STAFF PAPER

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Project	Rate-regulated Activities	
Paper topic	Scope—Interaction with IFRIC 12	
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Objective

1. Many respondents to the Exposure Draft *Regulatory Assets and Regulatory Liabilities* (Exposure Draft) said that it is unclear how the proposals in the Exposure Draft interact with IFRIC 12 *Service Concession Arrangements.*[1]

2. To address respondents' concerns, the staff developed some examples that illustrate the interaction between the proposed model and IFRIC 12 and used them to discuss the interaction with different types of stakeholders in different jurisdictions.[2] This paper:

   (a) summarises feedback from these stakeholders;

   (b) analyses the feedback; and

   (c) recommends how the final Accounting Standard could clarify the interaction between the model and IFRIC 12.

Staff recommendations

3. We recommend the final Accounting Standard:

[1] Agenda Paper 9A discussed at the IASB meeting in October 2021 and Agenda Paper 9 discussed at the IASB meeting in December 2021.
[2] Agenda Paper 9A discussed at the February 2022 IASB meeting.

(a) clarifies the intended interaction between the model and IFRIC 12. That is, an entity would apply IFRIC 12 first and then, apply the requirements of the final Accounting Standard to any remaining rights and obligations to determine if the entity has regulatory assets or regulatory liabilities.

(b) includes examples to illustrate the interaction between the model and IFRIC 12.

Structure of the paper

4. This paper is structured as follows:

   (a) proposals in the Exposure Draft (paragraph 6);

   (b) summary of comments received during the comment period (paragraphs 7–10);

   (c) development of examples (paragraphs 11–20);

   (d) feedback received on the examples developed (paragraphs 21–37);

   (e) staff analysis (paragraphs 38–53); and

   (f) conclusions (paragraphs 54–57).

5. Appendix A describes the stakeholders we spoke to. Appendix B includes the examples we discussed with those stakeholders.

Proposals in the Exposure Draft

6. Paragraph B47 of the Exposure Draft states that:

> IFRIC 12 applies to a public-to-private service concession arrangement if the grantor controls or regulates the price at which the operator must provide services, and if other specified conditions are met. Accordingly, some arrangements within the scope of IFRIC 12 may create regulatory assets or regulatory liabilities within the scope of this [draft] Standard. An entity shall account for those regulatory assets or regulatory liabilities

separately from the assets and liabilities within the scope of IFRIC 12.

Summary of comments received during the comment period

7. Most respondents who commented on the proposed guidance agreed that service concession arrangements can create regulatory assets and regulatory liabilities. An accounting firm suggested the IASB carry out more outreach to understand how often service concession arrangements create regulatory assets and regulatory liabilities.

8. Many respondents who commented said that the proposed guidance is insufficient and suggested the IASB provide detailed guidance and illustrative examples on how an entity would account for regulatory assets and regulatory liabilities in all three financial reporting models in IFRIC 12—the financial asset model, the intangible asset model, and the hybrid model. Supporting the need for detailed guidance:
   (a) almost all respondents from Latin America said that service concession arrangements are common in the utility sector; and
   (b) an accountancy body from Asia-Oceania said that an intangible asset recognised by applying IFRIC 12 and a regulatory asset are similar in nature.

9. In developing the guidance and the illustrative examples, some respondents suggested the IASB consider the diverse features of service concession arrangements, such as arrangements in which:
   (a) the grantor is the customer for some services and the general public are customers for other services (see Examples 1–4 in Appendix B);
   (b) the grantor contractually guarantees to pay the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts (see Example 2 in Appendix B);
   (c) the operator has a right to reset the rates charged to customers after a specified period based on costs incurred during that specified period (see Examples 1–3 in Appendix B);
   (d) the operator has a right to increase rates charged to customers at regular intervals during the concession period, but the grantor extends the concession

period instead of allowing the operator to increase the rates (see Example 4 in Appendix B); and

(e) a government body is typically both the grantor and the sole customer (paragraph 17).

10. A European national standard-setter suggested the IASB specify that:

(a) regulatory assets and regulatory liabilities do not arise in a service concession arrangement accounted for applying the financial asset model; and

(b) regulatory assets and regulatory liabilities arise only during the operating phase of a service concession arrangement accounted for applying the intangible asset model.

