
IASB[®] Meeting

Date **February 2024**
Project **Rate-regulated Activities**
Topic **Boundary of a regulatory agreement**
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Objective

1. This paper sets out staff analysis and recommendations on how the final Accounting Standard could articulate the guidance on the boundary of a regulatory agreement, acknowledging the possibility of both finite and indefinite rights to supply goods or services (rights to operate).

Staff recommendations

2. The staff recommend that the final Accounting Standard:
 - (a) acknowledge that rights to operate may be indefinite—paragraph 30;
 - (b) require that an entity that has an enforceable right to operate include all the unrecovered (unfulfilled) cash flows in the measurement of the regulatory asset (regulatory liability) if the entity has:
 - (i) an enforceable right to recover (obligation to fulfil) all or substantially all of the regulatory asset (regulatory liability) by adding amounts to (deducting amounts from) future regulated rates charged over its life; or
 - (ii) an enforceable right, on termination of the agreement, to receive (obligation to pay) compensation for all or substantially all of the

unrecovered regulatory asset (unfulfilled regulatory liability)—
paragraph 50; and

- (c) in cases where an entity has an enforceable right to operate but does not meet the conditions described in (b)(i) or (b)(ii), require that the entity determine the set of unrecovered (unfulfilled) cash flows for which its legislative or regulatory frameworks provide sufficient assurance for recovery (fulfilment) and include those cash flows in the measurement of a regulatory asset (regulatory liability)—paragraph 58.

Structure of the paper

- 3. This paper is structured as follows:
 - (a) background (paragraphs 6–9);
 - (b) proposals in the Exposure Draft [*Regulatory Assets and Regulatory Liabilities*](#) (Exposure Draft) (paragraphs 10–17);
 - (c) feedback on the Exposure Draft (paragraphs 18–20); and
 - (d) staff analysis (paragraphs 21–62).
- 4. The paper includes an appendix that summarises feedback from recent outreach with preparers regarding the determination of the boundary in their particular cases.
- 5. The recommendations in this paper refer to both regulatory assets and regulatory liabilities but, for simplicity, the analysis focuses on regulatory assets—the same concepts would be applicable to regulatory liabilities.

Background

6. At its October 2023 meeting, the IASB redeliberated the proposals in the Exposure Draft relating to the boundary of a regulatory agreement.¹ The IASB tentatively decided that the final Accounting Standard would:
- (a) retain the proposed guidance in the Exposure Draft on rights to renew or cancel a regulatory agreement. The IASB would clarify in the prospective Accounting Standard that those rights might be explicit or implicit.
 - (b) retain the proposed guidance in the Exposure Draft on compensation for cancellation of a regulatory agreement. The IASB would clarify in the prospective Accounting Standard that the guidance also applies to other circumstances in which termination occurs.²
 - (c) include the principles in paragraph 35(c) of IFRS 15 *Revenue from Contracts with Customers* that relate to an entity's right to payment for performance completed to date. An entity would use those principles to help it assess whether there exists an enforceable present right to receive, or an enforceable present obligation to pay, compensation on termination of a regulatory agreement for an amount comprising unrecovered regulatory assets and unfulfilled regulatory liabilities.
 - (d) retain the proposed requirements in the Exposure Draft on reassessment of and changes to the boundary of a regulatory agreement.³
7. The IASB also tentatively decided not to add more guidance on how an entity assesses its practical ability to renew, and other parties' practical ability to cancel, a regulatory agreement.
8. The last section of [Agenda Paper 9B](#) discussed by the IASB in October 2023 identified two options for clarifying how an entity determines the boundary when it

¹ [Agenda Paper 9B](#) discussed at the October 2023 IASB meeting.

² This paper refers to 'compensation on cancellation' when referring to the Exposure Draft proposals and 'compensation on termination' elsewhere.

³ [IASB Update](#) October 2023.

has enforceable rights to compensation on termination, and the entity or another party has enforceable rights to renew or to cancel the agreement.

9. IASB members did not form a view on the potential clarification at that meeting and the staff suggested continuing the discussion at a future meeting. This paper continues that discussion, taking account of recent feedback from outreach summarised in the appendix to this paper.

Proposals in the Exposure Draft

10. This section is structured as follows:
- (a) enforceable present right (obligation) to recover (fulfil) a regulatory asset (regulatory liability) by increasing (decreasing) future regulated rates—(paragraphs 11–14); and
 - (b) enforceable right to receive (obligation to pay) compensation on cancellation of the regulatory agreement—(paragraphs 15–17).

