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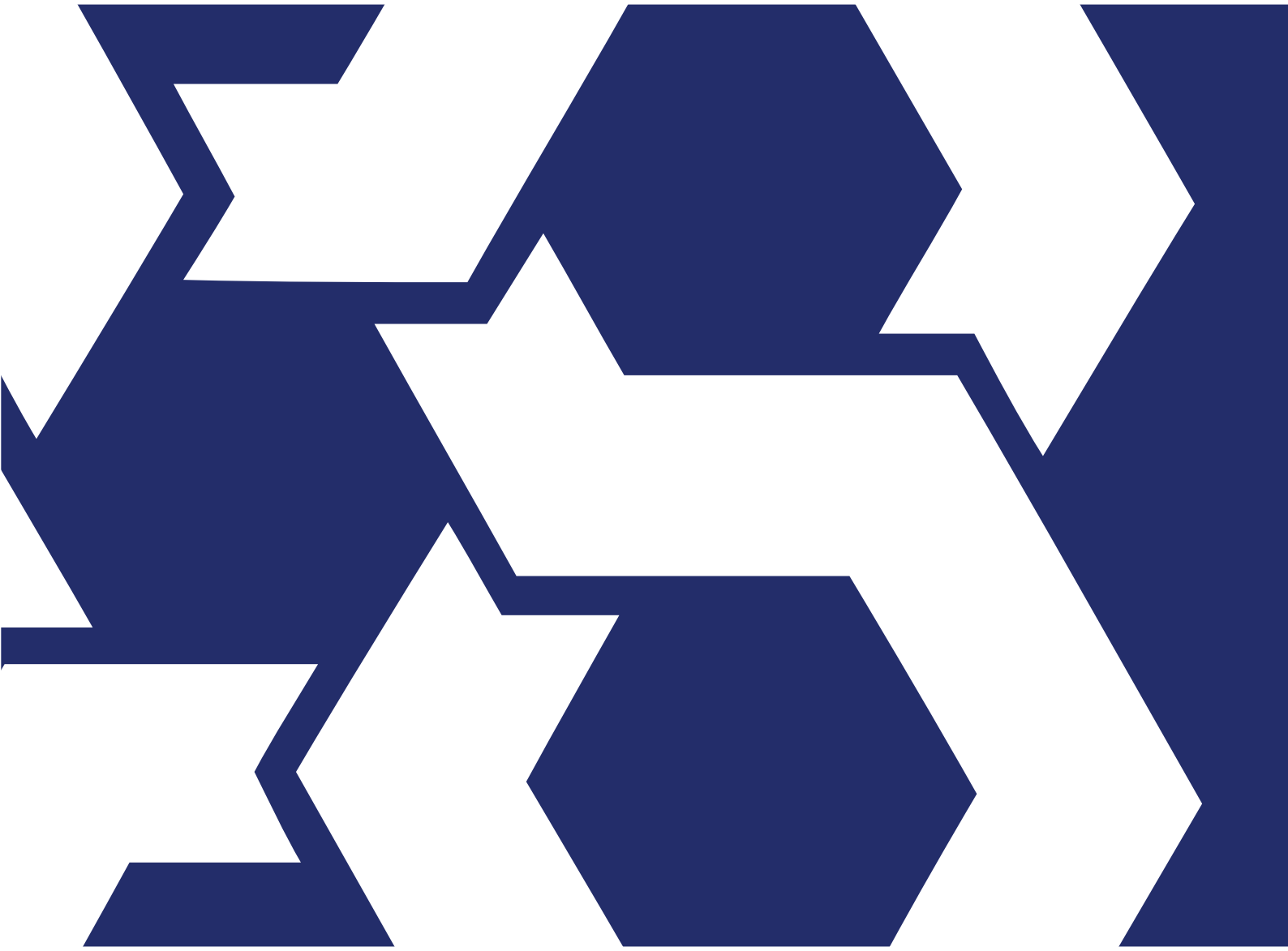
Illustrative Examples on Regulatory Assets and Regulatory Liabilities



International Accounting Standards Board

Illustrative Examples on
IFRS 20
Regulatory Assets and Regulatory Liabilities

This Illustrative Examples accompanies IFRS 20 *Regulatory Assets and Regulatory Liabilities* (issued May 2026; see separate booklet) and is issued by the International Accounting Standards Board (IASB).

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Illustrative Examples on IFRS 20 *Regulatory Assets and Regulatory Liabilities*

These examples accompany, but are not part of, IFRS 20 Regulatory Assets and Regulatory Liabilities. *They illustrate aspects of IFRS 20 but are not intended to provide interpretative guidance.*

Introduction

IE1 These examples illustrate how an entity might apply some of the requirements in IFRS 20 to particular aspects of the accounting for regulatory assets and regulatory liabilities based on the limited facts presented. The analysis in each example is not intended to represent the only manner in which the requirements could be applied.

IE2 The fact patterns in these examples are simplified. All relevant facts and circumstances of a particular fact pattern would have to be evaluated when applying IFRS 20.

IE3 For simplicity, unless specified otherwise, all examples:

(a) assume that an entity supplies regulatory goods or services under a regulatory agreement;

(b) assume that an entity has only the regulatory assets or regulatory liabilities discussed in the example;

(c) assume that an entity applies the cost model in IFRS Accounting Standards applicable to depreciable and amortisable assets;

(d) assume that all revenue from contracts with customers (IFRS 15 revenue) is recognised when (or as) the entity supplies goods or services to customers;

(e) assume, for examples that include arrangements in the scope of IFRIC 12 *Service Concession Arrangements*, the arrangements meet the definition of a regulatory agreement;

(f) denominate all monetary amounts in 'currency units' (CU), rounded to the nearest whole number; and

(g) ignore income taxes.

Relationship between an entity's regulatory capital base and its depreciable or amortisable assets

IE4 Examples 1A–5 illustrate IFRS 20 requirements for determining whether an entity's regulatory capital base has, or does not have, a direct relationship with its depreciable or amortisable assets. A depreciable or amortisable asset is an asset that is depreciable or amortisable in accordance with IFRS Accounting Standards, for example IAS 16 *Property, Plant and Equipment*, IAS 38 *Intangible Assets* or IFRS 16 *Leases*.

IE5 An entity's regulatory capital base might also include items other than depreciable and amortisable assets. If an example illustrates a relationship with only depreciable and amortisable assets, references in that example to the 'regulatory capital base' shall be read as 'a part of the regulatory capital base' unless specified otherwise.

Example 1A—Regulatory capital base has a direct relationship with depreciable and amortisable assets

IE6 Example 1A illustrates features of the regulatory capital base that an entity considers in determining that its regulatory capital base has a direct relationship with its depreciable and amortisable assets.

Fact pattern

IE7 Entity A is entitled to regulatory depreciation of its regulatory capital base.

IE8 The regulator determines the regulatory capital base and regulatory depreciation to enable Entity A to recover its depreciable and amortisable assets. The regulator determines the regulatory capital base using depreciable and amortisable assets that Entity A accounts for by applying IFRS Accounting Standards. The regulator determines regulatory depreciation to provide compensation for depreciation and amortisation expense based on the depreciation and amortisation expense Entity A recognises by applying IFRS Accounting Standards.

IE9 Entity A's regulatory capital base and its depreciable and amortisable assets have many similarities—for example:

(a) most of the items in the regulatory capital base are depreciable and amortisable assets;

(b) most of the classes in the regulatory capital base are the same as the asset classes as determined by applying IFRS Accounting Standards (that is, IFRS asset classes);

(c) all assets in the regulatory capital base are measured using the same measurement basis as the related depreciable and amortisable assets—that is, historical cost; and

(d) the regulatory recovery periods and patterns for most of the assets in the regulatory capital base are the same as the useful lives and depreciation methods of the related depreciable and amortisable assets determined by applying IFRS Accounting Standards.

IE10 The regulatory capital base also includes lump-sum adjustments that the regulator determines for the overall amount of assets in the regulatory capital base. Entity A is able to allocate those adjustments to IFRS asset classes using a reasonable and supportable basis.

IE11 When differences arise between classes in the regulatory capital base and IFRS asset classes, they are mainly due to the lump-sum adjustments described in paragraph IE10. Entity A is able to track such differences over the recovery periods of the regulatory classes and the useful lives of the IFRS asset classes.

Analysis

IE12 Entity A considers paragraphs B60–B68 of IFRS 20 to determine the relationship between its regulatory capital base and its depreciable or amortisable assets.

IE13 Applying paragraph B62 of IFRS 20, Entity A considers all reasonable and supportable information that is available without undue cost or effort, including:

(a) the regulatory methodology underlying the determination of the regulatory capital base and regulatory depreciation; and

(b) how the regulator monitors whether the regulatory depreciation provides compensation for the depreciation or amortisation expense.

IE14 Entity A determines that each IFRS asset class is the smallest aggregation of assets for which it is able to track, by amount and reporting period, how regulatory depreciation provides compensation for depreciation or amortisation expense. Therefore, Entity A concludes that its regulatory capital base has a direct relationship with its depreciable or amortisable assets in each IFRS asset class.

Example 1B—Regulatory capital base has a direct relationship with depreciable and amortisable assets—Different measurement bases

IE15 Example 1B illustrates how an entity considers whether different measurement bases affect the relationship between its regulatory capital base and its depreciable or amortisable assets.

Fact pattern

IE16 Example 1B assumes the same fact pattern as Example 1A, except that the regulatory agreement specifies that the regulatory capital base is adjusted for inflation.

IE17 The regulatory agreement specifies that inflation adjustments are calculated separately for each asset in the regulatory capital base. The inflation adjustments are included in the regulated rates as part of regulatory depreciation arising from each asset.

IE18 Accordingly, regulatory depreciation is determined in a way that provides compensation for the depreciation and amortisation expense Entity A recognises in a period and for the recovery of the cumulative inflation adjustment for individual assets in the regulatory capital base over the recovery periods of the assets.

Analysis

IE19 Applying paragraphs B60–B68 of IFRS 20, Entity A also considers the methodology specified in the regulatory agreement for calculating the inflation adjustments and including them in the regulated rates. Entity A determines—for each IFRS asset class—that it is able to separate the inflation adjustments from other amounts of regulatory depreciation. Entity A

concludes—for each IFRS asset class—that the inflation adjustments do not affect its ability to track, by amount and reporting period, how regulatory depreciation provides compensation for depreciation or amortisation expense.

IE20 Therefore, Entity A concludes that its regulatory capital base has a direct relationship with its depreciable or amortisable assets in each IFRS asset class.

Example 2—Determining the type of relationship and individual differences in timing for a group of depreciable or amortisable assets

IE21 Example 2 illustrates how an entity applies IFRS 20 requirements to determine the type of relationship and individual differences in timing for a group of depreciable or amortisable assets.

Fact pattern

IE22 Entity A completed the construction of assets during Year 0. Those assets became available for use on the first day of Year 1. Entity A recognises those assets as property, plant and equipment by applying IAS 16. Entity A recognises depreciation expense on a straight-line basis over the assets' useful lives.

IE23 The regulatory agreement specifies that the cost of those assets is included in the regulatory capital base once the assets are available for use. The regulatory agreement entitles Entity A to recover the cost of the assets through regulatory depreciation on a straight-line basis over the regulatory recovery period.

IE24 For simplicity, this example assumes that:

(a) Entity A does not have other depreciable and amortisable assets; and

(b) the regulatory agreement does not provide regulatory returns on the regulatory capital base.

IE25 The regulator determines the regulatory capital base and regulatory depreciation using information about the property, plant and equipment Entity A has accounted for by applying IAS 16. The regulator requires Entity A to track any differences between the classes of assets in its regulatory capital base (that is, regulatory classes) and the classes of property, plant and equipment as determined by applying IAS 16 (that is, IFRS asset classes). The regulatory methodology for determining the regulatory capital base enables Entity A to identify:

(a) the amounts in each IFRS asset class that are included in each regulatory class; and

(b) the amount of depreciation expense arising from each IFRS asset class that is compensated through regulatory depreciation arising from each regulatory class.

IE26 Table 2.1 shows property, plant and equipment by IFRS asset class.

Table 2.1—Property, plant and equipment			
In CU **IFRS asset class**	**Cost**	**Useful lives (weighted average)**	**Depreciation expense per year**
Asset Class 1	3,000	5 years	600
Asset Class 2	12,000	2 to 4 years (3 years)	4,000
Total	**15,000**		**4,600**

IE27 Table 2.2 shows a matrix reconciling the regulatory capital base with property, plant and equipment.

Table 2.2—Reconciliation between regulatory capital base and property, plant and equipment				
		IFRS asset class		
In CU	**Recovery period**	**Asset Class 1**	**Asset Class 2**	**Total**
Regulatory Class 1	5 years	3,000	3,000	**6,000**
Regulatory Class 2	2 years	—	9,000	**9,000**
Total		**3,000**	**12,000**	**15,000**
Of which:				
Regulatory recovery period and useful lives are the same		3,000	—	**3,000**
Regulatory recovery period is:				
– longer than useful lives		—	3,000	**3,000**
– shorter than useful lives		—	9,000	**9,000**
Total		**3,000**	**12,000**	**15,000**

Analysis

IE28 Entity A considers paragraphs B60–B68 of IFRS 20 to determine the relationship between its regulatory capital base and its depreciable or amortisable assets.

IE29 Applying paragraph B62 of IFRS 20, Entity A considers all reasonable and supportable information that is available without undue cost or effort, including:

(a) the regulatory methodology underlying the determination of the regulatory capital base and regulatory depreciation; and

(b) how the regulator monitors whether the regulatory depreciation provides compensation for the depreciation or amortisation expense.

IE30 Entity A determines that:

(a) it is able to disaggregate each IFRS asset class into regulatory classes—for example, Entity A is able to disaggregate IFRS Asset Class 2 into Regulatory Class 1 and Regulatory Class 2.