Development of examples

11. As mentioned in paragraphs 7–10, many respondents said the guidance on the interaction between the model and IFRIC 12 was insufficient and suggested the IASB developed examples illustrating that interaction.

12. To address these concerns, we developed examples (see Appendix B) that we used to discuss the interaction between the model and IFRIC 12 with different types of stakeholders in different jurisdictions (see Appendix A). When developing these examples, we considered:

(a) our views on the interaction between the model and IFRIC 12 (paragraphs 13–15).

(b) feedback received during the comment period and our views on that feedback (paragraphs 16–20).

Our views on the interaction between the model and IFRIC 12

13. The Exposure Draft says that some service concession arrangements within the scope of IFRIC 12 may create regulatory assets or regulatory liabilities (paragraph B47 of the Exposure Draft). When this is the case, an entity should account for those regulatory assets or regulatory liabilities separately from the assets and liabilities within the scope of IFRIC 12.

14. In developing the proposals in the Exposure Draft, the IASB intended the information provided by the model to supplement the information entities provide by applying other IFRS Accounting Standards (paragraph BC30 of the Basis for Conclusions on the Exposure Draft). In practical terms, this means that an entity would apply IFRIC 12 first and then apply the requirements of the final Standard to any remaining rights and obligations to determine if the entity has regulatory assets or regulatory liabilities.

15. However, stakeholders said the Exposure Draft included insufficient guidance to illustrate how the model would interact with IFRIC 12. Because of this, we developed examples that are consistent with an entity applying IFRIC 12 first and then the proposals in the Exposure Draft to any remaining rights and obligations.

Feedback received during the comment period and our views on that feedback

16. In response to the feedback on the Exposure Draft, we developed four examples that illustrate the interaction between the model and IFRIC 12. In all four examples, the entity applies the intangible asset model in IFRIC 12. During the operating phase:

    (a) the entity has a right to recover higher input costs incurred in a period in the regulated rates to be charged to customers in future periods—Example 1;

    (b) the entity has a right to recover higher input costs incurred in a period in the regulated rates to be charged to customers in future period, but the grantor guarantees to pay any shortfalls between the higher input costs incurred and the amounts recovered from the customers—Example 2;

    (c) the entity has a right to recover higher input costs incurred in a period in the regulated rates to be charged to customers during an extended period of the service concession arrangement—Example 3; and

    (d) the entity incurred higher input costs in a period, the service concession period is extended but the entity has no right to recover the higher input costs incurred in the regulated rates to be charged to customers in the extended period—Example 4.

17. The examples cover all of the features of arrangements suggested by respondents to the Exposure Draft (paragraph 9), with the exception of the feature in paragraph

9(e)—that is, arrangements in which a government body is both the grantor and the sole customer. We do not think arrangements of this type are very common—only one accounting firm suggested that we illustrate arrangements of this type and none of the stakeholders that we spoke to when discussing the examples suggested that we should illustrate arrangements of this type. Consequently, we think it is unnecessary to include an example of this type of arrangement in the final Standard.

18. The examples we developed deal with regulatory assets arising during the operating phase of the arrangements only. This is because we do not expect regulatory assets or regulatory liabilities to arise during the construction phase of service concession arrangements, regardless of whether they are accounted for by applying the intangible asset or the financial asset model in IFRIC 12. This is because IFRIC 12 requires that the consideration received or receivable by the operator for construction services be accounted for as either a financial asset or an intangible asset. Consequently, these requirements would prevent part of the consideration for construction services being accounted for as a regulatory asset.

19. In addition, the examples we developed deal with arrangements accounted for applying the intangible asset model in IFRIC 12. This is because we do not expect arrangements accounted for using the financial asset model to give rise to regulatory assets or regulatory liabilities if the total expected consideration forms part of the financial asset initially recognised—that is, if the total expected consideration includes both the construction services and the operation services. This is because any changes to an entity's rights to future cash flows would be captured as part of the measurement of the financial asset. We think situations in which the total expected consideration includes both the construction services and the operation services are likely to be the most common. In other situations, an entity would need to consider the contractual terms of its arrangement and assess whether these terms would create regulatory assets or regulatory liabilities during the operating phase of the arrangement. However, we think the examples developed are sufficient for entities to make these assessments.