Enforceable present right (obligation) to recover (fulfil) a regulatory asset (regulatory liability) through future regulated rates

11. The Exposure Draft proposes that when measuring a regulatory asset or a regulatory liability an entity includes all future estimated cash flows arising from the regulatory asset or regulatory liability that are within the boundary of a regulatory agreement.⁴
12. It describes the boundary of a regulatory agreement as the latest future date at which an entity has:
- (a) an enforceable present right to recover a regulatory asset by increasing the regulated rate to be charged to customers; or

⁴ Paragraphs 31–34 of the Exposure Draft.

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- (b) an enforceable present obligation to fulfil a regulatory liability by decreasing the regulated rate to be charged to customers.⁵
13. Paragraph B30 of the Exposure Draft sets out the two conditions that are necessary for an entity to have **an enforceable present right to increase future regulated rates (emphasis added)**:
- B30 An entity's **present right to increase the regulated rate** at a future date is **enforceable** only if:
- (a) the regulatory agreement gives the entity the **present right to supply goods or services at that future date**; and
 - (b) no party apart from the entity has a right to cancel the regulatory agreement before that date **without arranging compensation for the entity to recover** its regulatory asset.
14. Paragraph B31 of the Exposure Draft explains how rights of renewal can extend the period over which an entity has an enforceable present right to add an amount to future regulated rates (**emphasis added**):
- B31 Sometimes an entity has an enforceable right to renew a regulatory agreement. Such a right can give the entity a **present right to supply goods or services at a future date** covered by that renewal if no other party has an enforceable right to prevent the renewal **without arranging compensation for the entity to recover** its regulatory asset.

Enforceable right to receive (obligation to pay) compensation on cancellation

15. When developing the proposals in the Exposure Draft the IASB discussed enforceable make-whole mechanisms on cancellation of a regulatory agreement. The staff's description of make-whole mechanisms was as follows (**emphasis added**):

⁵ Paragraph B28 of the Exposure Draft.

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- (a) make-whole mechanisms are designed to ensure that, if an entity ceases to supply the regulated goods or services, it will be compensated for any amounts it has been unable to add to the regulated rates charged (ie the outstanding amounts of what would be regulatory assets if the regulatory agreement had continued).
- (b) enforceable make-whole mechanisms **do not create a right to add an amount** to the future regulated rate(s) charged to customers. Instead, they create a **right to receive payment** for amounts not yet added to the regulated rate(s) when the agreement is terminated. That right would not itself meet the definition of a regulatory asset because it would be recovered by receiving compensation, not by adding an amount to future regulated rates.
- (c) provided the make-whole mechanism is adequate, an entity would be **economically indifferent** between recovering a regulatory asset through future regulated rates charged to customers or through compensation on termination of the regulatory agreement. In effect, an enforceable make-whole mechanism means that the **boundary of the regulatory agreement is not constrained by the duration of an entity's right to operate**.
- (d) it would be unusual for there to be a material difference between the cash flows arising from a make-whole mechanism and the cash flows from the continuation of the regulatory agreement and corresponding adjustments to the rate(s) charged to customers.⁶
16. The Exposure Draft addresses make-whole mechanisms in the section dealing with compensation on cancellation. Paragraphs B35–B38 of the Exposure Draft outline:
- (a) when cash flows from compensation are cash flows within the boundary of the regulatory agreement (paragraph B36—shown below);

B36 To the extent that the amounts of receipts or payments of such compensation depend solely on the monetary amount of

⁶ July 2019 [Agenda Paper 9B](#) and September 2019 [Agenda Paper 9A](#).

unrecovered regulatory assets or unfulfilled regulatory liabilities, they are cash flows within the boundary of the regulatory agreement.

- (b) how to deal with differences between unrecovered regulatory assets (unfulfilled regulatory liabilities) and the amount of compensation when measuring regulatory assets (regulatory liabilities) (paragraph B37); and
 - (c) when to derecognise a regulatory asset (regulatory liability) and recognise a financial asset (financial liability) when cancellation has been exercised (paragraph B38).
17. Paragraphs BC151 and BC152 of the Basis for Conclusions accompanying the Exposure Draft explain the rationale for including cash flows from make-whole mechanisms in the boundary of the regulatory agreement (**emphasis added**).