(b) each disaggregated part of an IFRS asset class is the smallest aggregation of assets for which it is able to track, by amount and reporting period, how depreciation expense is compensated through regulatory depreciation.

IE31 Applying paragraphs B65–B66 of IFRS 20, Entity A determines that its regulatory capital base has a direct relationship with its property, plant and equipment in each disaggregated part of an IFRS asset class. Entity A uses this aggregation of assets to determine individual differences in timing arising from regulatory depreciation.

IE32 To determine individual differences in timing, Entity A compares the recovery period of the regulatory class with the weighted-average useful life of the assets in each disaggregated part of an IFRS asset class. Entity A recognises—from each disaggregated part of an IFRS asset class—a regulatory asset or regulatory liability that arises if its weighted-average useful life differs from the recovery period for the regulatory class.

IE33 IFRS Asset Class 2 comprises assets with a weighted-average useful life of three years. Of those assets:

(a) CU3,000 is recovered through regulatory depreciation over five years. A regulatory asset arises from regulatory depreciation because part of the total allowed compensation for regulatory goods or services supplied during Years 1–3 will be included in IFRS 15 revenue in the future. Entity A recognises the regulatory asset and recovers it over Years 4–5.

(b) CU9,000 is recovered through regulatory depreciation over two years. A regulatory liability arises from regulatory depreciation because part of the total allowed compensation for regulatory goods or services to be supplied in the future has already been included in IFRS 15 revenue during Years 1–2. Entity A recognises the regulatory liability and fulfils it in Year 3.

IE34 Table 2.3 shows the reconciliation of regulatory assets.

Table 2.3—Reconciliation of the carrying amount of regulatory assets

In CU	Year 1	Year 2	Year 3	Year 4	Year 5
Opening carrying amount	—	400	800	1,200	600
Amount recognised[(a)]	400	400	400	—	—
Amount recovered[(b)]	—	—	—	(600)	(600)
Closing carrying amount	**400**	**800**	**1,200**	**600**	**—**

(a) For Years 1–3, the amount recognised is calculated as the difference between depreciation expense of CU1,000 [CU3,000 ÷ 3] and regulatory depreciation of CU600 [CU3,000 ÷ 5].

(b) In Years 4–5, the regulatory asset is recovered through regulatory depreciation of CU600.

IE35 Table 2.4 shows the reconciliation of regulatory liabilities.

Table 2.4—Reconciliation of the carrying amount of regulatory liabilities

In CU	Year 1	Year 2	Year 3
Opening carrying amount	—	1,500	3,000
Amount recognised[(a)]	1,500	1,500	—
Amount fulfilled[(b)]	—	—	(3,000)
Closing carrying amount	**1,500**	**3,000**	**—**

(a) For Years 1–2, the amount recognised is calculated as the difference between regulatory depreciation of CU4,500 [CU9,000 ÷ 2] and depreciation expense of CU3,000 [CU9,000 ÷ 3].

(b) In Year 3, the regulatory liability is fulfilled because the regulated rates charged in that year do not include any regulatory depreciation that compensates Entity A for the depreciation expense it recognises of CU3,000 in that year.

Example 3A—Regulatory capital base does not have a direct relationship with depreciable and amortisable assets

IE36 Example 3A illustrates features of the regulatory capital base that an entity considers in determining that its regulatory capital base does not have a direct relationship with its depreciable and amortisable assets.

Fact pattern

IE37 Entity A is entitled to an amount of allowed revenue that includes regulatory depreciation of its regulatory capital base.[1] The regulator determines the allowed revenue using Entity A's budgeted costs, adjusted by efficiency targets. In doing so, the regulator weakens the link between the allowed revenue for a period and the costs incurred by Entity A during that period.

IE38 The regulator determines the regulatory capital base using mainly capital expenditure, as specified by the regulatory agreement, instead of information about Entity A's depreciable and amortisable assets. Entity A's regulatory capital base and its depreciable and amortisable assets differ substantially—for example:

(a) the items in the regulatory capital base differ from the depreciable and amortisable assets Entity A accounts for by applying IFRS Accounting Standards. The regulatory capital base includes items that do not qualify for capitalisation applying those Accounting Standards and excludes items that are capitalised applying those Accounting Standards.

(b) the classes in the regulatory capital base differ from the asset classes as determined by applying IFRS Accounting Standards (that is, IFRS asset classes). Each regulatory class includes assets from different IFRS asset classes. In addition, assets in each IFRS asset class are included in different regulatory classes.

(c) the regulator determines the regulatory recovery period for each regulatory class based on the average economic lives of the assets within that class. The economic lives of those assets might differ from the useful lives of depreciable or amortisable assets determined by applying IFRS Accounting Standards. The depreciable or amortisable assets in each IFRS asset class can have a wide range of useful lives.

(d) the regulatory capital base is adjusted for inflation. The regulator does not monitor the recovery of inflation adjustments separately from other items in the regulatory capital base in determining regulatory depreciation.

IE39 The regulator determines the regulatory depreciation to be included in the allowed revenue for a period by considering factors that are unrelated to the depreciation and amortisation expense Entity A recognises in that period by applying IFRS Accounting Standards. In particular, the regulator:

1 Appendix A of IFRS 20 *Regulatory Assets and Regulatory Liabilities* defines allowed revenue as the total amount of compensation that a regulatory agreement entitles an entity to charge customers through regulated rates in a period. The allowed revenue for a period is divided by the estimated quantity of goods or services to be supplied to customers in that period. That calculation determines the regulated rate per unit that the entity will charge customers to recover the allowed revenue during that period.

(a) uses the regulatory depreciation, calculated as described in paragraph IE38(c), for the penultimate year within Regulatory Period 1 to determine the regulatory depreciation to be included in the allowed revenue for Regulatory Period 2; and

(b) makes lump-sum adjustments to the regulatory depreciation for Regulatory Period 1, as determined in (a), to exclude specific amounts and to reflect the expected level of investment and the targeted efficiency for Regulatory Period 2.

Analysis

IE40 Entity A considers paragraphs B60–B68 of IFRS 20 to determine the relationship between its regulatory capital base and its depreciable or amortisable assets.

IE41 Applying paragraph B62 of IFRS 20, Entity A considers all reasonable and supportable information that is available without undue cost or effort, including:

(a) the regulatory methodology underlying the determination of the regulatory capital base and regulatory depreciation; and

(b) how the regulator monitors whether the regulatory depreciation provides compensation for the depreciation or amortisation expense.

IE42 Entity A determines that the assets and classes in the regulatory capital base differ substantially from its depreciable or amortisable assets and from the IFRS asset classes. Entity A concludes that it is unable to track differences between the classes in the regulatory capital base and the IFRS asset classes. Entity A also determines that the regulator neither considers depreciation or amortisation expense in determining regulatory depreciation nor monitors how regulatory depreciation provides compensation for depreciation or amortisation expense.

IE43 Therefore, Entity A determines that it is unable to track, by amount and reporting period, how regulatory depreciation provides compensation for depreciation or amortisation expense for any IFRS asset class. Entity A makes its determination considering the indicators in paragraphs B67–B68 of IFRS 20 of whether a regulatory capital base has a direct relationship with depreciable or amortisable assets. Entity A concludes that its regulatory capital base does not have a direct relationship with its depreciable and amortisable assets.

Example 3B—Regulatory capital base does not have a direct relationship with depreciable and amortisable assets, but includes specific items that are tracked separately

IE44 Example 3B illustrates how an entity considers separate tracking of a part of its regulatory capital base comprising specific items in determining the relationship with those specific items if the remaining part of the regulatory capital base does not have a direct relationship with depreciable and amortisable assets and any other related items.

Fact pattern

IE45 Example 3B assumes the same fact pattern as Example 3A, except that the regulatory capital base also includes specific allowable expenses that did not arise from depreciable and amortisable assets.

IE46 The regulator monitors the recovery of these specific allowable expenses separately from the rest of the regulatory capital base. The regulator determines the amount of regulatory depreciation related to these specific allowable expenses by using a separate depreciation schedule.

Analysis

IE47 Applying paragraph B61 of IFRS 20, Entity A determines the relationship for that part of the regulatory capital base that comprises the specific allowable expenses separately from the remaining part of the regulatory capital base. Entity A determines that it is able to track, by amount and reporting period, how regulatory depreciation provides compensation for specific allowable expenses arising in each reporting period. Therefore, Entity A concludes that a part of its regulatory capital base has a direct relationship with the specific allowable expenses.

Example 4—Regulatory capital base determined based on total expenditure

IE48 Example 4 illustrates how an entity considers the methodology the regulator uses to determine the regulatory capital base and regulatory depreciation in determining the relationship between its regulatory capital base and its depreciable or amortisable assets.

Fact pattern

IE49 Entity A is entitled to an amount of allowed revenue that includes regulatory depreciation of its regulatory capital base. The regulator determines the allowed revenue using Entity A's budgeted costs, adjusted by efficiency targets. In doing so, the regulator weakens the link between the allowed revenue for a period and the costs incurred by Entity A during that period.

IE50 In particular, the regulator determines the allowed revenue using an approach that considers Entity A's total expenditure, comprising operating and capital expenditure, for a regulatory period. The regulator determines total expenditure considering targeted efficiency, instead of the actual amount of total expenditure. The regulator also determines capital expenditure differently from the amounts Entity A recognises as depreciable and amortisable assets by applying IFRS Accounting Standards.

IE51 The regulator applies a capitalisation rate to the total expenditure to determine the amount to be added to Entity A's regulatory capital base in that period. The regulator includes the remaining balance of the total expenditure in the regulated rates charged for the same period.

IE52 The regulator determines:

(a) the capitalisation rate with the aim of accelerating or deferring funding for Entity A by considering factors in addition to the ratios of capital expenditure to total expenditure. Therefore, the regulator might change the capitalisation rate from one regulatory period to the next regulatory period in a way that does not reflect the ratios of capital expenditure to total expenditure.

(b) the regulatory capital base without using information about depreciable and amortisable assets. The regulatory capital base is a rolling balance that cannot be segregated into individual items or classes. That balance includes capital and operating expenditure, together with other items such as performance incentives and inflation adjustments.

(c) regulatory depreciation of the regulatory capital base by considering factors that are unrelated to the depreciation and amortisation expense Entity A recognises by applying IFRS Accounting Standards. The regulator determines a single regulatory depreciation rate for the regulatory capital base. The regulatory recovery period of the regulatory capital base differs significantly from the useful lives of depreciable and amortisable assets and might change between regulatory periods.

Analysis

IE53 Entity A considers paragraphs B60–B68 of IFRS 20 to determine the relationship between its regulatory capital base and its depreciable or amortisable assets.

IE54 Applying paragraph B62 of IFRS 20, Entity A considers all reasonable and supportable information that is available without undue cost or effort, including:

(a) the regulatory methodology underlying the determination of the regulatory capital base and regulatory depreciation; and

(b) how the regulator monitors whether the regulatory depreciation provides compensation for the depreciation or amortisation expense.

IE55 Entity A determines that its regulatory capital base is a rolling balance that cannot be linked to depreciable and amortisable assets that it accounts for by applying IFRS Accounting Standards. Entity A also determines that it is unable —using a reasonable and supportable basis—to allocate efficiency adjustments in the regulatory capital base to the asset classes as determined by applying IFRS Accounting Standards (that is, IFRS asset classes). Therefore, Entity A concludes that it is unable to track differences between its regulatory capital base and its depreciable and amortisable assets by IFRS asset class. Entity A further determines that the regulator neither considers depreciation or amortisation expense in determining regulatory depreciation nor monitors how regulatory depreciation provides compensation for depreciation or amortisation expense.

IE56 Therefore, Entity A determines that it is unable to track, by amount and reporting period, how regulatory depreciation provides compensation for depreciation or amortisation expense for any IFRS asset class. Entity A makes its determination considering the indicators in paragraphs B67–B68 of IFRS 20 of whether a regulatory capital base has a direct relationship with depreciable or amortisable assets. Entity A concludes that its regulatory capital base does not have a direct relationship with its depreciable and amortisable assets.

Example 5—A change in facts or circumstances or new information that affects only new assets added to the regulatory capital base

IE57 Example 5 illustrates how an entity considers whether a change in facts or circumstances or new information alters the relationship between its regulatory capital base and its depreciable or amortisable assets.

Fact pattern

IE58 Entity A is entitled to an amount of allowed revenue that includes regulatory depreciation of its regulatory capital base. Applying paragraphs B60–B68 of IFRS 20, Entity A has determined that its regulatory capital base has a direct relationship with its depreciable and amortisable assets. Entity A has determined that direct relationship with the assets in each of the asset classes as determined by applying IFRS Accounting Standards (that is, IFRS asset classes).

IE59 In the current period, the regulator changes the terms of the regulatory agreement. The changes relate to the methodology the regulator uses to determine the regulatory capital base in terms of its composition, classes and recovery period. This new methodology affects only those assets added to the regulatory capital base after the new methodology takes effect.

IE60 As a result of the new methodology, a part of the regulatory capital base will include assets that differ substantially from depreciable and amortisable assets Entity A recognises after the changes take effect. The classes in this part of the regulatory capital base will also differ substantially from the IFRS asset classes. Entity A will be unable, on an ongoing basis, to track any differences between the new classes in this part of the regulatory capital base and the IFRS asset classes for the new depreciable and amortisable assets. After the new methodology takes effect, the regulator will determine regulatory depreciation for this part of the regulatory capital base by considering factors unrelated to the depreciation or amortisation of the new depreciable and amortisable assets.

IE61 The regulatory capital base, in effect, consists of two bases: one that includes the assets in the regulatory capital base immediately before the changes to the methodology (the old base that includes old assets) and one that includes the assets added after the changes to the methodology (the new base that includes new assets). The regulator applies:

(a) the old methodology to determine the regulatory depreciation of the old base; and

(b) the new methodology to determine the new base and related regulatory depreciation.