20. We did not think it is necessary to develop an example of a service concession arrangement accounted for applying the hybrid model in IFRIC 12. None of the stakeholders that we spoke to said that we should consider developing an example of

a service concession arrangement accounted for applying the hybrid model (paragraphs 21–37).

Feedback received on the examples developed

21. The stakeholders we spoke to generally welcomed the examples developed by the staff. Most stakeholders said the examples are helpful in clarifying the interaction between the model and IFRIC 12. In particular, they said the examples help clarify that the proposed model supplements the information an entity already provides by applying IFRS Accounting Standards. These stakeholders also suggested some improvements to the examples to better reflect their current service concession arrangements (paragraphs 23–24).

22. We have summarised the feedback as follows:

    (a) right to increase future regulated rates to recover costs incurred because of unusual events (paragraphs 23–24);

    (b) guaranteed shortfalls arising during the operating phase of the service concession arrangement (paragraphs 25–28);

    (c) extension of the service concession arrangement period (paragraphs 29–33);

    (d) usefulness of the examples developed and completeness (paragraphs 34–36); and

    (e) other matters raised (paragraph 37).

Right to increase future regulated rates to recover costs incurred because of unusual events

23. Examples 1 and 3 in Appendix B illustrate situations in which an entity has the right to increase future regulated rates to recover costs incurred because of unusual events. Some stakeholders suggested we should amend these examples to illustrate a situation when, from the inception of the arrangement, the regulated rate is determined so that an entity is entitled to recover actual costs incurred in supplying goods or services to customers during the operating phase. In such an example, the entity would be allowed to adjust differences between estimated and actual costs incurred during the operation of the arrangement in future regulated rates.

24. According to these stakeholders, this suggestion would:

    (a) avoid the need for entities to first assess the implications of a contract modification in IFRS 15 *Revenue from Contracts with Customers*. According to these stakeholders the contract modification requirements in IFRS 15 would not prevent the entity from accounting for a regulatory asset in Examples 1 and 3. However, the current drafting of these examples would require entities to make this assessment, which may add unnecessary complexity to the fact patterns.

    (b) reflect better the features of service concession arrangements that are common in Latin America.

Guaranteed shortfalls arising during the operating phase of the arrangement

25. Example 2 in Appendix B assumes that:

    (a) an entity incurred higher input costs due to an unusual event during the operating phase of the arrangement. The arrangement includes a clause that guarantees that the entity will be able to recover costs related to unusual events.

    (b) upon the occurrence of the unusual event, the grantor:

        (i) agreed to allow the entity to recover the higher input costs by increasing the regulated rates to be charged to customers in future periods; and

        (ii) guaranteed to reimburse any outstanding amounts that the entity does not recover from customers relating to the higher input costs incurred.

26. The analysis of that fact pattern included two possible views:

    (a) View 1, the entity recognises the higher input costs as a financial asset.

    (b) View 2, the entity recognises two assets:

        (i) a regulatory asset—for the amounts the entity expects it will recover through the higher regulated rates to be charged to customers in future periods; and

(ii) a financial asset—for any shortfall between the higher input costs incurred and the amounts the entity expects to recover through the higher regulated rates charged to customers.

27. Many stakeholders supported View 1. The main reasons provided were:

(a) the proposed model supplements the information that an entity already provides applying IFRS Accounting Standards. According to these stakeholders the unconditional right to receive cash for any shortfalls between the higher input costs incurred and the amounts collected from customers means that the higher input costs meet the definition of a financial asset in IAS 32 *Financial Instruments: Presentation*. Consequently, for these stakeholders the fact pattern in Example 2 would not give rise to a regulatory asset in the scope of the final Standard.

(b) according to paragraph 16 of IFRIC 12, if an entity provides construction or upgrade services, the entity is required to recognise the consideration for those services as a financial asset when the grantor contractually guarantees to pay the shortfall between amounts received from users of the public service and specified or determinable amounts. These stakeholders do not think there is a difference between guaranteed shortfalls arising from construction or upgrades services and guaranteed shortfalls arising during the operation of an arrangement that would warrant a different treatment for the latter.