BC151 The presence within a cancellation right of a requirement to provide compensation, discussed in paragraphs B35–B38 of the Exposure Draft, results in uncertainty about how an entity will recover a regulatory asset—by increasing future regulated rates, or by receiving such compensation. As long as this uncertainty persists, it could be argued that the entity has both a regulatory asset and a financial asset, each recovered in different scenarios. Nevertheless, the Board considers that accounting for those two assets separately would not provide users of financial statements with useful information and would cause needless complexity for both users and preparers. Moreover, the right to receive compensation does not exist in isolation. It exists only to protect an entity's right to recover part of the total allowed compensation for goods or services already supplied to customers. Similar considerations apply to an entity's obligation to pay compensation if a regulatory agreement is cancelled before the entity fulfils a regulatory liability.

BC152 For the reasons given in paragraph BC151, the Exposure Draft proposes that cash flows arising from a right to receive compensation for unrecovered regulatory assets or an obligation to pay compensation for unfulfilled regulatory liabilities **be regarded as arising within the boundary of the regulatory agreement**, and thus be **included in the measurement** of the related regulatory assets or regulatory liabilities.

Feedback on the Exposure Draft

18. [Agenda Paper 9B](#) in October 2023 included a comprehensive analysis of feedback on the boundary proposals in the Exposure Draft. This paper repeats the feedback that relates to the matters being considered at this meeting.
19. A few respondents sought confirmation that the boundary of a regulatory agreement would not be limited to the regulatory period or the licence period. These respondents:
- (a) stressed the importance of considering the combined effect of rights to renew and rights to compensation. They stated that regulatory agreements (particularly those with continually renewing or perpetual licences) cannot be cancelled without the entity receiving compensation. According to these respondents, that right to compensation gives an entity assurance that it will recover long-lived regulatory assets.
 - (b) said that their regulatory agreements do not have renewal or cancellation rights, or do not include explicit compensation mechanisms for non-renewal. Consequently, these respondents also queried how entitlements to, or valid expectations of, compensation for unrecovered (unfulfilled) long-term regulatory assets (regulatory liabilities) affect boundary assessments.⁷
20. A few respondents wanted to know whether, in determining which cash flows fall within the boundary, an entity should consider valid expectations that a licence will be renewed or the possibility that a licence will be cancelled.⁸

⁷ Paragraph 22 of [Agenda Paper 9B](#), October 2023.

⁸ Paragraph 24(b) of [Agenda Paper 9B](#), October 2023.

Staff analysis

21. The Exposure Draft proposes that:
- (a) the boundary of a regulatory agreement is the latest future date at which an entity has an enforceable present right to recover a regulatory asset by **increasing the regulated rate** (that is, *a right to add an amount*) to be charged to customers.
 - (b) the cash flows arising from a **right to compensation** on cancellation for unrecovered regulatory assets are cash flows **within the boundary** of a regulatory agreement.
22. Paragraph B30 of the Exposure Draft proposes that the **enforceability** of an entity's **right to add an amount** to future regulated rates so that it recovers a regulatory asset depends on the entity having:
- (a) **a right to operate** the regulated activities and supply the regulated goods or services in the future (paragraph 13). That right to operate is often set out in a licence or a service concession arrangement; and
 - (b) **a right to recover** the regulatory asset.
23. The Exposure Draft proposals contemplate an entity having a right to operate for a defined period or periods of time, being the initial period agreed, along with any extensions to that period via rights to renew.⁹ The IASB has already made tentative decisions dealing with rights to renew or cancel a regulatory agreement in October 2023 (paragraph 6). The recent feedback from outreach does not challenge those decisions. However, recent feedback indicates that some entities have rights to operate that are indefinite, or that are finite but are seen as perpetual because their licences to operate are continually renewed. The IASB has not previously discussed indefinite rights to operate.

⁹ Paragraphs B30 and B31 of the Exposure Draft.

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24. The recent feedback indicates that identifying whether entities have a right to operate is not necessarily difficult. What may be more difficult to assess is whether the entity has a right to recover the regulatory asset in full.
25. This section considers how the final Accounting Standard could articulate the guidance on the boundary of a regulatory agreement, acknowledging the possibility of both finite and indefinite rights to operate. We think that the right to recover a regulatory asset may be supported by legislative or regulatory frameworks that provide sufficient assurance that the entity:
- (a) will recover all or substantially all of the regulatory asset over the asset's life through regulated rates charged; or
 - (b) will be compensated for all or substantially all of the unrecovered regulatory asset in the event of termination of the regulatory agreement.
26. This section is structured as follows:
- (a) indefinite rights to operate (paragraphs 27–30);
 - (b) rights to recover all or substantially all of a regulatory asset (paragraphs 31–50);
 - (c) lack of evidence of rights to recover all or substantially all of a regulatory asset (paragraphs 51–58); and
 - (d) conclusion (paragraphs 59–62).