Analysis

IE62 Because the regulator applies different methodologies to each base, Entity A applies paragraph B61 of IFRS 20 to consider whether:

(a) the old base has a direct relationship with the old depreciable or amortisable assets; and

(b) the new base has a direct relationship with the new depreciable or amortisable assets.

IE63 Entity A determines that the changes in the terms of the regulatory agreement do not alter the direct relationship between the old base and the old depreciable and amortisable assets.

IE64 Entity A determines that the classes in the new base differ substantially from the IFRS asset classes. The regulator does not consider the depreciation or amortisation expense of those new depreciable and amortisable assets in determining regulatory depreciation of the new base. Neither does the regulator monitor how regulatory depreciation provides compensation for such depreciation or amortisation expense.

IE65 Entity A determines that it will be unable to track, by amount and reporting period, how regulatory depreciation of the new base provides compensation for the depreciation or amortisation expense of the new depreciable and amortisable assets for any IFRS asset class. Entity A makes its determination considering the indicators in paragraphs B67–B68 of IFRS 20 of whether a regulatory capital base has a direct relationship with depreciable or amortisable assets.

IE66 Therefore, Entity A concludes that:

(a) a part of its regulatory capital base—that is, the old base—has a direct relationship with the old depreciable or amortisable assets in each IFRS asset class.

(b) the remaining part of its regulatory capital base—that is, the new base—does not have a direct relationship with the new depreciable and amortisable assets.

Compensation for allowable expenses and deductions for chargeable income provided or made through regulatory depreciation

IE67 Examples 6A–8 illustrate IFRS 20 requirements for identifying and recognising a regulatory asset or regulatory liability arising from regulatory depreciation that provides compensation for an allowable expense or makes a deduction for chargeable income. Some of these examples also illustrate IFRS 20 requirements for measuring such a regulatory asset or regulatory liability. In these examples, an entity's regulatory capital base has a direct relationship

with its depreciable or amortisable assets, or with related items other than those assets if applicable.

Example 6A—Regulatory recovery period longer than an asset's useful life

IE68 Example 6A illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset arising when the regulatory agreement specifies a recovery period longer than the useful life of a depreciable asset.

Fact pattern

IE69 This example assumes that:

(a) the entity's regulatory capital base has a direct relationship with its depreciable or amortisable assets.

(b) the regulatory capital base consists of only one item of plant.

(c) the entity completed the construction of the item of plant during Year 0, and this item became available for use on the first day of Year 1. The cost of the item of plant was CU1,000, both for regulatory purposes and as determined by applying IAS 16.

(d) the item of plant has a useful life of four years and the entity recognises depreciation expense on a straight-line basis over this period. However, the regulatory agreement entitles the entity to recover the cost of the plant through the regulated rates charged to customers over five years, as shown in Table 6A.1.

(e) the regulatory agreement entitles Entity A to a regulatory return calculated as 8% of the unrecovered balance of the regulatory capital base at the beginning of the year.

IE70 The regulatory agreement entitles Entity A to compensation relating to its regulatory capital base, comprising:

(a) regulatory depreciation—that is, the compensation for the depreciation expense; and

(b) a regulatory return.

IE71 Table 6A.1 shows the regulatory compensation related to the entity's regulatory capital base for Years 1–5. The regulatory compensation is included in determining the regulated rates charged in Years 1–5 and hence in IFRS 15 revenue in the same period.

Table 6A.1—Compensation related to the regulatory capital base						
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory capital base						
Opening balance [A]	1,000	800	600	400	200	**—**
Regulatory depreciation[(a)]	(200)	(200)	(200)	(200)	(200)	**(1,000)**
Closing balance	**800**	**600**	**400**	**200**	**—**	**—**
Compensation related to the regulatory capital base						
Regulatory depreciation	200	200	200	200	200	**1,000**
Regulatory returns = 8% × [A]	80	64	48	32	16	**240**
Regulatory compensation—IFRS 15 revenue	**280**	**264**	**248**	**232**	**216**	**1,240**

(a) The regulatory depreciation in this table reflects the pace of recovery specified in the regulatory agreement.

Analysis

IE72 Entity A considers the types of compensation in paragraph IE70 and applies the requirements in paragraph 19 of IFRS 20 to determine when that compensation forms part of total allowed of compensation. Table 6A.2 shows the total allowed compensation for Years 1–5, which comprises:

(a) regulatory depreciation—applying paragraph B15 of IFRS 20, the regulatory depreciation forms part of the total allowed compensation for the reporting period in which Entity A recognises depreciation expense by applying IAS 16; and

(b) regulatory return—applying paragraph B33 of IFRS 20, the regulatory return forms part of the total allowed compensation for the reporting period in which the rate of return is applied to the regulatory capital base.

Table 6A.2—Total allowed compensation (TAC)						
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory depreciation as part of TAC (paragraph IE72(a))	250	250	250	250	—	**1,000**

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Table 6A.2—Total allowed compensation (TAC)						
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory return as part of TAC (paragraph IE72(b))	80	64	48	32	16	**240**
Total allowed compensation	**330**	**314**	**298**	**282**	**16**	**1,240**
IFRS 15 revenue (Table 6A.1)	280	264	248	232	216	**1,240**
Regulatory income (regulatory expense)	**50**	**50**	**50**	**50**	**(200)**	**—**
Of which:						
Under-recovery: the part of total allowed compensation not yet included in IFRS 15 revenue	50	50	50	50	—	**—**
Regulatory asset[(a)]	50	100	150	200	—	**—**

(a) The regulatory asset arises from regulatory depreciation (see paragraph IE73). Entity A recovers the regulatory asset in Year 5. No differences in timing arise from regulatory returns (see paragraph IE74).

IE73 Regulatory depreciation provides compensation for the depreciation expense. This compensation gives rise to differences in timing because the asset's regulatory recovery period is longer than its useful life, and thus part of the total allowed compensation for regulatory goods or services supplied in Years 1–4 will be included in IFRS 15 revenue in Year 5. Therefore, Entity A recognises a regulatory asset in Year 1. During Years 2–4 the carrying amount of the regulatory asset increases because of an increase in the amount that Entity A is entitled to add in determining the regulated rates to be charged to customers in Year 5.

IE74 The regulatory returns are calculated by applying the rate of return of 8% to the unrecovered balance of the regulatory capital base at the beginning of each of Years 1–5. Regulatory returns are included in the regulated rates charged in each of these years and hence included in IFRS 15 revenue in each of these years. This coincides with the periods when regulatory returns form part of the total allowed compensation (see paragraph IE72(b)). Therefore, no differences in timing arise from the regulatory returns.

IE75 The regulatory asset arises from regulatory depreciation. Entity A measures the regulatory asset by discounting the estimated future cash flows arising from the regulatory asset. The regulatory interest rate for this regulatory asset is the rate of return that the regulatory agreement applies to the regulatory

capital base. Because the regulatory interest rate is also the discount rate, the discounted amount of the regulatory asset in Year 1 equals the sum of the estimated future cash flows excluding the future cash flows from regulatory interest. In subsequent years, the discounted amount will equal the sum of the estimated future cash flows excluding the future cash flows from regulatory interest that has not yet accrued. For example, at the end of Year 4, if the estimated future cash flows are not subject to uncertainty, the discounted amount of the regulatory asset is CU200 (CU216 – CU16) (see Table 6A.3).

IE76 Table 6A.3 shows the reconciliation of the regulatory asset.

Table 6A.3—Reconciliation of the carrying amount of the regulatory asset

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening carrying amount [A]	—	50	100	150	200
Amount recognised	50	50	50	50	—
Regulatory interest income = 8% × [A]	—	4	8	12	16
Amount recovered	—	(4)	(8)	(12)	(216)
Closing carrying amount (Table 6A.2)	**50**	**100**	**150**	**200**	**—**

IE77 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 6A.4.

Table 6A.4—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue[(a)] (Table 6A.1)	280	264	248	232	216	**1,240**
Regulatory income (regulatory expense) (Table 6A.2)	50	50	50	50	(200)	**—**
Total revenue	330	314	298	282	16	**1,240**
Depreciation expense	(250)	(250)	(250)	(250)	—	**(1,000)**
Profit	**80**	**64**	**48**	**32**	**16**	**240**

(a) Example 6A uses the simplifying assumption that Entity A has only one item of plant in its regulatory capital base. A more realistic fact pattern would include several assets in the regulatory capital base. These other assets would be used to supply goods or services to customers in Year 5.

IE78 The profit in each of Years 1–5 reflects the fact that the regulatory agreement entitles Entity A to regulatory returns during Years 1–5.

Example 6B—Regulatory recovery period shorter than an asset's useful life

IE79 Example 6B illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory liability arising when the regulatory agreement specifies a recovery period shorter than the useful life of a depreciable asset.

Fact pattern

IE80 Example 6B assumes the same fact pattern as Example 6A, except that:

(a) the item of plant has a useful life of five years, and Entity A recognises depreciation expense on a straight-line basis over this period; and

(b) the regulatory agreement entitles Entity A to recover the cost of the plant through the regulated rates charged to customers over four years.

IE81 Table 6B.1 shows the regulatory compensation related to the entity's regulatory capital base for Years 1–4. The regulatory compensation is included in determining the regulated rates charged in Years 1–4 and hence in IFRS 15 revenue in the same period. There is no regulatory compensation in Year 5.

Table 6B.1—Compensation related to the regulatory capital base

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory capital base						
Opening balance [A]	1,000	750	500	250	—	**—**
Regulatory depreciation[(a)]	(250)	(250)	(250)	(250)	—	**(1,000)**
Closing balance	**750**	**500**	**250**	**—**	**—**	**—**
Compensation related to the regulatory capital base						
Regulatory depreciation	250	250	250	250	—	**1,000**
Regulatory returns = 8% × [A]	80	60	40	20	—	**200**
Regulatory compensation—IFRS 15 revenue	**330**	**310**	**290**	**270**	**—**	**1,200**

(a) The regulatory depreciation in this table reflects the pace of recovery specified in the regulatory agreement.

Analysis

IE82 Entity A considers the types of compensation in paragraph IE70 and applies the requirements in paragraph 19 of IFRS 20 to determine when that compensation forms part of total allowed compensation. Table 6B.2 shows the total allowed compensation for Years 1–5, which comprises:

(a) regulatory depreciation—applying paragraph B15 of IFRS 20, the regulatory depreciation forms part of the total allowed compensation for the reporting period in which Entity A recognises depreciation expense by applying IAS 16; and

(b) regulatory return—applying paragraph B33 of IFRS 20, the regulatory return forms part of the total allowed compensation for the reporting period in which the rate of return is applied to the regulatory capital base.

Table 6B.2—Total allowed compensation (TAC)

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory depreciation as part of TAC (paragraph IE82(a))	200	200	200	200	200	**1,000**
Regulatory return as part of TAC (paragraph IE82(b))	80	60	40	20	—	**200**
Total allowed compensation	**280**	**260**	**240**	**220**	**200**	**1,200**
IFRS 15 revenue (Table 6B.1)	330	310	290	270	—	**1,200**
Regulatory income (regulatory expense)	**(50)**	**(50)**	**(50)**	**(50)**	**200**	**—**
Of which:						
Over-recovery: the part of total allowed compensation for regulatory goods or services to be supplied in the future already included in IFRS 15 revenue	(50)	(50)	(50)	(50)	—	**—**
Regulatory liability[(a)]	50	100	150	200	—	**—**

(a) The regulatory liability arises from regulatory depreciation (see paragraph IE83). Entity A fulfils the regulatory liability in Year 5. No differences in timing arise from regulatory returns (see paragraph IE84).

IE83 Regulatory depreciation provides compensation for the depreciation expense. This compensation gives rise to differences in timing because the asset's regulatory recovery period is shorter than its useful life, and thus part of the total allowed compensation for regulatory goods or services to be supplied in Year 5 has been included in IFRS 15 revenue for Years 1–4. Therefore, Entity A recognises a regulatory liability in Year 1. During Years 2–4, the carrying amount of the regulatory liability increases because of an increase in the amount that Entity A is obliged to deduct in determining the regulated rates to be charged to customers in Year 5.

IE84 The regulatory returns are calculated by applying the rate of return of 8% on the unrecovered balance of the regulatory capital base at the beginning of each of Years 1–4. Regulatory returns are included in the regulated rates charged in each of these years and hence included in IFRS 15 revenue in each of these years. This coincides with the periods when the regulatory returns form part of the total allowed compensation (see paragraph IE82(b)). Therefore, no difference in timing arises from the regulatory returns.

IE85 The regulatory liability arises from regulatory depreciation. Entity A measures the regulatory liability by discounting the estimated future cash flows arising from the regulatory liability. The regulatory interest rate for this regulatory liability is the rate of return that the regulatory agreement applies to the regulatory capital base. Because the regulatory interest rate is also the discount rate, the discounted amount of the regulatory liability in Year 1 equals the sum of the estimated future cash flows excluding the future cash flows from regulatory interest. In subsequent years, the discounted amount will equal the sum of the estimated future cash flows excluding the future cash flows from regulatory interest that has not yet accrued. For example, at the end of Year 4, if the estimated future cash flows are not subject to uncertainty, the discounted amount of the regulatory liability is CU200 (CU216 – CU16) (see Table 6B.3).

IE86 Table 6B.3 shows the reconciliation of the regulatory liability.

Table 6B.3—Reconciliation of the carrying amount of the regulatory liability

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening carrying amount [A]	—	50	100	150	200
Amount recognised	50	50	50	50	—
Regulatory interest expense = 8% × [A]	—	4	8	12	16
Amount fulfilled	—	(4)	(8)	(12)	(216)
Closing carrying amount (Table 6B.2)	**50**	**100**	**150**	**200**	**—**

IE87 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 6B.4.

