IFRS

STAFF PAPER

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Consultative Group for Rate Regulation Meeting

Project	**Rate-regulated Activities**		
Paper topic	Uncertainty		
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Purpose of the paper

1. We ask Consultative group members to provide information about the sources of uncertainty arising from the rate-adjustment mechanism and how such uncertainty is dealt with in practice, for both regulatory and financial reporting purposes, when recognising and measuring rate adjustments. This information will inform the Board's decisions about recognition, measurement and disclosure requirements for the model.

Summary of the Board's discussions so far

2. In its June 2017 meeting, the Board discussed examples of rate-adjustments illustrating how the model could recognise:
   (a) the origination of a regulatory rate adjustment in profit or loss;
   (b) the pattern and timing of the reversing adjustment(s) in profit or loss; and
   (c) the resulting outstanding rate-adjustment balance (ie regulatory asset or regulatory liability) at each reporting date in the balance sheet.

3. The examples assumed:

   (a) the regulatory agreement was sufficiently explicit that there was no uncertainty that the regulatory asset or regulatory liability existed; and

   (b) there was a high probability that the regulatory asset or regulatory liability would result in an inflow or outflow of economic benefits at the time and in the amounts estimated.

4. In its July 2017 meeting, the Board began to discuss possible implications for applying the model in conditions of uncertainty about the existence, outcome and measurement of regulatory rate-adjustments. Board members acknowledged that uncertainty arises in many situations and so most existing IFRS Standards require the use of estimates and judgements. Consequently, in developing the model, the Board is not looking to restrict the recognition of regulatory assets and regulatory liabilities to those whose existence or outcome is certain.

5. However, before asking the Board to reach a preliminary view about recognition and measurement requirements for the model, we are interested to learn more about how, for both regulatory and financial reporting purposes, entities approach circumstances in which:

   (a) judgement is needed to determine whether a particular transaction or other event is captured by the rate-adjustment mechanism; or

   (b) a particular transaction or other event is captured by the rate-adjustment mechanism but judgement is needed to determine whether, and if so at what amount, the rate-adjustment will ultimately be reflected in the amounts billed to customers. For example, the rate-adjustment may reflect an estimation variance but the correction of the variance may be constrained by a 'variance collar' (ie an adjustment to the rate is triggered only if the cumulative estimation variance exceeds a specified floor, or is below a specified cap, at a date that is not the entity's IFRS reporting date).

6. Specifically, we would like to know how uncertainty is reflected in decisions about the timing and amount of regulatory assets or regulatory liabilities:

   (a) recognised in financial statements prepared using IFRS 14 *Regulatory Deferral Accounts* or local GAAP; or

   (b) included in information prepared for management purposes if the entity does not recognise regulatory assets or regulatory liabilities in its financial statements.

Questions for Consultative Group members

Uncertainty
We ask Consultative Group members to provide information about the sources of uncertainty arising from the rate-adjustment mechanism and how such uncertainty is dealt with in practice, for both regulatory and financial reporting purposes, when recognising and measuring rate adjustments. This information will inform the Board's decisions about recognition, measurement and disclosure requirements for the model.

7. When gathering and reporting the information we are seeking, Consultative Group members may find it helpful to consider the following questions:

   (a) In your experience, when assessing whether a past transaction or event creates a temporary difference that will result in a rate adjustment:

      (i) What sources of uncertainty do you face in making your assessment?

      (ii) What evidence do you obtain to make your assessment?

   (b) How do you deal with uncertainty when the inclusion of a potential rate adjustment is subject to a cap, a floor, or a 'collar' (see paragraph 5(b))?

(c) How do you deal with uncertainty when the inclusion of a potential rate adjustment in amounts billed to customers is subject to demand risk?[1]

(d) If you currently (or previously) recognised regulatory assets (and regulatory liabilities) using local GAAP requirements or IFRS 14, what level of likelihood, if any, do you (did you) set as a threshold in determining whether to recognise regulatory assets or regulatory liabilities (eg probable, possible or other (please specify))?

[1] Demand risk means the risk that the amounts included in bills to customers will be higher or lower than the amount of the regulatory adjustment (regulatory asset or regulatory liability) recognised because customers buy a higher or lower quantity of goods or services than estimated in the rate calculation.