Indefinite rights to operate

27. The boundary proposals in the Exposure Draft contemplate regulatory agreements that confer rights to operate for fixed periods. However, based on recent feedback, we think that some entities, particularly those that operate via an overarching framework or through a continually renewable licence, could argue that they will have a right to operate that is indefinite (see appendix). The following feedback supports this argument:

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- (a) some entities operate via an overarching framework (for example, a national Code of Energy) that acknowledges an entity meets the economic and technical criteria to supply specified goods or services and allocates the right to supply those goods or services to the entity for an indefinite period of time.
 - (b) some entities operate through renewable licences:
 - (i) the renewal of the licence is often viewed as an administrative procedure—renewal occurs unless there is a significant breach in any of the conditions of the licence; and
 - (ii) the direct costs of renewal are not high.
 - (c) in both (a) and (b), there are often no other entities that could replace the entity—that is, replacing the entity would lead to major disruption in the provision of an essential public service.
28. We think that the final Accounting Standard should acknowledge the possibility of entities having indefinite rights to operate. An entity could use the factors in paragraph 27 when determining whether its right to operate is indefinite.
29. The fact that rights to operate are finite or indefinite does not change the boundary concept set out in paragraph 34 of the Exposure Draft. Cash flows within the boundary are those for which an entity has an enforceable present right to add an amount to future regulated rates. As mentioned in paragraph 22, the enforceability of an entity's right to add an amount to future regulated rates depends on the entity having a right to operate and a right to recover. Whether the right to operate is finite or indefinite does not affect the enforceability of the right to add—as long as the entity has both a right to operate and a right to recover, there is an enforceable right to add. Therefore whether the right to operate is finite or indefinite does not affect the boundary concept in the Exposure Draft.

30. We recommend the final Accounting Standard acknowledge that rights to operate may be indefinite.

Question for the IASB

1. Does the IASB agree with the recommendation in paragraph 30?

Rights to recover all or substantially all of a regulatory asset

31. The boundary proposals require that an entity has a right to operate **and** a right to recover the regulatory asset. We recommend to clarify that a right to operate may be indefinite (paragraph 30).
32. This section:
- (a) focuses on an entity's right to recover a regulatory asset—whether that be by adding amounts to regulated rates over the asset's life or by compensation on termination; and
 - (b) considers how guidance on an entity's right to recover a regulatory asset could clarify which cash flows an entity includes within the boundary (that is, within the measurement of that regulatory asset), considering both scenarios in (a).
33. Feedback from recent outreach shows that some entities are subject to legislative or regulatory frameworks that provide a high level of assurance that an entity will recover all or substantially all of a regulatory asset over the asset's life. We think that an entity could use the following indicators to determine that its legislative or regulatory frameworks provide sufficient assurance that it will recover a regulatory asset over the asset's life:
- (a) the methodology that the regulator follows for determining the regulated rate is enshrined in law or in the regulatory framework and the rate is determined so that the entity recovers its costs and earns a fair return. A methodology that ensures an entity recovers its costs would protect the entity from loss on

- termination because the entity would be entitled to recover any outstanding amounts.
- (b) there is historical consistency and clarity in the regulator’s approach to cost recovery in the determination of the regulated rate.
 - (c) there is no indication of uncertainty or potential changes to the regulatory agreement regarding the recovery of costs in the determination of the regulated rate.
34. In addition, entities may also be subject to a legislative framework that would ensure investors recover all or substantially all of their investments (including any unrecovered regulatory assets), with no relevant precedents of lack of compensation on termination. The existence of such a legislative framework means that in the case of termination, the entity would be entitled to recover substantially all outstanding amounts.
35. We think both situations—assurance that an entity will recover *all or substantially all* of a regulatory asset over its life or an entity’s right to compensation on termination—would allow an entity to regard all cash flows arising from a regulatory asset as arising within the boundary. The following paragraphs consider in more detail the rights for compensation on termination.
36. The earlier descriptions of make-whole mechanisms considered by the IASB said that, **provided the make-whole mechanism is adequate**, an entity would be *economically indifferent* between recovering a regulatory asset through future regulated rates charged to customers or through compensation on termination of the regulatory agreement (paragraph 15(c)).
37. The Exposure Draft does not specify that compensation has to be ‘adequate’ or meet a certain threshold for the cash flows from compensation to be included in the boundary. The Exposure Draft proposes that:
- (a) all cash flows arising from a right to receive compensation for unrecovered regulatory assets are cash flows within the boundary (as long as the amount of

such compensation depends solely on the monetary amount of the unrecovered regulatory assets);¹⁰ and