Table 6B.4—Statement of financial performance						
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue[(a)] (Table 6B.1)	330	310	290	270	—	**1,200**
Regulatory income (regulatory expense) (Table 6B.2)	(50)	(50)	(50)	(50)	200	**—**
Total revenue	280	260	240	220	200	**1,200**
Depreciation expense	(200)	(200)	(200)	(200)	(200)	**(1,000)**
Profit	**80**	**60**	**40**	**20**	**—**	**200**

(a) IFRS 15 revenue in Year 5 is nil because of the simplifying assumption that Entity A has a single item of plant it recovers over four years in accordance with the regulatory agreement. A more realistic fact pattern would include several assets in the regulatory capital base. These other assets would be used to supply goods or services to customers in Year 5.

IE88 The profit in each of Years 1–4 reflects the fact that the regulatory agreement entitles Entity A to regulatory returns during Years 1–4.

Example 7—Related item other than depreciable or amortisable assets

IE89 Example 7 illustrates IFRS 20 requirements for identifying and recognising a regulatory asset arising when compensation for an allowable expense that does not arise from depreciable or amortisable assets is provided through regulatory depreciation.

Fact pattern

IE90 Entity A applies IFRS Accounting Standards in the current reporting period to recognise an overhead expense that does not arise from depreciable or amortisable assets.

IE91 The regulatory agreement treats that expense as allowable, requires the overhead expense to be added to the regulatory capital base, and compensates Entity A for the overhead expense through the regulatory depreciation of the regulatory capital base in future periods. The entity's regulatory capital base has a direct relationship with related items other than depreciable or amortisable assets.

IE92 The regulator monitors the provision of compensation for the overhead expense through regulatory depreciation separately from other items in the regulatory capital base. The regulator determines the amount of regulatory depreciation related to that expense using a separate depreciation schedule.

Analysis

IE93 Entity A applies paragraphs B60–B63 and B69–B70 of IFRS 20 and determines that it is able to track, by amount and reporting period, how regulatory depreciation provides compensation for the overhead expense. Therefore, Entity A concludes that its regulatory capital base has a direct relationship with this allowable expense.

IE94 Applying paragraph B15 of IFRS 20, the amount of the regulatory depreciation that provides compensation for this allowable expense forms part of the total allowed compensation for the reporting period in which Entity A recognises the allowable expense. Because the regulatory agreement requires Entity A to add this expense to the regulatory capital base, the amount of the regulatory depreciation that provides compensation for the allowable expense will be included in IFRS 15 revenue in the future.

IE95 Entity A recognises as a regulatory asset its enforceable present right to add an amount in determining the regulated rates to be charged to customers in future periods. This amount compensates Entity A for the allowable expense included in its regulatory capital base through regulatory depreciation.

Example 8—Gain on sale of an asset

IE96 Example 8 illustrates IFRS 20 requirements for identifying and recognising a regulatory liability arising when a gain on the sale of a depreciable asset is deducted from an entity's regulatory capital base.

Fact pattern

IE97 A regulatory agreement specifies that Entity A has the right to recover the cost of a depreciable asset over a period that coincides with the asset's useful life determined by applying IFRS Accounting Standards. The entity's regulatory capital base has a direct relationship with its depreciable or amortisable assets.

IE98 In the current reporting period, Entity A recognises a gain on the sale of the asset. The regulatory agreement treats the gain as chargeable income and requires it to be deducted from the regulatory capital base and hence from regulatory depreciation in future periods. The regulatory agreement also requires any outstanding balance of that asset in the regulatory capital base to be eliminated because Entity A will no longer recover that balance through regulatory depreciation.

Analysis

IE99 The gain that Entity A recognised on the sale of the asset during the current reporting period is chargeable income that reduces the total allowed compensation for the reporting period.

IE100 Applying paragraph B22 of IFRS 20, Entity A recognises as a regulatory liability in the current reporting period its enforceable present obligation to deduct the gain on the sale of the asset from regulatory depreciation in future periods.

Compensation for allowable expenses and deductions for chargeable income provided or made separately from regulatory depreciation

IE101 Examples 9–17 illustrate IFRS 20 requirements for identifying and recognising a regulatory asset or regulatory liability arising from compensation for allowable expenses or deductions for chargeable income provided or made separately from regulatory depreciation. Some of these examples also illustrate IFRS 20 requirements for measuring such a regulatory asset or regulatory liability.

Compensation for depreciation expense provided in advance

Example 9—Compensation for part of the construction cost of an asset not yet available for use provided separately from regulatory depreciation

IE102 Example 9 illustrates IFRS 20 requirements for identifying and recognising a regulatory liability arising when:

(a) a regulatory agreement entitles an entity to include part of the compensation for the construction cost of a depreciable asset separately from regulatory depreciation in determining the regulated rates charged to customers during construction; and

(b) the entity's regulatory capital base has a direct relationship with its depreciable or amortisable assets.

Fact pattern

IE103 A regulatory agreement specifies that Entity A is entitled to include an amount that provides compensation for part of the construction cost of a depreciable asset separately from regulatory depreciation in determining the regulated rates charged to customers in the current reporting period. The asset is not yet available for use.

IE104 The regulator does not add the amount that provides compensation for part of the construction cost of the asset to the entity's regulatory capital base because that amount is included in determining the regulated rates charged in the current reporting period. Consequently, the amount reduces the regulatory depreciation that would otherwise provide compensation for part of the depreciation expense for the asset. Entity A's regulatory capital base has a direct relationship with its depreciable or amortisable assets. That is, Entity A is able to track, by amount and reporting period, how regulatory depreciation provides compensation for depreciation expense for the asset, including how compensation for part of the depreciation expense included in

regulated rates charged in the period reduces the regulatory depreciation in future periods.

Analysis

IE105 The amount that provides part of the compensation for the construction cost is included in determining the regulated rates charged in the current reporting period and hence in IFRS 15 revenue in the same period.

IE106 That amount reflects an advance compensation of the depreciation expense that Entity A will recognise in future periods. A difference in timing arises because part of the total allowed compensation for regulatory goods or services that Entity A will supply in the future has already been included in IFRS 15 revenue in the current reporting period.

IE107 Applying paragraph B59 of IFRS 20, Entity A recognises a regulatory liability in the current reporting period. The regulatory liability is an enforceable present obligation to deduct that amount (that is, the amount that compensates part of the future depreciation expense that has already been charged to customers through regulated rates) in determining the regulated rates to be charged to customers in future periods.

Input costs

Example 10—Compensation for an allowable expense (input costs) at an amount that differs from the amount of the expense

IE108 Example 10 illustrates IFRS 20 requirements for identifying and recognising a regulatory asset or regulatory liability arising from compensation for an allowable expense that is determined at an amount that differs from the amount of the expense—for example, using benchmarking techniques.

Fact pattern

IE109 In Year 1, Entity A recognises an expense of CU900 by applying IFRS Accounting Standards.

IE110 The regulatory agreement entitles Entity A to compensation for that expense and specifies that the compensation is determined using benchmarking techniques. The regulator determines that the compensation for the expense for Year 1 is CU1,000. That compensation is included in determining the regulated rates charged and hence in IFRS 15 revenue in the same year.

IE111 The compensation of CU1,000 that is determined using benchmarking techniques comprises:

(a) recovery of the allowable expense recognised in Year 1 of CU900; and

(b) an efficiency gain of CU100, calculated as the difference between the compensation and the allowable expense recognised in Year 1 (CU1,000 – CU900).

IE112 The regulatory agreement requires that the efficiency gain of CU100 is shared between:

(a) Entity A at 60%—that is, Entity A is entitled to benefit from an amount of CU60 (60% of CU100); and

(b) customers at 40%—that is, Entity A has an enforceable present obligation to deduct an amount of CU40 (40% of CU100) in determining the regulated rates to be charged in Year 3.

IE113 Entity A also recognises input costs of CU500 as an expense and the related compensation as IFRS 15 revenue during Years 1–3.

IE114 The regulatory agreement does not specify an interest rate for the regulatory liability arising in Year 1.

Analysis

IE115 Applying paragraph B15 of IFRS 20, Entity A determines that the compensation for the allowable expense recognised in Year 1 forms part of the total allowed compensation for the same year. Therefore, no difference in timing arises from the amount of the compensation that relates to Entity A's allowable expense recognised of CU900 and its share of the efficiency gain of CU60. Entity A:

(a) applies paragraph B26 of IFRS 20 and determines that the amount of CU60 is a measurement difference that will not reverse over time; and

(b) reflects the measurement difference in the statement of financial performance in the period in which Entity A recognises the IFRS 15 revenue and the related allowable expense—that is, in Year 1.

IE116 The remaining amount of the compensation of CU40 is the customers' share of the efficiency gain that will be deducted in determining the regulated rates for Year 3. A difference in timing arises because part of the total allowed compensation for regulatory goods or services to be supplied in Year 3 has already been included in IFRS 15 revenue in Year 1.

IE117 Applying paragraph 26 of IFRS 20, Entity A recognises a regulatory liability and regulatory expense at the end of Year 1. Applying paragraph 48 of IFRS 20, Entity A concludes that the regulatory interest rate is nil. Therefore, Entity A measures the regulatory liability using a discount rate of 0%. In Year 3, Entity A fulfils the regulatory liability by deducting CU40 from regulated rates charged to customers and hence from IFRS 15 revenue. Therefore, in Year 3 Entity A also derecognises the regulatory liability and recognises regulatory income of CU40.

IE118 Entity A's statement of financial performance for Years 1–3 is shown in Table 10.1.

Table 10.1—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Total**
IFRS 15 revenue[(a)]	1,500	500	460	**2,460**
Regulatory income (regulatory expense)	(40)	—	40	**—**
Total revenue	1,460	500	500	**2,460**
Input costs	(500)	(500)	(500)	**(1,500)**
Other expense	(900)	—	—	**(900)**
Profit	**60**	**—**	**—**	**60**

(a) IFRS 15 revenue for all years includes compensation for input costs of CU500. In addition, (i) IFRS 15 revenue in Year 1 includes compensation of CU1,000 for an allowable expense determined using benchmarking techniques; and (ii) IFRS 15 revenue in Year 3 includes a deduction of CU40 relating to the fulfilment of the regulatory liability recognised in Year 1.

Borrowing costs

Example 11—Compensation for borrowing costs provided separately from regulatory returns

IE119 Example 11 illustrates IFRS 20 requirements for identifying and recognising a regulatory asset or regulatory liability arising from compensation for borrowing costs provided separately from regulatory returns on an entity's regulatory capital base.

Fact pattern

IE120 Entity A starts construction of an item of property, plant and equipment (the asset) on the first day of Year 1 and completes construction on the last day of Year 2. Entity A incurs construction costs of CU5,000 evenly over each of Years 1–2 (that is, total construction costs of CU10,000). Entity A also incurs borrowing costs at an interest rate of 3%, which the entity capitalises in accordance with IAS 23 *Borrowing Costs*. The asset is available for use on the first day of Year 3 and has a useful life of three years. Entity A recognises depreciation expense as determined by applying IAS 16 using the straight-line method over Years 3–5.

IE121 The regulatory agreement provides Entity A with regulatory returns consisting of an equity return on the regulatory capital base. The regulatory capital base includes the construction costs of the asset not yet available for use. The regulatory agreement also provides compensation specifically for borrowing costs Entity A incurs in a reporting period, including borrowing costs capitalised as part of the cost of the asset. That compensation is provided through a component of the compensation separate from both the regulatory returns and the regulatory depreciation of the regulatory capital base. Compensation for borrowing costs is determined using an estimate of the borrowing costs for the period and is included in determining the regulated rates charged and hence in IFRS 15 revenue in the same period. Any difference

between the estimated and actual amounts of borrowing costs for a period is not added or deducted in determining the regulated rates charged in future periods. For simplicity, this example assumes that:

(a) Entity A incurs borrowing costs only for the construction of the asset and capitalises those borrowing costs during Years 1–2;

(b) Entity A finances the construction of the asset entirely with borrowings and repays the borrowings when the construction is complete;

(c) Entity A recovers the cost of the asset through the regulatory depreciation of the regulatory capital base evenly over the asset's useful life; and

(d) the regulator uses estimated borrowing costs of CU96 for Year 1 and CU224 for Year 2 in determining the compensation for those costs.

IE122 Table 11.1 shows the compensation included in regulated rates for borrowing costs and the capitalised borrowing costs.

Table 11.1—Amounts included in regulated rates and capitalised borrowing costs

In CU	**Year 1**	**Year 2**	**Total**
Compensation included in regulated rates for borrowing costs	96	224	**320**
Capitalised borrowing costs[(a)]	81	234	**315**
Difference	**15**	**(10)**	**5**

(a) For simplicity, capitalised borrowing costs are calculated: (a) for Year 1 at [(CU5,000 + (CU5,000 ÷ 12)) ÷ 2] × 3%; and (b) for Year 2 at {CU5,081 + [(CU5,000 + (CU5,000 ÷ 12)) ÷ 2]} × 3%.

Analysis

IE123 In this example:

(a) the regulatory returns on the regulatory capital base consist of only an equity return. Entity A applies paragraph B33 of IFRS 20 to account for the regulatory returns on the regulatory capital base. The regulatory returns form part of the total allowed compensation for the reporting period in which the regulatory agreement applies the rate of return to the regulatory capital base. Therefore, no difference in timing arises from the regulatory returns during Years 1–2.

(b) the compensation relates specifically to borrowing costs that Entity A has capitalised—that is, compensation for an allowable expense. Entity A applies paragraphs B18–B19 of IFRS 20 to account for that compensation. The compensation for borrowing costs is provided through a component of compensation separate from regulatory depreciation of the regulatory capital base. Therefore, the recognition of a regulatory asset or regulatory liability arising from that

compensation does not depend on Entity A's regulatory capital base having a direct relationship with its depreciable and amortisable assets.