(c) the guarantee from the grantor removes demand risk from the entity. This is a key difference from situations when the recovery of input costs is not guaranteed as it is the case in Example 1 in Appendix B.

(d) View 1 is simpler and more pragmatic than View 2. A stakeholder said View 2 is more complex because it will require an entity to continuously assess whether amounts need to be reclassified from regulatory asset to financial asset or vice versa. These reclassifications will also affect presentation.

(e) credit risk—a stakeholder said balances due from a grantor (generally a government or public authority) are subject to lower credit risk than the balances due from customers. This stakeholder thought View 1 may better reflect the asset's credit risk than View 2—classifying part of the asset as a

regulatory asset could lead users of financial statements to incorrectly conclude that the regulatory asset has a higher credit risk than is in fact the case.

28. Some other stakeholders supported View 2. These stakeholders were predominantly preparers in the electricity and gas sectors in Brazil. The main reasons provided were that:

    (a) View 2 reflects better how the entity expects to recover the higher input costs. According to these stakeholders, amounts that are expected to be recovered from customers should be accounted for as a regulatory asset. Only amounts expected to be recovered from the grantor should be accounted for as a financial asset. According to these stakeholders under their current arrangements the amounts expected to be recovered from the grantor will be less than the amounts expected to be recovered from customers. Consequently, these stakeholders also think View 2 will result in more useful information for users because it will help them understand what part of the higher input costs will be recovered through regulated rates charged to customers (regulatory asset) and what part will be recovered from the grantor (financial asset).

    (b) View 2 is not necessarily more complex than View 1—a stakeholder said that changes in the expected future cash flows that the entity will receive from both customers and the grantor would only result in remeasurements of the regulatory asset and the financial asset which they to do not see as being complex.

    (c) a stakeholder noted that the effect on profit or loss of any financial asset recognised applying View 1 would not be reflected as revenue from contracts with customers but as another type of income. This is because the grantor is not a customer of the entity in respect of its operation services. As a result, in the statement of financial performance, the entity would present the effect of the financial asset, and subsequent changes in the financial asset, as income in a different line from that of revenue from contracts with customers. This stakeholder found this outcome to be counter-intuitive because in the case of a financial asset for construction services, the grantor is typically both the

entity's customer and the guarantor of any shortfalls and recognises the full amount as revenue.

(d) the grantor would recognise a financial liability for the amount that it expects to pay to the entity. In many cases this amount is expected to be a small part of the total amount of higher input costs. Consequently, applying View 1, the entity would recognise a financial asset that is larger than the grantor's financial liability. A stakeholder found this outcome counter-intuitive.

Extension of the service concession arrangement period

29. Example 3 in Appendix B assumes that:

(a) an entity incurred higher input costs due to an unusual event during the operating phase of the arrangement; and

(b) the grantor agreed to extend the concession period and to allow the entity to recover the higher input costs incurred by increasing the regulated rates charged to customers during the extended period.

30. The analysis of the fact pattern in this example concluded that the entity's right to include the higher input costs incurred in the regulated rates charged during the extended period gives rise to a regulatory asset.

31. Example 4 in Appendix B describes a similar fact pattern. However, in this case, during the extended period the regulated rates remain unchanged from those charged during the original arrangement period. Consequently, the entity might have an opportunity during the extended period to recover the higher input costs incurred but recovery is not certain. The analysis of the fact pattern in this example concluded that the extension of the arrangement period does not give the entity a right to recover the higher input costs incurred. Consequently, the entity does not have a regulatory asset as a result of the extension of the arrangement period.

32. Most of the stakeholders agreed with the analysis in Example 3—that is, that the right to recover the higher input costs incurred by adding them in the regulated rates to be charged to customers during the extended period gives rise to a regulatory asset. They also agreed with the analysis in Example 4—that is, that the extension of the arrangement period would not give the entity a right to recover the higher input costs

incurred by adding them in the future regulated rates. This is because the regulated rates to be charged during the extended period of the arrangement would remain unchanged.