- (b) any difference between the unrecovered regulatory assets and the compensation be dealt with by the measurement proposals.¹¹

38. We think that for an entity to be economically indifferent between recovering a regulatory asset through future regulated rates charged to customers or through compensation on termination, it would be necessary that the compensation be for *all or substantially all* unrecovered regulatory assets. In other words, for the cash flows arising from an enforceable right to receive compensation for unrecovered regulatory assets to be regarded as arising within the boundary of the regulatory agreement and thus, included in the measurement of the related regulatory assets, we think that right to compensation needs to be for all or substantially all unrecovered regulatory assets.
39. We recommend that cash flows arising from an enforceable right to receive compensation on termination be regarded as arising within the boundary only if that right to compensation is for all or substantially all unrecovered regulatory assets. This proposal would limit the population of cash flows that an entity would consider as arising within the boundary. We think this limitation is appropriate because it would ensure the entity is indifferent between recovering the regulatory asset by adding amounts to future regulated rates or by receiving compensation on termination of the regulatory agreement.
40. We think the proposed guidance in paragraph B37 of the Exposure Draft regarding uncertain cash flows would still be useful to address any difference between the amount of compensation on termination and the unrecovered regulatory assets.
41. We think that an entity could conclude it has a right to recover its regulatory asset because the legislative or regulatory frameworks provide:

¹⁰ Paragraph B36 of the Exposure Draft and paragraph BC152 of the Basis for Conclusions accompanying the Exposure Draft—see paragraphs 16 and 17 of this paper.

¹¹ Paragraph B37 of the Exposure Draft.

- (a) sufficient assurance that the entity will recover all or substantially all of the regulatory asset over the asset's life through regulated rates charged; or
- (b) a right for compensation on termination for all or substantially all of the unrecovered regulatory asset.

In such cases we think an entity should regard all cash flows arising from a regulatory asset as arising within the boundary when measuring the regulatory asset.

42. That conclusion would not be affected by whether the entity has a finite or indefinite right to operate. The following paragraphs illustrate this.

Finite rights to operate

43. An entity operating in accordance with a service concession arrangement generally has a finite right to operate. These arrangements may or may not fall within the scope of IFRIC 12 *Service Concession Arrangements*.¹² According to the feedback from preparers that operate under service concession arrangements, the possibility of renewing the arrangement is limited, either by law or because there is a new bid process at the end of the concession.
44. Service concession arrangements generally include explicit rights to compensation for unrecovered regulatory assets on termination. Compensation could occur in one of three ways:
- (a) through compensation from the regulator;
 - (b) by transferring any unrecovered regulatory assets to the new operator and receiving compensation from the new operator; or
 - (c) through being permitted to adjust rates charged to other groups of customers.

¹² The IASB has tentatively decided—[Agenda Paper 9A](#) discussed in September 2022—to clarify in the final Accounting Standard 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 Standard to any remaining rights and obligations to determine if the entity has regulatory assets or regulatory liabilities.

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45. The feedback from the outreach suggests that it would be unusual for there to be a material difference between the amount of compensation and the amount of unrecovered regulatory assets.
 46. The feedback indicates that an entity operating under a service concession arrangement—that is, an entity with finite rights to operate—could substantiate its right to recover a regulatory asset through an explicit right to compensation on termination. In addition, the feedback from outreach indicates that that compensation would be generally for all or substantially all outstanding balances. In such cases we think it would be appropriate that an entity consider all estimated future cash flows arising from a regulatory asset in the measurement of that regulatory asset.