IE124 Applying paragraph B15 of IFRS 20, Entity A determines that the compensation for borrowing costs forms part of the total allowed compensation for the reporting period in which the entity recognises borrowing costs as an expense—that is, the period in which the borrowing costs are included as part of the depreciation expense for the asset. A difference in timing arises during Years 1–2 because the amounts included in the regulated rates charged—and hence in IFRS 15 revenue—provide compensation for capitalised borrowing costs that will be included as part of depreciation expense over the asset's useful life (Years 3–5).

IE125 Therefore, Entity A recognises a regulatory liability and regulatory expense of CU320 arising from the compensation for borrowing costs during Years 1–2. Entity A fulfils the regulatory liability and recognises regulatory income during Years 3–5. Applying paragraph B26 of IFRS 20, Entity A determines that the difference between the compensation of CU320 and the borrowing costs of CU315 is a measurement difference (see Table 11.1). Entity A reflects the measurement difference in the statement of financial performance in the periods it recognises regulatory income as the regulatory liability is fulfilled and the borrowing costs as part of depreciation expense—that is, in Years 3–5.

IE126 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 11.2.

Table 11.2—Statement of financial performance

	Construction		Operation			
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue (excluding regulatory equity returns)	96	224	3,334	3,333	3,333	**10,320**
Regulatory income (regulatory expense)	(96)	(224)	106	107	107	**—**
Total revenue	—	—	3,440	3,440	3,440	**10,320**
Depreciation expense	—	—	(3,439)	(3,438)	(3,438)	**(10,315)**
Profit[(a)]	**—**	**—**	**1**	**2**	**2**	**5**

(a) For Years 3–5, the profit represents the measurement difference between the compensation for borrowing costs (regulatory income arising from fulfilment of the regulatory liability) and the capitalised borrowing costs (included in depreciation expense—see paragraph IE125).

Pensions

Example 12A—Compensation for pension costs that affect regulated rates only when an entity pays the related cash

IE127 Example 12A illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset arising from compensation for the costs related to a net defined benefit (pension) liability. The regulatory agreement provides compensation for pension costs in determining the regulated rates only when an entity pays the related cash.

Fact pattern

IE128 The regulatory agreement entitles Entity A to recover pension costs it incurs for a group of employees. Entity A operates an unfunded pension plan for this group of employees and pays benefits to those employees when the benefits fall due. The regulatory agreement provides Entity A compensation for the pension costs in determining the regulated rates only when the entity pays the benefits and settles its obligations under the plan.

IE129 In Year 1, Entity A estimates that the services those employees render in Years 1–3 will lead to an obligation to pay benefits of CU1,500 at the end of each of Years 4–5. For simplicity, this example assumes that:

(a) the estimated and actual benefits paid are the same; and

(b) no gains or losses arise from remeasurement of the pension liability applying IAS 19 *Employee Benefits* during Years 1–5.

IE130 Table 12A.1 shows the pension liability and the related amounts to be included in regulated rates.

Table 12A.1—Pension liability

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Opening carrying amount	—	902	1,858	2,870	1,456	**—**
Service cost	902	929	956	—	—	**2,787**
Interest cost[(a)]	—	27	56	86	44	**213**
Benefits paid	—	—	—	(1,500)	(1,500)	**(3,000)**
Closing carrying amount	**902**	**1,858**	**2,870**	**1,456**	**—**	**—**
Amounts included in regulated rates—IFRS 15 revenue	**—**	**—**	**—**	**1,500**	**1,500**	**3,000**

(a) Calculated using a discount rate of 3%.

Analysis

IE131 Applying paragraph B15 of IFRS 20, compensation for pension expenses recognised in a reporting period forms part of the total allowed compensation for that period. Differences in timing arise because Entity A will include compensation for the items of expense related to the pension liability recognised in Years 1–5 in the regulated rates charged—and hence in IFRS 15 revenue—only when it pays the benefits under the plan in Years 4–5.

IE132 Therefore, Entity A accounts for a regulatory asset during Years 1–5. The regulatory asset will be recovered over Years 4–5.

IE133 Applying paragraph 60 of IFRS 20, Entity A measures the regulatory asset using the carrying amount of the related pension liability resulting from applying IAS 19. This example assumes that the carrying amounts of the regulatory asset and the pension liability are the same, both at initial recognition of the regulatory asset and subsequently.

IE134 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 12A.2.

Table 12A.2—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue (Table 12A.1)	—	—	—	1,500	1,500	**3,000**
Regulatory income (regulatory expense)	902	956	1,012	(1,414)	(1,456)	**—**
Total revenue	902	956	1,012	86	44	**3,000**
Service cost	(902)	(929)	(956)	—	—	**(2,787)**
Finance cost	—	(27)	(56)	(86)	(44)	**(213)**
Profit	**—**	**—**	**—**	**—**	**—**	**—**

IE135 The profit of nil in each of Years 1–5 depicts the fact that the compensation for pension costs allows Entity A to recover the pension costs it incurs for the group of employees in supplying regulatory goods or services during Years 1–5.

IE136 Table 12A.3 shows the reconciliation of the regulatory asset.

Table 12A.3—Reconciliation of the carrying amount of the regulatory asset

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening carrying amount	—	902	1,858	2,870	1,456
Amount recognised	902	929	956	—	—
Regulatory interest income[(a)]	—	27	56	86	44

continued...

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Table 12A.3—Reconciliation of the carrying amount of the regulatory asset					
Amount recovered	—	—	—	(1,500)	(1,500)
Closing carrying amount	**902**	**1,858**	**2,870**	**1,456**	**—**

(a) Regulatory interest income is calculated as 3% on the carrying amount of the regulatory asset at the beginning of the year. The interest of 3% is the discount rate used for the pension liability. The amount of regulatory interest income is the same as the amount of interest cost of the pension liability (Table 12A.1).

Example 12B—Compensation for pension costs that affect regulated rates based on estimates of cash payments

IE137 Example 12B illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset and for presenting related regulatory income or regulatory expense arising from compensation for pension costs. The regulatory agreement provides compensation for pension costs in determining the regulated rates charged for a period based on estimates of cash payments for that period. The regulatory agreement prohibits any differences between the estimated and actual cash payments from being added or deducted in determining future regulated rates.

Fact pattern

IE138 Example 12B assumes the same fact pattern as Example 12A, except that the regulatory agreement specifies that the pension costs to be included in determining the regulated rates are based on estimates of benefit payments and there are differences between the estimated and the actual amounts.

IE139 In Year 1, Entity A estimates that it will pay benefits of CU1,500 at the end of each of Years 4–5. The regulator approves these amounts to be included in determining the regulated rates to be charged in Years 4–5. Entity A pays benefits of CU1,600 at the end of Year 4 and updates the estimated benefit payments for Year 5 to CU1,700. This example assumes that the estimated and actual benefit payments at the end of Year 5 are the same—that is, CU1,700. The regulatory agreement prohibits Entity A from adding or deducting any differences between the estimated benefit payments and the actual benefit payments in determining future regulated rates.

IE140 Table 12B.1 shows the pension liability and the related amounts to be included in regulated rates.

Table 12B.1—Pension liability

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Opening carrying amount	—	902	1,858	2,870	1,650	**—**
Service cost	902	929	956	—	—	**2,787**
Interest cost[(a)]	—	27	56	86	50	**219**
Remeasurement loss	—	—	—	294	—	**294**
Benefits paid	—	—	—	(1,600)	(1,700)	**(3,300)**
Closing carrying amount	**902**	**1,858**	**2,870**	**1,650**	**—**	**—**
Amounts included in regulated rates—IFRS 15 revenue	**—**	**—**	**—**	**1,500**	**1,500**	**3,000**

(a) Calculated using a discount rate of 3%.

Analysis

IE141 As in Example 12A, Entity A accounts for a regulatory asset during Years 1–5. The regulatory asset will be recovered over Years 4–5.

IE142 Applying paragraph 60 of IFRS 20, Entity A measures the regulatory asset using the carrying amount of the related pension liability resulting from applying IAS 19. In Years 1–3, the carrying amounts of the regulatory asset and the pension liability are the same.

IE143 In Years 4–5, Entity A reduces the carrying amount of the pension liability to reflect the actual benefit payments. Applying IAS 19, Entity A:

(a) accounts for the effects of the differences between the estimated and actual benefit payments on the carrying amount of the pension liability as a remeasurement loss that is included in other comprehensive income; and

(b) will not reclassify the remeasurement loss to the statement of profit or loss in a subsequent period.

IE144 Entity A measures the regulatory asset in Years 4–5 using the carrying amount of the pension liability but adjusts that carrying amount to reflect differences between the estimated and actual benefit payments. This is because the regulatory agreement provides Entity A compensation for pension costs based on estimated benefit payments. Entity A does not have a right to compensation for the remeasurement loss and the additional finance costs of the pension liability arising in Years 4–5. Therefore, no regulatory income

results from the differences between the estimated and actual benefit payments.

IE145 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 12B.2.

Table 12B.2—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue (Table 12B.1)	—	—	—	1,500	1,500	**3,000**
Regulatory income (regulatory expense)	902	956	1,012	(1,414)	(1,456)	**—**
Total revenue	902	956	1,012	86	44	**3,000**
Service cost	(902)	(929)	(956)	—	—	**(2,787)**
Finance cost	—	(27)	(56)	(86)	(50)	**(219)**
Profit/(loss)	**—**	**—**	**—**	**—**	**(6)**	**(6)**
Regulatory income (regulatory expense)	—	—	—	—	—	**—**
Remeasurement loss	—	—	—	(294)	—	**(294)**
Other comprehensive income	**—**	**—**	**—**	**(294)**	**—**	**(294)**
Total comprehensive income	**—**	**—**	**—**	**(294)**	**(6)**	**(300)**
Representing:						
Remeasurement loss	—	—	—	(294)	—	**(294)**
Finance cost unrecovered	—	—	—	—	(6)	**(6)**
Difference	**—**	**—**	**—**	**(294)**	**(6)**	**(300)**

IE146 The profit or loss for each of Years 1–5 reflects the fact that the compensation for pension costs allows Entity A to recover the pension costs it incurs in supplying regulatory goods or services during Years 1–5 using the estimates of benefit payments. Differences between the estimated and actual benefit payments give rise to differences between the compensation for pension costs of CU3,000 and the related expense of CU3,300 during Years 4–5. Differences between the compensation and the pension expenses arise in the periods in which Entity A recognises the remeasurement loss of the pension liability and the additional finance cost of the pension liability. Entity A determines that those differences are measurement differences by applying paragraph B26 of IFRS 20 and reflects the measurement differences in Years 4–5.

IE147 Table 12B.3 shows the reconciliation of the regulatory asset.

Table 12B.3—Reconciliation of the carrying amount of the regulatory asset

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening carrying amount	—	902	1,858	2,870	1,456
Amount recognised[(a)]	902	929	956	—	—
Regulatory interest income[(b)]	—	27	56	86	44
Amount recovered	—	—	—	(1,500)	(1,500)
Closing carrying amount	**902**	**1,858**	**2,870**	**1,456**	**—**

(a) For Years 1–3, the amount recognised is calculated as the service cost recognised. For Years 4–5, no amount is recognised because the remeasurement loss and the additional finance costs are not recoverable (Table 12B.2).

(b) Regulatory interest income is calculated as 3% on the carrying amount of the regulatory asset at the beginning of the year. The interest of 3% is the discount rate used for the pension liability.

Example 13—Compensation for pension costs that affect regulated rates based on the related item of expense or income determined by applying IFRS Accounting Standards

IE148 Example 13 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset and for presenting related regulatory income or regulatory expense arising from compensation for pension costs provided by a regulatory agreement. The regulatory agreement determines the compensation for pension costs based on the related item of expense or income determined by applying IFRS Accounting Standards.

Fact pattern

IE149 Entity A operates an unfunded pension plan for a group of employees and pays benefits to those employees when the benefits fall due. On the first day of Year 1, Entity A estimates that the services this group of employees render in Years 1–3 will lead to an obligation to pay benefits of CU15,000 at the end of each of Years 4–5. Entity A measures the pension liability by applying IAS 19. During Years 2–5, Entity A recognises a remeasurement gain or loss arising from changes in the discount rate used to measure the pension liability. For simplicity, this example assumes no other remeasurement gains or losses arise from the pension liability.

IE150 The regulatory agreement entitles Entity A to compensation for pension costs for a period based on the related expense or income it recognises in that period by applying IAS 19, with a two-year time lag. The regulatory agreement does not specify an interest rate for a regulatory asset or regulatory liability that arises from compensation for pension costs.

IE151 Table 13.1 shows the pension liability and the related amounts to be included in regulated rates.

Table 13.1—Pension liability

In CU	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Total
Opening carrying amount	—	8,942	18,245	28,291	14,493	—	—	**—**
Service cost	8,942	9,123	9,430	—	—	—	—	**27,495**
Interest cost	—	330	725	998	472	—	—	**2,525**
Remeasurement (gain) or loss	—	(150)	(109)	204	35	—	—	**(20)**
Benefits paid	—	—	—	(15,000)	(15,000)	—	—	**(30,000)**
Closing carrying amount	**8,942**	**18,245**	**28,291**	**14,493**	**—**	**—**	**—**	**—**
Amounts included in regulated rates —IFRS 15 revenue[(a)]	**—**	**—**	**8,942**	**9,303**	**10,046**	**1,202**	**507**	**30,000**

(a) The amounts included in determining the regulated rates comprise service cost, interest cost and remeasurement gain or loss.

Analysis

IE152 Entity A is entitled to compensation for allowable expenses—that is, the pension expenses recognised by applying IAS 19. Applying paragraph B15 of IFRS 20, compensation for pension expenses recognised in a reporting period forms part of the total allowed compensation for that period. The regulatory agreement entitles Entity A to include the compensation for pension expenses recognised in a reporting period in regulated rates charged with a two-year time lag. Therefore, a difference in timing arises from the compensation related to pension expenses.