33. Many stakeholders said the fact patterns involving an extension of the arrangement period are not very common in their sectors. When referring to Example 3, a stakeholder said it is unusual for the grantor to extend the service concession period and at the same time allow the entity to increase the rates. That stakeholder said typically a new operator or the grantor would compensate the entity for higher costs incurred at the end of the service concession period.

Usefulness of the examples developed and completeness

34. Most stakeholders said including in the final Standard examples similar to those in Appendix B would help illustrate the interaction between the model and IFRIC 12 and would help address the concerns raised by stakeholders (paragraphs 7–10).

35. A few stakeholders said the examples are useful in confirming that the final Standard would supplement information already provided by an entity applying IFRS Accounting Standards. This means entities need to apply all other IFRS Accounting Standards first and then assess whether their regulatory agreements give rise to regulatory assets and regulatory liabilities.

36. We also asked stakeholders whether they were aware of any other fact patterns that we should consider including in the final Standard. Apart from the modification suggested to Examples 1 and 3 described in paragraph 23, none of the stakeholders identified any other fact patterns.

Other matters

37. We also spoke to preparers with service concession arrangements in the water management and motorway sectors in Europe. These stakeholders said that the way in which the regulated rates are determined do not give rise to differences in timing. Consequently, according to these stakeholders, their arrangements do not give rise to regulatory assets and regulatory liabilities.

Staff analysis

38. This section analyses the extent to which the examples help mitigate the concerns raised about the proposals (paragraph 40) and the extent to which stakeholders agreed with the analysis included on the examples developed (paragraphs 41–43).

39. This section also describes and analyses the main concern raised by stakeholders on the examples developed (paragraphs 45–53).

Feedback suggests the examples help mitigate the concerns about the proposals and reflects stakeholders' support for the analysis included in the examples

40. The outreach suggests that the examples helped stakeholders to understand how the model interacts with IFRIC 12 (paragraphs 8 and 9). In particular, some stakeholders said the examples clarify the fact that an entity would apply IFRIC 12 first and would then assess whether their regulatory agreements give rise to regulatory assets and/or regulatory liabilities.

41. Stakeholders generally agreed with the analysis included in the examples. In particular, many stakeholders said that they found Examples 1 and 2 useful. Consequently, we think we should include illustrative examples similar to Examples 1 and 2 in the final Standard.

42. The examples also helped clarify that an extension of the service concession period would not necessarily give rise to a regulatory asset (paragraph 9(d) and Example 4). For a regulatory asset to arise, the entity would need to have an enforceable right to recover higher costs incurred in a previous period by including them in the regulated rates to be charged to customers during the extended period (Example 3). Having said that, because many of the stakeholders to whom we spoke said it was not common for arrangements to be extended, we do not think it is necessary for the final Standard to include examples similar to Examples 3 and 4.

43. In addition, none of the stakeholders to whom we spoke said that they would have expected examples to show:

    (a) regulatory assets or regulatory liabilities arising during the construction phase (paragraphs 10(b) and 18). A few of these stakeholders said that, because

regulatory assets or regulatory liabilities are expected to arise during the operating phase of an arrangement, the most frequent interaction between the model and IFRS Accounting Standards will be with IFRS 15 or IFRS 9 *Financial Instruments* rather than with IFRIC 12 (Examples 1–4); or

(b) regulatory assets and regulatory liabilities to arise in an arrangement accounted for applying the financial asset model (paragraphs 10(a) and 19).

44. However, we think it may be help preparers in applying the final Standard and help to address the stakeholder's comments in paragraph 10, if the IASB adds examples to the final Standard showing that:

(a) regulatory assets and regulatory liabilities do not typically arise in a service concession arrangement accounted for applying the financial asset model; and

(b) regulatory assets and regulatory liabilities typically arise only during the operating phase of a service concession arrangement accounted for applying the intangible asset model.

Main concern raised by stakeholders

45. As discussed in paragraph 28, some stakeholders—mainly preparers in the electricity and gas sectors in Brazil—disagreed with View 1 in Example 2 (that is, that the right to recover the higher than expected input costs could give rise to a financial asset). These stakeholders noted that the fact pattern in Example 2 is similar to their current arrangements. These stakeholders currently account for the right to recover the higher than expected input costs as a financial asset. However, they think it would be more appropriate to account for the right to recover the higher than expected input costs as a regulatory asset for the amount they expect to recover through regulated rates and as financial asset for the amount they expect to recover through the guarantee (that is, View 2 in that example). The main reason for their view is that entities will recover most of the higher input costs through regulated rates charged to customers, with only a small part expected to be recovered from the grantor through the guarantee (see paragraph 28).