Indefinite rights to operate

47. As described in paragraph 27, an entity may conclude it has a right to operate that is indefinite. In addition, its regulatory agreement may ensure that it will recover all or substantially all of the costs incurred in supplying goods or services over the life of the regulatory asset and possibly indefinitely. Feedback that supports this argument includes comments about the existence of legislative or regulatory frameworks that support the recovery of costs and the recovery of all or substantially all unrecovered regulatory assets if the regulatory agreement terminates.
48. In this case, the entity would include all estimated future cash flows arising from a regulatory asset in the measurement of the regulatory asset without having to identify a specific point in time as the boundary of the regulatory agreement.
49. Legislative or regulatory frameworks that provide assurance for recoverability of costs may also establish conditions for such recoverability. For example, regulators often limit the recoverability of costs to those that an entity has incurred prudently or incurred when operating the assets with certain degree of efficiency. We think those regulatory checks would mainly contribute to measurement uncertainty rather than to the determination of the set of cash flows that need to be considered within the boundary—that is, within the measurement of a regulatory asset.

50. We recommend the final Accounting Standard require that an entity that has an enforceable right to operate include all the unrecovered (unfulfilled) cash flows in the measurement of the regulatory asset (regulatory liability) if the entity has:
- (a) an enforceable right to recover (obligation to fulfil) all or substantially all of the regulatory asset (regulatory liability) by adding amounts to (deducting amounts from) future regulated rates charged over its life; or
 - (b) an enforceable right, on termination of the agreement, to receive (obligation to pay) compensation for all or substantially all of the unrecovered regulatory asset (unfulfilled regulatory liability).

Question for the IASB

2. Does the IASB agree with the recommendation in paragraph 50?

Lack of evidence of rights to recover all or substantially all of a regulatory asset

51. Legislative or regulatory frameworks may *not* provide:
- (a) sufficient assurance that an entity will recover all or substantially all of a regulatory asset over the asset's life through regulated rates charged; or
 - (b) a right for compensation on termination for all or substantially all of the unrecovered regulatory asset.
52. If legislative or regulatory frameworks do not provide sufficient assurance that an entity has a right to recover all or substantially all of its regulatory assets, the entity would need to consider all potential cash flows and identify which of those cash flows it should include in the measurement of regulatory assets.¹³ This would apply to both

¹³ The need to consider all reasonable and supportable information when estimating cash flows is already included in paragraph 32 of the Exposure Draft.

the case an entity has a right to operate that is finite or an entity with a right to operate that is indefinite. The following paragraphs illustrate this.

Finite rights to operate

53. As mentioned in paragraph 43, a common example of an entity having a finite right to operate is a service concession arrangement. Although we think this scenario is unlikely to occur (because entities enter into service concession arrangements expecting to recover their investments), we have included it to illustrate the range of possibilities. Assume an entity operates under a 30-year service concession arrangement that will not be renewed and that gives the entity the right to recover only 60% of any unrecovered regulatory assets in Year 30. In such a scenario, the cash flows at risk of not being included in the measurement of regulatory assets would be:
- (a) the cash flows of long-term regulatory assets that would be outstanding close to, or beyond, the end of the service concession arrangement; and
 - (b) the cash flows of regulatory assets that originate close to the end of the arrangement.
54. When measuring such regulatory assets, an entity would consider only those cash flows for which it has a right to recover, including compensation for any unrecovered regulatory assets on termination, as being within the boundary.

Indefinite rights to operate

55. An entity with an indefinite right to operate would have a right to supply goods or services for an indefinite period. Despite this the entity may be unable to include all the estimated future cash flows in the measurement of the regulatory asset because it may not have an enforceable present right to increase future regulated rates sufficiently to recover all or substantially all of the regulatory asset or the legislative or regulatory frameworks may not ensure the entity has a right of compensation for all or substantially all of the unrecovered regulatory asset. The fact that it is subject to a legislative or regulatory framework that is not fully supportive of cost recovery could call into question its ability to recover all or part of a regulatory asset.

56. However, such entities may still have present enforceable rights to recover certain types of costs or to recover costs relating to certain periods of time.
57. We think such an entity would need to determine the set of cash flows for which its legislative or regulatory frameworks provide sufficient assurance for recovery and for which it therefore has an enforceable right to add amounts to future regulated rates. This set of cash flows may be in relation to types of costs, costs incurred up to a certain point or costs that will be recovered by a certain point. For example, the entity may include cash flows up to a specified period in the measurement of its regulatory assets.
58. Paragraph 50 describes the conditions that would result in an entity including all the unrecovered (unfulfilled) cash flows in the measurement of the regulatory asset (regulatory liability). In cases where an entity has an enforceable right to operate but does not meet the conditions described in paragraph 50(a) or paragraph 50(b), we recommend the final Accounting Standard require that the entity determine the set of unrecovered (unfulfilled) cash flows for which its legislative or regulatory frameworks provide sufficient assurance for recovery (fulfilment) and include those cash flows in the measurement of a regulatory asset (regulatory liability).