IE153 Applying paragraphs 34–51 of IFRS 20, Entity A measures the related regulatory asset arising in Years 1–5. The regulatory agreement does not specify an interest rate for the regulatory asset. Applying paragraph 48 of IFRS 20, Entity A concludes that the regulatory interest rate is nil. Therefore, Entity A measures the regulatory asset using a discount rate of 0%.

IE154 In its statement of financial performance, applying IAS 19, Entity A includes the remeasurement gain or loss in other comprehensive income and will not reclassify the remeasurement gain or loss to the statement of profit or loss in a subsequent period. Applying paragraph 64 of IFRS 20, Entity A includes in other comprehensive income any regulatory expense or regulatory income related to the recognition of the remeasurement gain or loss. Entity A will not reclassify the regulatory expense or regulatory income included in other comprehensive income to the statement of profit or loss. As Entity A recovers the pension expenses through the regulated rates charged over Years 3–7, the

entity derecognises the regulatory asset and presents the related regulatory expense in the statement of profit or loss.

IE155 Assuming no other transactions take place in Years 1–7, Entity A's statement of financial performance for these years is shown in Table 13.2.

Table 13.2—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Year 6**	**Year 7**	**Total**
IFRS 15 revenue (Table 13.1)	—	—	8,942	9,303	10,046	1,202	507	**30,000**
Regulatory income (regulatory expense)	8,942	9,453	1,213	(8,305)	(9,574)	(1,202)	(507)	**20**
Total revenue	8,942	9,453	10,155	998	472	—	—	**30,020**
Service cost	(8,942)	(9,123)	(9,430)	—	—	—	—	**(27,495)**
Finance cost	—	(330)	(725)	(998)	(472)	—	—	**(2,525)**
Profit	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Regulatory income (regulatory expense)	—	(150)	(109)	204	35	—	—	**(20)**
Remeasurement gain or (loss)	—	150	109	(204)	(35)	—	—	**20**
Other comprehensive income	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Total comprehensive income	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**

IE156 Table 13.3 shows the reconciliation of the regulatory asset.

Table 13.3—Reconciliation of the carrying amount of the regulatory asset

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Year 6**	**Year 7**
Opening carrying amount	—	8,942	18,245	19,349	11,248	1,709	507
Amount recognised	8,942	9,303	10,046	1,202	507	—	—
Amount recovered	—	—	(8,942)	(9,303)	(10,046)	(1,202)	(507)
Closing carrying amount	**8,942**	**18,245**	**19,349**	**11,248**	**1,709**	**507**	**—**

Provisions

Example 14—Compensation for environmental costs that affect regulated rates only when an entity pays the related cash

IE157 Example 14 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset arising from compensation for environmental clean-up costs provided by a regulatory agreement in determining the regulated rates when the entity pays the related cash in a future period.

Fact pattern

IE158 In the current reporting period, Entity A incurs an obligation for environmental clean-up costs and, therefore, recognises a provision by applying IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Entity A also recognises expenses:

(a) on recognition of the provision—for the environmental clean-up costs, measured at present value; and

(b) subsequently—for the finance cost arising from the unwinding of the discount.

IE159 The regulatory agreement gives Entity A the right to add the environmental clean-up costs and the finance cost in determining the regulated rates only when it pays the related cash in a future period.

Analysis

IE160 Applying paragraph B15 of IFRS 20, the compensation for the environmental clean-up costs and the finance cost that Entity A recognises as an expense in a reporting period forms part of the total allowed compensation for the same period. Because the compensation for these costs will affect regulated rates only when Entity A pays the related cash in a future period, this part of the total allowed compensation for regulatory goods or services already supplied has not yet been included in IFRS 15 revenue.

IE161 Applying paragraph 26 of IFRS 20, Entity A recognises as a regulatory asset its enforceable present right to add the compensation for these costs in determining the regulated rates to be charged to customers in future periods. Applying paragraph 60 of IFRS 20, Entity A measures this regulatory asset by:

(a) using the carrying amount of the provision resulting from applying IAS 37; and

(b) adjusting that carrying amount to reflect any differences between the provision and the regulatory asset (for example, uncertainty present in the regulatory asset but not present in the provision).

Example 15—Compensation for decommissioning costs that affect regulated rates based on the related item of expense determined by applying another accounting framework

IE162 Example 15 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory liability arising from compensation for decommissioning costs provided by a regulatory agreement in determining the regulated rates based on the related item of expense determined by applying another accounting framework.

Fact pattern

IE163 Entity A has an asset that becomes available for use on the last day of Year 1. Entity A accounts for the asset as an item of property, plant and equipment by applying IAS 16. The asset has a five-year useful life and is depreciated on a straight-line basis. Entity A has an obligation to decommission the asset at the end of Year 6. Entity A estimates it will settle the provision at the end of Year 6 for CU10,000.

IE164 Applying IAS 37, Entity A recognises a decommissioning provision at the end of Year 1. It measures the provision by discounting the estimated decommissioning cost of CU10,000 to its present value using a discount rate of 5% (determined by applying IAS 37). The present value of the estimated decommissioning costs is CU7,835. Applying IAS 16, Entity A recognises the present value of the decommissioning costs as part of the cost of the asset.

IE165 The regulatory agreement provides Entity A compensation for decommissioning costs and specifies that decommissioning expense is an allowable expense. The regulator does not include the decommissioning costs in Entity A's regulatory capital base. Therefore, the compensation for these costs is provided separately from regulatory depreciation of the regulatory capital base.

IE166 In particular, the regulatory agreement determines the compensation for the decommissioning expense for a reporting period based on amounts determined by applying an accounting framework different from IFRS Accounting Standards, comprising:

(a) an amount of depreciation expense for that period related to the decommissioning costs included as part of the cost of the asset; and

(b) an amount of the financing expense arising from the unwinding of the discount for that period.

IE167 At initial recognition of the decommissioning provision, the measurement of the provision determined by applying the other accounting framework and IFRS Accounting Standards is the same. The compensation for the decommissioning expense determined for a reporting period by applying the other accounting framework is included in determining the regulated rates charged and hence in IFRS 15 revenue in the same period.

IE168 Table 15.1 shows the regulatory compensation for Years 2–6.

Table 15.1—Regulatory compensation

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Year 6**	**Total**
Present value of provision at 5%	7,835	8,227	8,638	9,070	9,524	10,000	
Financing expense from unwinding of the discount [A]	—	392	411	432	454	476	**2,165**
Property, plant and equipment	7,835	6,268	4,701	3,134	1,567	—	
Depreciation expense [B]	—	1,567	1,567	1,567	1,567	1,567	**7,835**
Regulatory compensation [A] + [B]	**—**	**1,959**	**1,978**	**1,999**	**2,021**	**2,043**	**10,000**

IE169 Applying IAS 37, Entity A remeasures the provision at the end of Year 2 to reflect a change in the current market-based discount rate from 5% to 9%. The estimated decommissioning costs at the end of Year 2 remain the same. The present value of the provision at the end of Year 2 using a discount rate of 9% is CU7,083—that is, CU1,144 lower than CU8,227 determined using the discount rate for the provision at initial recognition of 5% (see Table 15.1). Applying IFRIC 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, Entity A also reduces the carrying amount of the asset by CU1,144. Therefore, Entity A measures the asset at CU5,124 at the end of Year 2.

IE170 The remeasurement of the provision at the end of Year 2 also affects the depreciation expense and the financing expense Entity A recognises in Years 3–6. For simplicity, this example assumes that the estimated decommissioning costs and the discount rate remain the same during Years 3–6.

IE171 The other accounting framework does not require an entity to update the discount rate used to measure the provision for changes in market interest rates. Consequently, as shown in Table 15.2, a difference in timing (a regulatory liability) arises from the compensation for decommissioning costs. The regulatory agreement does not specify an interest rate for regulatory assets or regulatory liabilities arising from these differences.

Table 15.2—Difference in timing						
In CU	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Year 6**	**Total**
Present value of provision at 9%	7,083	7,721	8,416	9,174	10,000	
Financing expense from unwinding of the discount (IFRS Accounting Standards)		638	695	758	826	**2,917**
Property, plant and equipment	5,124	3,843	2,562	1,281	—	
Depreciation expense (IFRS Accounting Standards)		1,281	1,281	1,281	1,281	**5,124**
Regulatory compensation—IFRS 15 revenue (Table 15.1) [A]	**1,959**	**1,978**	**1,999**	**2,021**	**2,043**	**10,000**
Financing expense from unwinding of the discount (IFRS Accounting Standards)	392	638	695	758	826	**3,309**
Depreciation expense (IFRS Accounting Standards)	1,567	1,281	1,281	1,281	1,281	**6,691**
Total decommissioning expense (IFRS Accounting Standards) [B]	**1,959**	**1,919**	**1,976**	**2,039**	**2,107**	**10,000**
Difference [A] – [B]	**—**	**59**	**23**	**(18)**	**(64)**	**—**
Regulatory liability	**—**	**59**	**82**	**64**	**—**	

Analysis

IE172 Differences arise between:

(a) the amount of regulatory compensation (determined by applying the other accounting framework in accordance with the regulatory agreement) included in the regulated rates Entity A charges in a period; and

(b) the amount of decommissioning expense (comprising depreciation expense and financing expense) Entity A recognises in that period by applying IFRS Accounting Standards.

IE173 Those differences will reverse over time because the total amount of decommissioning expense Entity A recognises for Years 2–6 is the same as the total IFRS 15 revenue the entity recognises for the regulatory compensation for those years. Therefore, those differences are differences in timing as

described in paragraph B29 of IFRS 20, not measurement differences as described in paragraph B26 of IFRS 20.

IE174 In Year 3, the IFRS 15 revenue recognised for the regulatory compensation determined by applying the other accounting framework is higher than the decommissioning expense Entity A recognised by applying IFRS Accounting Standards. Therefore, a regulatory liability of CU59 arises because part of the total allowed compensation for regulatory goods or services to be supplied in the future has already been included in IFRS 15 revenue. The carrying amount of the regulatory liability increases in Year 4 for the same reason. Entity A fulfils the regulatory liability during Years 5–6 because the decommissioning expense the entity recognises is higher than the IFRS 15 revenue the entity recognises for the regulatory compensation.

IE175 Applying paragraphs 34–51 of IFRS 20, Entity A measures the regulatory liability arising in Year 3. The regulatory agreement does not specify an interest rate for the regulatory liability. Applying paragraph 48 of IFRS 20, Entity A concludes that the regulatory interest rate is nil. Therefore, Entity A measures the regulatory liability using a discount rate of 0%.

Taxes

Example 16—Compensation for income taxes that affect regulated rates only when an entity pays the related cash

IE176 Example 16 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset arising from compensation for income tax expense provided by a regulatory agreement in determining the regulated rates when the entity pays the related cash in a future period.

Fact pattern

IE177 Entity A recognises a deferred tax liability and deferred tax expense arising from an asset in the current reporting period by applying IAS 12 *Income Taxes*. The regulatory agreement provides Entity A compensation for the income tax expense in determining the regulated rates charged to customers when the entity has paid the related cash.

Analysis

IE178 Applying paragraph B15 of IFRS 20, the compensation for the tax expense recognised in the current reporting period forms part of the total allowed compensation for the same period. Because the compensation will affect regulated rates only when Entity A pays the related cash in a future period, this part of the total allowed compensation for regulatory goods or services already supplied has not yet been included in IFRS 15 revenue.

IE179 Applying paragraph 26 of IFRS 20, Entity A recognises as a regulatory asset its enforceable present right to add the compensation for the tax expense recognised in the current reporting period in determining the regulated rates to be charged to customers in future periods.

Applying paragraph 60 of IFRS 20, Entity A measures this regulatory asset by:

(a) using the carrying amount of the deferred tax liability resulting from applying IAS 12; and

(b) adjusting that carrying amount to reflect any differences between the deferred tax liability and the regulatory asset (for example, uncertainty present in the regulatory asset but not present in the deferred tax liability).

Example 17—Compensation for income taxes that affect regulated rates based on amounts recognised as expense or income by applying IAS 12

IE180 Example 17 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset or regulatory liability arising from compensation for income taxes based on the related expense or income the entity recognises by applying IAS 12.

Fact pattern

IE181 The regulatory agreement entitles Entity A to compensation for income taxes. The regulatory agreement determines compensation for income taxes for a period based on the current tax expense for that period. The tax law specifies that taxable profit for a period includes IFRS 15 revenue for that period and that the tax rate is 40%.

IE182 In Year 1, Entity A's performance results in a performance penalty of CU60. The regulatory agreement makes a deduction for the penalty in determining the regulated rates Entity A charges in Year 2. A deduction from the regulated rates charged—and hence from IFRS 15 revenue—in a period reduces taxable profit for that period, resulting in current tax income (see paragraph IE181). Consequently, a deduction for the penalty from the regulated rates Entity A charges in Year 2 results in another deduction for current tax income from the regulated rates in that year. In summary, the regulatory agreement makes a deduction for both the penalty and the tax effects of the deduction for the penalty.

IE183 The regulatory agreement does not specify an interest rate for a regulatory liability that arises from performance penalties or compensation for income taxes.

Analysis

IE184 Applying paragraph B42 of IFRS 20, Entity A determines that the penalty reduces the total allowed compensation for the reporting period in which its performance occurs—that is, Year 1. A difference in timing arises in Year 1 because the penalty will be deducted in determining the regulated rates charged for Year 2. Therefore, Entity A recognises a regulatory liability and regulatory expense of CU60 in Year 1.

IE185 Applying paragraph B25 of IFRS 20, Entity A applies IAS 12 to account for differences between the carrying amount of the regulatory liability and its tax base.