46. We think the final Standard should clarify whether the fact pattern in Example 2 would give rise to a financial asset or to both a regulatory asset and a financial asset.

This could be done by including a similar example in the final Standard. Paragraphs 47–53 provide our analysis of how the arrangement described in Example 2 should be accounted for once the final Standard has been issued.

47. The supplementary nature of the model means that an entity would first apply other IFRS Accounting Standards and then the requirements in the final Standard.

48. Applying paragraph 11(c) of IAS 32, the entity will have a financial asset if the entity has a contractual right to receive cash or another financial asset from another entity for the higher input costs incurred. We think the entity's contractual right to recover the higher than expected input costs meets the definition of a financial asset in IAS 32 because:

    (a) the guarantee means that the entity has a contractual right to receive cash from the grantor for any outstanding amount relating to the increases in the regulated rates so that it *fully* recovers the higher input costs incurred. In the extreme case that the entity collected nothing from regulated rates charged to customers, the entity would have a contractual right to receive cash from the grantor amounting to the entire amount of the higher input costs incurred. Consequently, the guarantee means that the entity has a present, contractual right to recover the higher input costs incurred from or at the direction of the grantor without bearing demand risk. It is the grantor that bears the risk that the cash flows collected from customers will not be sufficient to recover the higher input costs due to a fall in demand;

    (b) the fact that the amount may come from customers and/or the grantor does not alter the entity's contractual right to *fully* recover the higher input costs incurred; and

    (c) the right is enforceable—paragraph 13 of IAS 32 clarifies that 'contractual' refers to 'an agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable by law.'

49. In addition, we think the fact pattern described in Example 2 can be analogised to situations when, in the context of construction services, an entity has a guarantee from the grantor to receive cash for the shortfall between amounts received from users of

the public services and specified or determinable amounts. In that situation, paragraph 16 of IFRIC 12 requires an entity to recognise a financial asset. Paragraph 16 of IFRIC 12 says:

> The operator shall recognise a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services; the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law. The operator has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator (a) specified or determinable amounts or (b) the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts, even if payment is contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements.

50. Paragraph BC42 of the Basis for Conclusions on IFRIC 12 says that 'the IFRIC noted that the operator has an unconditional right to receive cash to the extent that the grantor bears the risk (demand risk) that the cash flow generated by the users of the public service will not be sufficient to recover the operator's investment.'

51. We have not identified any matters that would indicate that the guaranteed shortfalls for operation services in Example 2 are significantly different to the guaranteed shortfalls for construction services such that the former would warrant a different accounting treatment from that in paragraph 16 in IFRIC 12.

52. We think a key difference between the regulatory asset arising in Example 1 and the regulatory asset arising in View 2 of Example 2 is that the regulatory asset in View 2 would not be subject to demand risk. Even though demand risk is not a necessary condition for a regulatory asset to exist, we think demand risk is a common feature of regulatory assets. The level of demand risk to which regulatory assets are subject may vary, however, we would expect regulatory assets to normally be subject to a degree

of demand risk.[3] The guarantee given by the grantor in Example 2 eliminates demand risk for the entity. Consequently, we think that recognising a financial asset rather than a regulatory asset better reflects the economics of the entity's right.

53. We therefore think that the entity in Example 2 should account for its contractual right to recover the higher than expected input costs as a financial asset applying IFRS 9. We think the final Standard could include an illustrative example to clarify this point.

Question for the IASB
1. Does the IASB have any questions or comments on the staff analysis in paragraphs 38–53?

Conclusions

54. The feedback received (paragraphs 21–37) suggests that the final Standard should clarify the intended interaction between the model and IFRIC 12. That is, an entity would need to apply IFRIC 12 first and then, apply the requirements of the final Standard to any remaining rights and obligations to determine if the entity has regulatory assets or regulatory liabilities.