Question for the IASB

3. Does the IASB agree with the recommendation in paragraph 58?

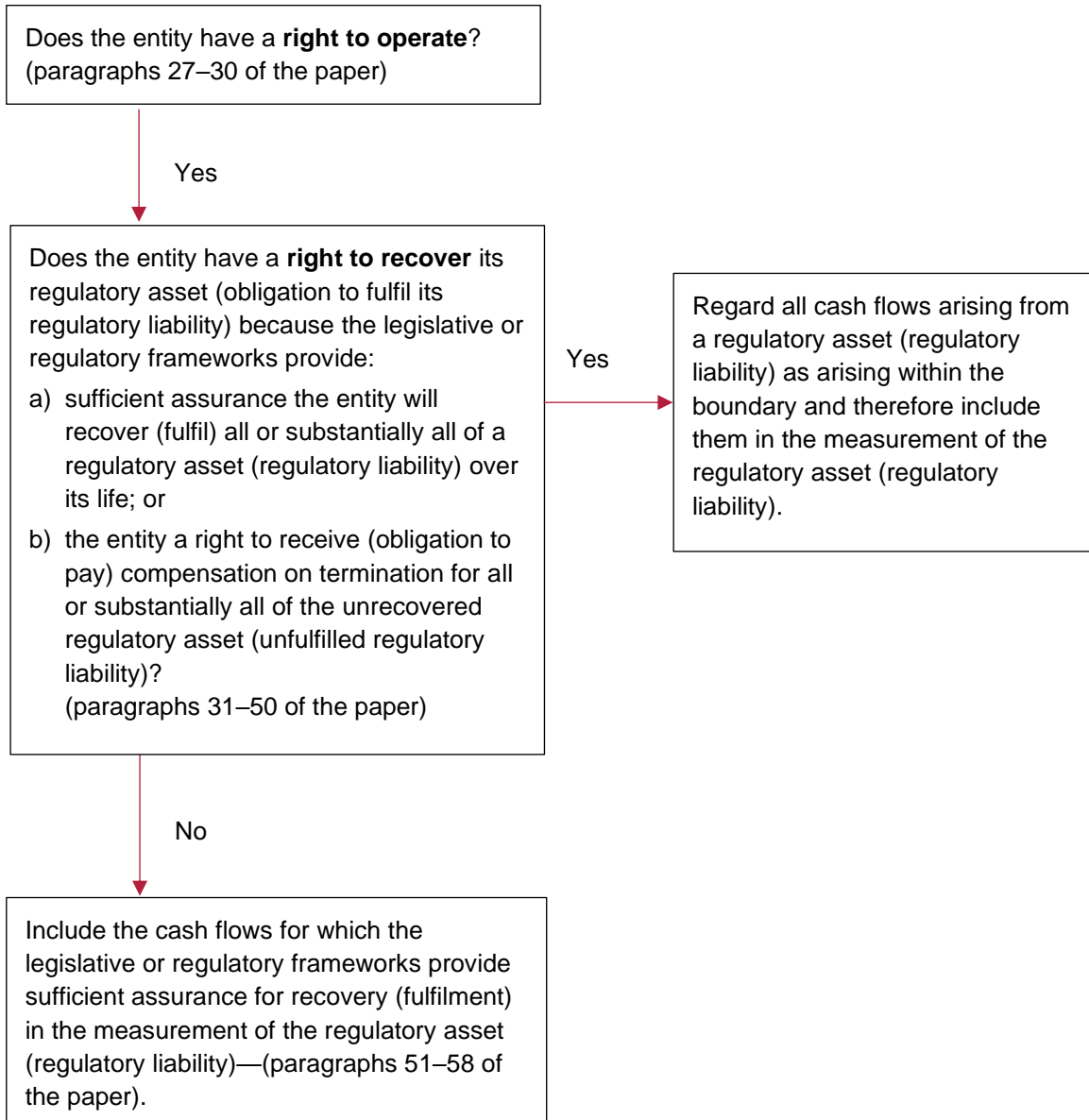
Conclusion

59. The Exposure Draft describes the boundary of a regulatory agreement as the latest future date at which an entity has an enforceable present right to add an amount to future regulated rates.¹⁴ The Exposure Draft also proposes that for the right to add to be enforceable, an entity must have:

¹⁴ Paragraphs 34 and B30 of the Exposure Draft.