Applying IAS 12, Entity A:

(a) determines that the regulatory liability has a tax base of zero, resulting in a deductible temporary difference; and

(b) recognises a deferred tax asset and deferred tax income of CU24 (CU60 × 40%) in Year 1.

IE186 Applying paragraphs B23–B25 of IFRS 20, Entity A determines that the deferred tax income of CU24 it recognises in Year 1 reduces the total allowed compensation for that year. However, the deferred tax income will be deducted in determining the regulated rates only when the related current tax income is recognised—that is, in Year 2. Therefore, the deferred tax income gives rise to another regulatory liability—that is, a regulatory liability of CU24 arising from the tax effects of the regulatory liability related to the penalty. Applying IAS 12, this regulatory liability also results in a deductible temporary difference. That deductible temporary difference results in an additional amount of deferred tax asset and deferred tax income that gives rise to an additional amount of regulatory liability in successive iterations.

IE187 In Year 1, Entity A recognises a regulatory liability and regulatory expense of CU40 (CU24 ÷ (1 – 40%)) arising from the tax effects of the regulatory liability related to the penalty. The amount of CU40 is the grossed up amount that includes the deduction for the tax effects of the regulatory liability related to the deferred tax income, measured initially at CU24 (see paragraph IE186). Entity A also increases the carrying amount of the deferred tax asset by CU16 (CU40 × 40%) by applying IAS 12.

IE188 The regulator makes deductions of CU100 when determining the regulated rates to be charged in Year 2. Hence, IFRS 15 revenue Entity A recognises in Year 2 includes these deductions, comprising:

(a) an amount of CU60 for the penalty (see paragraph IE184); and

(b) an amount of CU40 (CU24 + CU16) for the related tax effects (see paragraphs IE185 and IE187).

IE189 Therefore, Entity A fulfils the regulatory liabilities related to the penalty and income taxes in Year 2. Entity A also recognises the resulting regulatory income of CU100. Applying IAS 12, Entity A:

(a) recognises current tax income of CU40 (CU100 × 40%) arising from the deductions from IFRS 15 revenue; and

(b) derecognises the deferred tax asset—and recognises the resulting deferred tax expense—of CU40.

IE190 Table 17.1 summarises the regulatory liabilities related to the penalty and income taxes, together with the related tax effects.

Table 17.1—Breakdown of deduction

	Regulatory liabilities		
In CU	**Penalty [A]**	**Tax effects [B]**	**Total**
Amounts to be deducted from regulated rates in Year 2	**60**	**40**	**100**
Deferred tax asset related to the regulatory liabilities arising from:			
Penalty ([A] × 40%)		24	
Tax effects of the penalty ([B] × 40%)		16	
Deferred tax asset		**40**	

IE191 Assuming no other transactions take place in Years 1–2, Entity A's statement of financial performance for these years is shown in Table 17.2.

Table 17.2—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Total**
IFRS 15 revenue[(a)] (Table 17.1)	—	(100)	**(100)**
Regulatory income (regulatory expense)	(100)	100	**—**
Total revenue	**(100)**	**—**	**(100)**
Income tax income (income tax expense)			
Current	—	40	**40**
Deferred	40	(40)	**—**
Loss	**(60)**	**—**	**(60)**

(a) IFRS 15 revenue excludes amounts other than the penalty deducted from the regulated rates charged.

Regulatory returns on an asset not yet available for use in specific circumstances

IE192 Examples 18A–18B illustrate the requirements in paragraphs B35–B40 of IFRS 20 for accounting for a regulatory asset or regulatory liability arising from a regulatory return on assets not yet available for use if:

(a) an entity capitalises borrowing costs related to those assets by applying IAS 23;

(b) the regulatory return is only a debt return or both a debt and equity return; and

(c) the entity's regulatory capital base has a direct relationship with those assets.

Example 18A—Regulatory returns (both debt and equity) included in determining the regulated rates charged during the construction period

IE193 Example 18A illustrates IFRS 20 requirements for accounting for a regulatory liability arising when the regulatory agreement entitles an entity to include regulatory returns on an asset not yet available for use in determining the regulated rates charged during the construction of the asset. This example assumes the conditions described in paragraph IE192—and specifically, the regulatory return in paragraph IE192(b) comprises both a debt and equity return.

Fact pattern

IE194 Entity A starts construction of an item of property, plant and equipment (the asset) on the first day of Year 1 and completes construction on the last day of Year 2. Entity A incurs construction costs of CU5,000 evenly over each of Years 1–2 (that is, total construction costs of CU10,000). Entity A also incurs borrowing costs of CU81 in Year 1 and CU234 in Year 2 based on an interest rate of 3%, which the entity capitalises in accordance with IAS 23 (see Table 18A.2). The cost of the asset is CU10,315 as determined applying IAS 16. The asset is available for use on the first day of Year 3 and has a useful life of three years. Entity A recognises depreciation expense as determined by applying IAS 16 using the straight-line method over Years 3–5.

IE195 The regulatory agreement specifies that Entity A includes the cost of the asset, excluding the capitalised borrowing costs, in determining regulatory depreciation of its regulatory capital base once the asset is available for use and recovers the asset through regulated rates evenly over three years (Years 3–5). For simplicity, this example illustrates the compensation related to the regulatory capital base only to the extent related to this asset.

IE196 The regulatory agreement also entitles Entity A to a rate of return of 8%, which comprises both a debt and equity return:

(a) while the asset is not yet available for use (Years 1–2). A rate of return of 8% is applied to the average balance between the actual opening balance and the estimated closing balance of the asset for each year. The regulatory return for each year is included in determining the regulated rates charged in the same year. For simplicity, this example assumes that the actual closing balance of the asset for each year equals the estimate.

(b) while the asset is available for use (Years 3–5). A rate of return of 8% is applied to the unrecovered balance of the regulatory capital base at the beginning of each year and the regulatory return is included in determining the regulated rates charged in the same year.

IE197 Table 18A.1 shows the regulatory compensation related to the asset.

Table 18A.1—Compensation related to the regulatory capital base

	Construction		Operation			
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory capital base						
Opening balance	—	5,000	10,000	6,666	3,333	
Construction costs	5,000	5,000	—	—	—	**10,000**
Regulatory depreciation	—	—	(3,334)	(3,333)	(3,333)	**(10,000)**
Closing balance	**5,000**	**10,000**	**6,666**	**3,333**	**—**	
Compensation related to the regulatory capital base						
Regulatory depreciation	—	—	3,334	3,333	3,333	**10,000**
Regulatory returns[(a)]	200	600	800	533	267	**2,400**
Regulatory compensation—IFRS 15 revenue	**200**	**600**	**4,134**	**3,866**	**3,600**	**12,400**

(a) For Year 1, regulatory returns are calculated at [(CU0 + CU5,000) ÷ 2] × 8%. For Year 2, regulatory returns are calculated at [(CU5,000 + CU10,000) ÷ 2] × 8%. For Years 3–5, regulatory returns are calculated using 8% on the unrecovered balance of the regulatory capital base at the beginning of the year.

Analysis

IE198 Entity A capitalises borrowing costs incurred in the construction of the asset during Years 1–2. Applying paragraphs B35–B40 of IFRS 20, Entity A:

(a) treats part of the regulatory returns included in determining the regulated rates charged during Years 1–2 as compensation for an allowable expense—that is, the capitalised borrowing costs that will be included as part of depreciation expense over the asset's useful life (Years 3–5); and

(b) determines that the regulatory returns in excess of the capitalised borrowing costs form part of the total allowed compensation during the reporting periods in which the regulatory agreement applies the rate of return to the regulatory capital base (Years 1–2)—that is, for the periods in which the asset is not yet available for use.

IE199 Table 18A.2 shows the regulatory returns included in determining the regulated rates charged—and hence in IFRS 15 revenue—during the period in which the asset is not yet available for use and the capitalised borrowing costs incurred during that period.

Table 18A.2—Regulatory returns in excess of capitalised borrowing costs			
In CU	**Year 1**	**Year 2**	**Total**
Regulatory returns included in regulated rates charged—IFRS 15 revenue (Table 18A.1) [A]	200	600	800
Capitalised borrowing costs[(a)] [B]	81	234	315
Excess [A] – [B]	**119**	**366**	**485**

(a) For simplicity, capitalised borrowing costs are calculated: (a) for Year 1 at [(CU5,000 + (CU5,000 ÷ 12)) ÷ 2] × 3%; and (b) for Year 2 at {CU5,081 + [(CU5,000 + (CU5,000 ÷ 12)) ÷ 2]} × 3%.

IE200 Applying paragraphs B35–B40 of IFRS 20, the compensation for capitalised borrowing costs forms part of the total allowed compensation for the reporting periods in which the asset is available for use (Years 3–5). Entity A accounts for a regulatory liability arising from the regulatory returns amounting to the capitalised borrowing costs during the reporting periods in which the asset is not yet available for use. During Years 1–2, Entity A's statement of financial performance reflects the excess of regulatory returns over the capitalised borrowing costs. The regulatory liability is fulfilled over the reporting periods in which the asset is available for use—that is, the asset's useful life. Consequently, during Years 3–5, Entity A's statement of financial performance reflects equal but opposite amounts, that is:

(a) regulatory income consisting of the fulfilment of the regulatory liability arising from the regulatory returns amounting to the capitalised borrowing costs; and

(b) depreciation expense including the capitalised borrowing costs.

IE201 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 18A.3.

Table 18A.3—Statement of financial performance						
	Construction		**Operation**			
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue (Table 18A.1)	200	600	4,134	3,866	3,600	**12,400**
Regulatory income (regulatory expense)	(81)	(234)	105	105	105	**—**
Total revenue	119	366	4,239	3,971	3,705	**12,400**

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Table 18A.3—Statement of financial performance						
	Construction		Operation			
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Depreciation expense	—	—	(3,439)	(3,438)	(3,438)	**(10,315)**
Profit	**119**	**366**	**800**	**533**	**267**	**2,085**
Of which:						
Regulatory returns on an asset not yet available for use that exceed capitalised borrowing costs (Table 18A.2)	119	366	—	—	—	**485**
Regulatory returns on the regulatory capital base (Table 18A.1)	—	—	800	533	267	**1,600**

Example 18B—Regulatory returns (both debt and equity) included in determining the regulated rates charged during the operation period

IE202 Example 18B illustrates IFRS 20 requirements for accounting for a regulatory asset arising when the regulatory agreement entitles an entity to include regulatory returns on an asset not yet available for use in determining the regulated rates charged during the operation period of the asset. This example assumes the conditions described in paragraph IE192—and specifically, the regulatory return in paragraph IE192(b) comprises both a debt and equity return.

Fact pattern

IE203 Example 18B assumes the same fact pattern as Example 18A, except that the regulatory agreement entitles Entity A:

(a) to accrue regulatory returns of 8%, comprising both a debt and equity return on the average balance between the opening balance (including regulatory returns already accrued) and the closing balance of the asset for each year while the asset is not yet available for use (Years 1–2); and

(b) to recover both the construction costs and the regulatory returns added to the regulatory capital base through regulated rates charged to customers evenly over three years while the asset is available for use (Years 3–5).

IE204 For simplicity, this example illustrates the compensation related to the regulatory capital base only to the extent related to this asset.

IE205 Table 18B.1 shows the regulatory compensation related to the asset.

Table 18B.1—Compensation related to the regulatory capital base

	Construction		Operation			
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory capital base						
Opening balance	—	5,200	10,816	7,210	3,605	
Construction costs	5,000	5,000	—	—	—	**10,000**
Regulatory returns[(a)]	200	616	—	—	—	**816**
Regulatory depreciation	—	—	(3,606)	(3,605)	(3,605)	**(10,816)**
Closing balance	**5,200**	**10,816**	**7,210**	**3,605**	**—**	
Compensation related to the regulatory capital base						
Regulatory depreciation	—	—	3,606	3,605	3,605	**10,816**
Regulatory returns[(b)]	—	—	865	577	288	**1,730**
Regulatory compensation—IFRS 15 revenue	**—**	**—**	**4,471**	**4,182**	**3,893**	**12,546**

(a) For Year 1, regulatory returns are calculated at [(CU0 + CU5,000) ÷ 2] × 8%. For Year 2, regulatory returns are calculated at [(CU5,200 + CU10,200) ÷ 2] × 8%.

(b) Regulatory returns are calculated using the rate of return of 8% on the unrecovered balance of the regulatory capital base at the beginning of the year.

Analysis

IE206 Entity A capitalises borrowing costs incurred in the construction of the asset during Years 1–2. Applying paragraphs B35–B40 of IFRS 20, Entity A determines that the regulatory returns in excess of the capitalised borrowing costs during Years 1–2 form part of the total allowed compensation during that period—that is, the period in which the asset is not yet available for use.

IE207 Table 18B.2 shows the regulatory returns accrued during the period in which the asset is not yet available for use and the capitalised borrowing costs incurred during that period.

Table 18B.2—Regulatory returns in excess of capitalised borrowing costs			
In CU	**Year 1**	**Year 2**	**Total**
Regulatory returns accrued (Table 18B.1) [A]	200	616	**816**
Capitalised borrowing costs (Table 18A.2) [B]	81	234	**315**
Excess [A] – [B]	**119**	**382**	**501**

IE208 Regulatory returns accrued while the asset is not yet available for use are included in determining the regulated rates charged and hence in IFRS 15 revenue while the asset is available for use. Applying paragraphs B35–B40 of IFRS 20, Entity A accounts for a regulatory asset arising from the regulatory returns in excess of the capitalised borrowing costs during the reporting periods in which the asset is not yet available for use. That regulatory asset is recovered through regulated rates charged during the reporting periods in which the asset is available for use—that is, the asset's useful life.

IE209 During Years 1–2, Entity A's statement of financial performance reflects the excess of regulatory returns over the capitalised borrowing costs.