55. We think the final Standard should include examples illustrating the interaction between the final Standard and IFRIC 12, such as:

    (a) examples similar to Examples 1 and 2 included in Appendix B; and

    (b) examples dealing with circumstances that are not expected to give rise to regulatory assets and regulatory liabilities (paragraph 44).[4]

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[3] We have learned that, in some cases, regulators allow entities to pass demand risk to their customers when they have not been able to recover their allowed revenue due to a fall in demand. This is however different from allowing entities to pass demand risk to customers on all of their regulatory assets. We understand the latter would be less common.

[4] These examples could be added to the set of examples in Illustrative Example 7C accompanying the Exposure Draft.

56. We think Example 2 in appendix B should illustrate View 1—that is that the arrangement gives rise to a financial asset (see paragraphs 45–53).

57. For the reasons explained in paragraph 42, we think it is unnecessary to include in the final Standard examples similar to Examples 3 and 4 in Appendix B.

Questions for the IASB
2. Does the IASB agree: a. that the final Accounting Standard clarifies the intended interaction between the model and IFRIC 12. That is, an entity would apply IFRIC 12 first and then, apply the requirements of the final Accounting Standard to any remaining rights and obligations to determine if the entity has regulatory assets or regulatory liabilities (paragraph 54). b. that the final Accounting Standard includes examples to illustrate the interaction between the model and IFRIC 12 as described in paragraphs 55–57?

APPENDIX A— Stakeholders with whom the staff spoke

A1. The table below provides details of the stakeholders that the staff spoke to about the interaction between the model and IFRIC 12 and/or the examples in Appendix B.

Stakeholder type	Industry	Jurisdiction
Preparer	Water management	Europe
Preparer	Motorway concessions	Europe, North America, Latin America, Asia-Oceania
Preparer	Electricity	Europe and Latin America
Preparer	Motorway concessions	Europe, North America, Latin America
Preparer / Representative body	Gas	Latin America
Preparer / Representative body	Electricity	Latin America
Accounting firms (3)	Accountancy	Global
National standard-setters	Accountancy	Latin America
Accountancy body	Accountancy	Asia-Oceania

APPENDIX B—Examples discussed

IE1. Entity A (the entity) enters into a 10-year service concession arrangement with a grantor to construct a plant in Years 1–2 and use the plant to supply goods or services to customers from Years 3–10 (operational phase). In exchange for constructing the plant, the grantor gives Entity A an intangible asset, that is a right to charge customers for goods or services supplied using the plant.

IE2. The service concession arrangement entitles Entity A to charge regulated rates that are determined so that the entity can recover costs and obtain a specified return but neither the recovery of costs nor profitability is guaranteed. The grantor or Entity A can call for a review of the regulated rates if unusual events (as defined by the service concession arrangement) take place.

IE3. The terms of the service concession arrangement described above apply to all examples 1 to 4.

No	Example	Analysis
1	In Year 4, due to an unusual event (such as extreme weather conditions, for example, droughts affecting the electricity costs) Entity A incurred higher input costs. At the end of Year 4, the grantor and Entity A agreed to amend the service concession arrangement to entitle Entity A to recover the higher input costs incurred in Year 4 by increasing the regulated rates to be charged to customers in Years 5 and 6.	The amendment to the service concession arrangement allows Entity A to recover the higher input costs that it incurred in Year 4. The higher input costs incurred in Year 4 form part of the total allowed compensation for goods or services supplied in that year that will be included in revenue in Years 5 and 6.