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- (a) a right to operate at a future date; and
 - (b) a right for compensation if the regulatory agreement is cancelled before that date.
60. We are not recommending any change to those proposals. Nor are we recommending any changes to the IASB's tentative decisions dealing with rights to renew or cancel a regulatory agreement.
61. However, we are recommending that the final Accounting Standard acknowledges that an entity may have a right to operate that is indefinite. We also recommend that in deciding which cash flows are within the boundary (and therefore included in the measurement of a regulatory asset), an entity consider its right to operate and its right to recover a regulatory asset (either through future regulated rates or through compensation on termination of a regulatory agreement).
62. Flow chart 1 illustrates the process an entity would follow when determining which cash flows to include in the measurement of its regulatory assets and regulatory liabilities (based on the recommendations in this paper). Having identified the relevant cash flows, an entity would then need to consider whether the cash flows are subject to any uncertainties (for example, uncertainties arising from credit or demand risks).

Flow chart 1—Identifying the cash flows that arise within the boundary



Question for the IASB

4. Does the IASB have any comments on flow chart 1?

Appendix—Outreach

- A1. After the IASB meeting in October 2023, we reached out to a few preparers in Asia-Oceania, Europe, North America and Latin America to discuss the determination of the boundary in their particular cases. This appendix contains feedback from that outreach.
- A2. We have identified some common themes in this feedback.
- (a) Regulatory agreements can be perpetual or indefinite. Preparers in Asia-Oceania, North America and Europe gave examples of licences that are valid for an indefinite period or expected to be renewed indefinitely. They also gave examples of regulatory frameworks that give operators the practical ability to operate for an indefinite period.
 - (b) Regulatory agreements support the recoverability of costs. Some preparers said that the regulatory framework provides an entity with the right to recover costs and to earn a fair return. This is because the regulatory framework establishes the methodology the regulator uses to establish rates and ensures that certain costs, particularly those that are ‘non-controllable’, are always considered in the determination of rates. A few preparers were of the view that this right to recover costs could be seen to be indefinite.
 - (c) Unrecovered regulatory assets are expected to be recovered in some way. Some preparers said they would expect to recover unrecovered regulatory assets on termination of the agreement, on sale of a regulated business or on deregulation. Their expectations were based on explicit rights in a regulatory agreement (mainly in the case of entities operating under service concession arrangements), the existence of precedents or the legislative or regulatory frameworks suggesting the existence of explicit or implicit rights.
 - (d) The termination of a regulatory agreement may not be contemplated in the regulatory framework. Preparers said that some regulatory frameworks do not

include any provisions for termination because termination is not expected to occur.

A3. This feedback shares many common points with the views expressed by respondents to the 2013 Request for Information *Rate Regulation* about the characteristics of rate-regulated entities and the environment within which they operate (**emphasis added**).¹⁵

28. Typically, the entities that are subject to rate regulation have a **monopoly or near-monopoly right** to operate in a pre-determined geographical service territory. The monopoly right may be:

(a) explicit - for example, the right may be defined by an **exclusive licence agreement** with the rate regulatory or other licensing body, or through a **service concession arrangement** (which may or may not be within the scope of IFRIC 12 *Service Concession Arrangements* [...]), or through **legislation/regulation**; or

(b) implicit - for example, there may be significant barriers to entry (a 'natural monopoly') due to, for example, the high-level of capital investment required or because of physical constraints that apply to putting the necessary infrastructure in place (for example, accessing private land in order to lay a pipeline).

29. When a supplier entity is granted an explicit right to operate in a particular area, the specific direct cost to acquire or renew the right is typically not significant. **The length of time that the explicit right is granted for varies widely**. It is typically granted for a medium- or long-term period (for example, five to 30 years). **Renewal** is sometimes open to competition but is **more typically automatic**, as long as the entity can demonstrate compliance with the terms of the licence.

...

33. The consensus of respondents is that the rate-regulated entity **cannot cease, suspend, restructure or transfer operations (and the rights and obligations attached to those operations) without the approval of the rate regulator**. In most cases, this inability to cease operations is explicit in the licence, rate regulation or legislation. Where there is no explicit obligation to continue to operate, **the common understanding is that there is an implicit obligation** and the rate regulator or other government controlled body would step-in to ensure continuity of supply if necessary.

¹⁵ Quoted from the [Request for Information response summary](#) presented to the IASB in July 2013.