plus annual interest of 3% on the balance of the regulatory asset outstanding at the beginning of each period. Consequently, during X1, Entity A increased the amount of the related regulatory asset by CU80m and recognised regulatory income for the change in estimate. In addition, regulatory income reflecting the regulatory interest accrued of CU49m has been recognised as a further origination of the regulatory asset.

12. According to DR1(c), Entity A provides:

(a) quantitative information on the changes in estimates included in its regulatory income/(expense) line item for the period X0–X1 (see Figure 4); and

Figure 4		
Changes in estimates	**X0**	**X1**
Included in profit or loss		
Storm damage repair asset	-	80
Performance penalty liability	-	20
Regulatory income / (expense)	**-**	100

(b) qualitative information about the reasons for the changes in estimates (see Table 4). In Table 3, Entity A provided information about changes in estimates relating to the storm damage repair costs.

3 The information disclosed for the storm damage repair costs in Table 3 also covers disclosure requirements on changes in estimates according to DR1(c) (see paragraph 12(b)).

Table 4—Changes in estimates in X1
Performance penalty During X0, Entity A recognised a regulatory expense and related regulatory liability for an estimated penalty amounting to CU140m, resulting from the entity failing to meet a regulatory performance target. During X1, the entity received confirmation from the regulator that the penalty was set at CU120m. During X1, Entity A fulfilled the regulatory liability by deducting an amount of CU120m through the rate charged to its customers, recognising the CU20 change in the estimated amount in regulatory income.

13. According to DR2(a), Entity A discloses information about the maturity of its regulatory assets and regulatory liabilities at the end of X1 with comparative information for X0 (see Figure 5). The fact pattern assumes that Entity A has determined that its regulatory assets and regulatory liabilities are sufficiently homogenous to group them together according to their total carrying amounts.

Figure 5

Maturity of regulatory assets	Total	1 year	1-5 years
Regulatory asset in year X0	1,620	720	900
Regulatory asset in year X1	1,751	931	820

Maturity of regulatory liabilities	Total	1 year	1-5 years
Regulatory liability in year X0	340	340	-
Regulatory liability in year X1	50	50	-

14. In addition to disclosing the maturity analysis, according to DR2(b), Entity A provides information on risks and uncertainties associated with the regulatory assets and regulatory liabilities outstanding as of the reporting date.

15. For the period X0, Entity A provided disclosures about risks and uncertainties associated with the regulatory assets and regulatory liabilities outstanding in X0 (Tables 1 and 2). For the period ended X1, Entity A would have disclosed the following:

Table 5—Disclosure of risks and uncertainties in X1
As of the reporting date, there are no material amounts of regulatory assets or regulatory liabilities pending approval of or confirmation from the regulator.

16. According to DR3(a), Entity A discloses the discount rates used to discount the estimated cash flows reflected in the carrying amounts of the regulatory assets and regulatory liabilities outstanding at the end of the period X1. The fact pattern assumes that all regulatory assets and regulatory liabilities outstanding at X1 attract the same annual interest rate, which is the same as the interest rate approved by the regulator. Consequently, Entity A provides the following disclosure:

Table 6—Disclosure of discount rates used
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.

17. Entity A also disclosed the discount rates used when providing information on the originations of regulatory assets (see Tables 1 and 3) and on the originations of regulatory liabilities (see Table 2).

18. According to DR4, Entity A discloses the reconciliation of the total carrying amount of the regulatory assets and the total carrying amount of the regulatory liabilities from the beginning to the end of both periods, X0 and X1 (see Figure 6).

Figure 6				
For X0				
Reconciliation of regulatory asset	**Opening**	**Regulatory income / (expense)**	**Other amounts**	**X0**
Regulatory asset	-	1,620	-	1,620
Reconciliation of regulatory liability	**Opening**	**Regulatory income / (expense)**	**Other amounts**	**X0**
Regulatory liability	-	(340)	-	(340)
Total regulatory income/(expense)		1,280		

For X1				
Reconciliation of regulatory asset	**X0**	**Regulatory income / (expense)**	**Other amounts**	**X1**
Regulatory asset	1,620	131	-	1,751
Reconciliation of regulatory liability	**X0**	**Regulatory income / (expense)**	**Other amounts**	**X1**
Regulatory liability	(340)	290	-	(50)
Total regulatory income/(expense)		421		

19. As previously mentioned, according to DR1(a), Entity A provided a breakdown of the regulatory income / (expense) line item amounting to CU1,280m and CU421m in X0 and X1, respectively (see Figure 2).

20. As required by IAS 1 *Presentation of Financial Statements*, Entity A would have also disclosed in the notes to the financial statements:

(a) its significant accounting policies relating to its rate regulated activities;[4] and

(b) judgements and estimates that management has made in the process of applying the model and that have had the most significant effect on the amounts of regulatory assets, regulatory liabilities, regulatory income and regulatory expense recognised in the financial statements.[5]

[4] Paragraph 117 of IAS 1.

[5] Paragraphs 122 and 125 of IAS 1.