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No	Example	Analysis
		Applying IFRS X *Regulatory Assets and Regulatory Liabilities*, Entity A recognises as a regulatory asset its right to add the higher input costs incurred in Year 4 in determining the regulated rates to be charged to customers in Years 5 and 6.
2	Assume the same facts as in example 1. However, in this case the service concession arrangement includes a guarantee clause. This clause is not a guarantee of the compensation for the construction services provided at the start of the service concession arrangement rather the guarantee is limited to any compensation for unusual events. Under this clause, the grantor will reimburse Entity A at the end of the service concession arrangement for any outstanding amount relating to any increases in the regulated rates charged approved by the grantor as a result of unusual events. At the end of Year 4, the grantor and Entity A agreed the extreme weather conditions causing higher input costs were an unusual event. The grantor agreed to: (a) allow Entity A to recover the higher input costs incurred in Year 4 by increasing the regulated rates to be charged to customers in Years 5 and 6; and	**View 1** The guarantee clause in the service concession arrangement means that, Entity A has a contractual right to receive cash for any outstanding amount relating to the increases in the regulated rates charged in Years 5 and 6 at the end of the service concession arrangement so that it fully recovers the higher input costs it incurred in Year 4. Entity A recognises the higher input costs in Year 4 as a financial asset. Even in the case the higher input costs in Year 4 are fully paid by customers through the increased regulated rates charged in Years 5 and 6, Entity A has a present, unconditional contractual right to receive the higher input costs incurred in Year 4 from or at the direction of the grantor. The method of payment is a matter

No	Example	Analysis
	(b) reimburse Entity A for any outstanding amount relating to the increases in the regulated rates charged in Years 5 and 6 related to the higher input costs incurred in Year 4 at the end of the service concession arrangement.	of form only. This view is consistent with the accounting required in paragraph 16 of IFRIC 12. **View 2** The guarantee clause means that Entity A has a contractual right to receive cash for any outstanding amount relating to the adjustments to the regulated rates charged in Years 5 and 6 at the end of the service concession arrangement so that it fully recovers the higher input costs it incurred in Year 4. The entity expects that most of the higher input costs incurred in Year 4 will be recovered from regulated rates to be charged to customers in Years 5 and 6. The entity recognises two assets: (a) a regulatory asset—applying IFRS X *Regulatory Assets and Regulatory Liabilities*, the entity recognises as a regulatory asset the amounts it expects it will recover through the higher regulated rates charged to customers in Years 5 and 6; and (b) a financial asset—applying IFRS 9 *Financial Instruments*, the entity recognises a financial asset for the guarantee relating to any shortfalls between the higher input costs incurred in Year 4 and the amounts the entity expects to

No	Example	Analysis
		recover through the higher regulated rates charged to customers in Years 5 and 6—that is, a financial asset for the guarantee given by the grantor to pay the operator any amounts outstanding relating to the increases in the regulated rates charged in Years 5 and 6 at the end of the service concession arrangement.
3	In Year 8, due to an unusual event (such as extreme weather conditions, for example, droughts affecting the electricity costs) Entity A incurred higher input costs. At the end of Year 8, the grantor and Entity A agreed to extend the service concession period by four years, that is Years 11–14. During the extended period, Entity A has the right to add the higher input costs incurred in Year 8 in determining the regulated rates to be charged to customers in Years 11–14.	The extension of the service concession period will allow Entity A to recover the higher input costs incurred in Year 8. The higher input costs incurred in Year 8 form part of the total allowed compensation for goods or services supplied in that year that will be included in revenue in Years 11–14. Applying IFRS X *Regulatory Assets and Regulatory Liabilities,* Entity A recognises as a regulatory asset its right to add the higher input costs in determining the regulated rates to be charged to customers in Years 11–14. Entity A will also need to assess whether the extension of the service concession period gives rise to other rights and obligations that Entity A may need to recognise in accordance with other IFRS Accounting Standards.

No	Example	Analysis
4	In Year 8, due to an unusual event (such as extreme weather conditions, for example, droughts affecting the electricity costs) Entity A incurred higher input costs. At the end of Year 8, the grantor and Entity A agreed to extend the service concession period by four years, that is Years 11–14. During the extended period, the regulated rates to be charged to customers would remain at the same level as those charged in Year 10. Consequently, Entity A might have an opportunity to recover the higher input costs incurred in Year 8 during the extended period but this is not certain.	The extension of the service concession period does not give Entity A a right to add an amount in the regulated rates to be charged to customers in Years 11–14 to recover the higher input costs incurred in Year 8. Consequently, applying IFRS X *Regulatory Assets and Regulatory Liabilities,* Entity A does not have a regulatory asset in Year 8 as a result of the extension of the service concession arrangement. Entity A will also need to assess whether the extension of the service concession period gives rise to other rights and obligations that Entity A may need to recognise in accordance with other IFRS Accounting Standards.