IE210 During Years 3–5, Entity A's statement of financial performance reflects equal but opposite amounts:

(a) IFRS 15 revenue includes the regulatory returns accrued while the asset is not yet available for use;

(b) regulatory expense consists of the recovery of the regulatory asset arising from the regulatory returns in excess of the capitalised borrowing costs; and

(c) depreciation expense includes the capitalised borrowing costs.

IE211 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 18B.3.

Table 18B.3—Statement of financial performance						
	Construction		**Operation**			
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue (Table 18B.1)	—	—	4,471	4,182	3,893	**12,546**
Regulatory income (regulatory expense)	119	382	(167)	(167)	(167)	**—**
Total revenue	119	382	4,304	4,015	3,726	**12,546**
Depreciation expense	—	—	(3,439)	(3,438)	(3,438)	**(10,315)**
Profit	**119**	**382**	**865**	**577**	**288**	**2,231**

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Table 18B.3—Statement of financial performance						
	Construction		Operation			
In CU	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Of which:						
Regulatory returns on an asset not yet available for use that exceed capitalised borrowing costs (Table 18B.2)	119	382	—	—	—	**501**
Regulatory returns on the regulatory capital base (Table 18B.1)	—	—	865	577	288	**1,730**

Performance incentives

IE212 Examples 19–20 illustrate IFRS 20 requirements for accounting for a regulatory asset or regulatory liability arising from a performance incentive.

Example 19—Performance incentive—Bonus

IE213 Example 19 illustrates IFRS 20 requirements for identifying and recognising a regulatory asset arising from a performance bonus.

Fact pattern

IE214 A regulatory agreement entitles Entity A to a performance bonus if it meets specified performance criteria. Those criteria test the entity's performance only within the current reporting period.

IE215 Entity A meets the specified performance criteria in the current reporting period, entitling it to a performance bonus. The regulatory agreement gives Entity A the right to add the bonus in determining the regulated rates to be charged to customers in future periods.

Analysis

IE216 Applying paragraph B42 of IFRS 20, Entity A concludes that the performance bonus forms part of the total allowed compensation in the reporting period in which the entity's performance occurs (the current reporting period). Because the regulatory agreement specifies that the amount of the bonus is added to regulated rates to be charged to customers in future periods, that amount will be included in IFRS 15 revenue in the future.

IE217 Applying paragraph 26 of IFRS 20, Entity A recognises as a regulatory asset in the current reporting period its enforceable present right to add the amount of the bonus in determining the regulated rates to be charged to customers in future periods.

Example 20—Performance incentive—Performance period that extends beyond the reporting period

IE218 Example 20 illustrates IFRS 20 requirements for identifying and recognising a regulatory asset or regulatory liability arising from a performance incentive that relates to an entity's performance over a period that extends beyond the reporting period.

Fact pattern

IE219 Under the terms of a regulatory agreement, Entity A is subject to a performance incentive that relates to its performance over Years 1–5 in the construction of assets that it uses to supply regulatory goods or services. The performance incentive will result in a bonus or penalty based on 10% of the overall efficiency gain or loss arising from the difference between the construction cost targets and the actual costs Entity A incurs over Years 1–5. The regulatory agreement specifies that the bonus or penalty is added or deducted in determining the regulated rates to be charged to customers in Year 6.

IE220 Entity A estimates that it will incur a performance penalty for an overall efficiency loss over the performance period because of rising construction costs. Entity A estimates the amount of the performance penalty using the expected value method. Table 20.1 shows Entity A's estimates of the performance penalty that result from using that method.

Table 20.1—Performance penalty

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Cost targets	10,000	10,300	10,600	10,900	11,300	**53,100**
Construction costs	9,900	10,300	10,800	11,200	11,500	**53,700**
Efficiency gain/(loss)	100	—	(200)	(300)	(200)	**(600)**
Penalty (10%)						**60**

IE221 For simplicity, this example assumes that:

(a) Entity A completes 20% of the construction in each of Years 1–5; and

(b) the estimate of the performance penalty does not change over Years 1–5 and the estimated and actual amounts of the performance penalty at the end of Year 5 are the same.

Analysis

IE222 The performance incentive relates to Entity A's performance over Years 1–5, instead of its performance for each of those years. Entity A estimates that it will incur a performance penalty over the performance period. Applying paragraph B42 of IFRS 20, Entity A determines that the performance penalty reduces the total allowed compensation in the reporting periods in which the entity's performance occurs. Therefore, a difference in timing arises during

Years 1–5 because the performance penalty will be deducted in determining the regulated rates to be charged in Year 6.

IE223 Applying paragraphs B45–B47 of IFRS 20, Entity A assesses whether at the end of Year 1 it has an enforceable present obligation to deduct an amount that reflects its performance to date in determining regulated rates to be charged in future periods. To make this assessment, Entity A considers what rights and obligations it would have if the regulator or another party were to terminate the regulatory agreement at the end of Year 1 for reasons other than the entity's failure to perform as specified in the agreement. At the end of Year 1, Entity A's performance to date is a portion of the performance over Years 1–5 for which the entity estimates it will incur a penalty, instead of the efficiency gain that the entity has achieved in Year 1. Entity A determines that it has rights and obligations to continue performing over the performance period. Entity A concludes that at the end of Year 1 it has an enforceable present obligation to deduct an amount that reflects its performance to date.

IE224 Applying paragraph 26 of IFRS 20, Entity A recognises a regulatory liability. Entity A applies paragraph B47 of IFRS 20:

(a) to estimate the total amount of the performance penalty over Years 1–5.

(b) to determine performance to date at the end of Year 1 as the portion of the estimated amount in (a) that relates to Year 1 using a reasonable and supportable basis. Entity A concludes that a reasonable and supportable basis is the progress towards complete construction at the end of Year 1—that is, 20% of the performance penalty of CU60 relates to Year 1.

IE225 Assuming no other transactions take place in Years 1–6, Entity A's statement of financial performance for these years is shown in Table 20.2.

Table 20.2—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Year 6**	**Total**
IFRS 15 revenue[(a)]	—	—	—	—	—	(60)	**(60)**
Regulatory income (regulatory expense)	(12)	(12)	(12)	(12)	(12)	60	**—**
Total revenue	(12)	(12)	(12)	(12)	(12)	—	**(60)**
Expenses	—	—	—	—	—	—	**—**
Loss	**(12)**	**(12)**	**(12)**	**(12)**	**(12)**	**—**	**(60)**

(a) IFRS 15 revenue excludes amounts other than the penalty deducted from the regulated rates charged.

Inflation

Example 21—Compensation for inflation provided separately from regulatory depreciation

IE226 Example 21 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset or regulatory liability arising from compensation for inflation provided separately from regulatory depreciation.

Fact pattern

IE227 A regulatory agreement provides compensation for inflation arising in a reporting period through the allowed revenue for that period. The regulatory agreement entitles Entity A to recover the allowed revenue for a reporting period through the regulated rates charged during that period. The regulatory agreement also specifies that the amount of allowed revenue for a reporting period is determined by considering the amount of allowed revenue for the previous period adjusted by the expected inflation rate for the current period.

IE228 In accordance with the regulatory agreement, the regulator determines that the amount of allowed revenue for Year 5 is CU10,200. That amount is based on the allowed revenue for Year 4 of CU10,000, adjusted for the expected inflation during Year 5 of CU200 (2% of CU10,000).

IE229 The regulatory agreement requires that differences between the estimated and actual inflation rates for Year 5 be added or deducted in determining the regulated rates to be charged in Year 6. In Year 5, the actual inflation rate is 3%.

IE230 The regulatory agreement does not specify an interest rate for regulatory assets or regulatory liabilities arising from differences between the estimated and actual inflation rates.

IE231 For simplicity, this example assumes that the estimated and actual inflation rates were the same for the previous years.

IE232 The regulator uses the allowed revenue of CU10,200 and an estimated quantity of goods or services to be supplied to customers in Year 5 in determining the regulated rates to be charged to customers in Year 5. This example assumes actual quantities supplied equal estimated quantities and hence the amount of allowed revenue Entity A charges customers through the regulated rates during Year 5 is included in IFRS 15 revenue for that year.

Analysis

IE233 Applying paragraph B53 of IFRS 20, compensation for inflation in Year 5 forms part of the total allowed compensation for Year 5.

IE234 In accordance with the regulatory agreement, Entity A is entitled to compensation for inflation in Year 5 of CU300 (3% of CU10,000). Entity A included an amount of CU200 in determining the regulated rates charged to customers during Year 5. Consequently, Entity A is entitled to add an amount of CU100 in determining the regulated rates to be charged in Year 6.

IE235 Applying paragraph 26 of IFRS 20, Entity A recognises a regulatory asset and regulatory income at the end of Year 5 and measures it by applying paragraphs 34–51 of IFRS 20. Applying paragraph 48 of IFRS 20, Entity A concludes that the regulatory interest rate is nil. Therefore, Entity A measures the regulatory asset using a discount rate of 0%.

IE236 In Year 6, Entity A recovers the regulatory asset by adding CU100 to the regulated rates charged to customers and includes this amount in IFRS 15 revenue. Therefore, in Year 6 Entity A also derecognises the regulatory asset and recognises regulatory expense of CU100.

Allowed revenue and volume variances

Example 22—Allowed revenue and volume variances

IE237 Example 22 illustrates IFRS 20 requirements for identifying, recognising and measuring a regulatory asset or regulatory liability arising from amounts of allowed revenue under-recovered or over-recovered due to volume variances.

Fact pattern

IE238 Entity A starts supplying regulatory goods or services on the first day of Year 1.

IE239 The regulator determines that the regulated rate to be charged to customers in Year 1 is CU2 per unit. That regulated rate is based on:

(a) allowed revenue of CU240. This amount includes compensation for fixed input costs of CU100 and compensation for other operating costs of CU140 on an estimated basis; and

(b) an estimated quantity of 120 units to be supplied to customers.

IE240 In determining the regulated rate to be charged to customers in Year 2, the regulatory agreement gives Entity A the right to add or the obligation to deduct:

(a) the amount of allowed revenue under-recovered or over-recovered in Year 1; and

(b) differences between the estimated fixed input costs and actual fixed input costs incurred by the entity in Year 1.

IE241 When determining the regulated rates for Year 2, the regulator decides to treat amounts under-recovered or over-recovered of both allowed revenue and fixed input costs in paragraph IE240 as a single adjustment. The regulatory agreement does not specify an interest rate for regulatory assets or regulatory liabilities arising from amounts under-recovered or over-recovered.

IE242 The regulatory agreement prohibits Entity A from adjusting future regulated rates for any differences between the estimated and actual amounts of other operating costs recognised during Year 1.

IE243 In Year 1, Entity A:

(a) supplies 100 units, compared with the estimated quantity of 120 units. Consequently, the amount of allowed revenue under-recovered is CU40.

(b) recognises fixed input costs of CU120 applying IFRS Accounting Standards, compared with the estimate of CU100. Consequently, Entity A incurs higher than estimated fixed input costs by an amount of CU20.

(c) recognises other operating costs of CU135 by applying IFRS Accounting Standards, compared with the estimate of CU140. Consequently, Entity A incurs lower than estimated other operating costs by an amount of CU5.

Analysis

IE244 During Year 1, Entity A under-recovers:

(a) allowed revenue at an amount of CU40 because estimated quantities are higher than actual quantities supplied. Applying paragraph B57 of IFRS 20, the amount of allowed revenue under-recovered in Year 1 gives rise to a difference in timing. Entity A has a right to add the under-recovery of the allowed revenue of CU40 to the regulated rates charged in Year 2.

(b) fixed input costs of CU20. Applying paragraph B15 of IFRS 20, the fixed input costs recognised as an expense in Year 1 form part of the total allowed compensation for that period. Entity A has a right to add the under-recovery of fixed input costs of CU20 to the regulated rates charged in Year 2.

IE245 Entity A has two distinct rights—the right to recover the allowed revenue and the right to recover the fixed input costs by adding the under-recovered amounts to future regulated rates. Entity A's right to recover the allowed revenue amount for Year 1 (which was determined based on estimates of the fixed input costs and other operating costs) is distinct from any other rights and obligations that Entity A might have in relation to the compensation for items included in the allowed revenue determined for Year 1.

IE246 The regulated rates charged during Year 1 include compensation for other operating costs of CU140 on an estimated basis. In Year 1, Entity A recognises other operating costs of CU135. The regulatory agreement prohibits Entity A from adjusting future regulated rates for the CU5 difference between the estimated and actual costs. As determined by applying paragraph B26 of IFRS 20, that difference is a measurement difference that will not reverse over time. Entity A reflects the difference of CU5 (a gain) in the statement of financial performance in Year 1—that is, the period in which the entity recognises IFRS 15 revenue and other operating costs.

IE247 Applying paragraph 24 of IFRS 20, Entity A concludes that the rights arising from the differences in timing in paragraph IE244 meet the conditions to be treated as a single unit of account—that is, they are created by the same regulatory agreement, have a similar expiry pattern and are subject to similar risks. Therefore, applying paragraph 26 of IFRS 20, Entity A recognises a regulatory asset of CU60 at the end of Year 1.

IE248 Applying paragraphs 34–51 of IFRS 20, Entity A measures the regulatory asset arising in Year 1. Applying paragraph 48 of IFRS 20, Entity A concludes that the regulatory interest rate is nil. Therefore, Entity A measures the regulatory asset using a discount rate of 0%.

IE249 Assuming no other transactions take place in Year 1, Entity A's statement of financial performance for that year is shown in Table 22.1.

Table 22.1—Statement of financial performance

In CU	**Year 1**
IFRS 15 revenue	200
Regulatory income (regulatory expense)	60
Total revenue	260
Expenses[(a)]	(255)
Profit	**5**

(a) Expenses are calculated as the sum of the fixed input costs (CU120) and other operating costs (CU135).

Implied regulatory interest rate

Example 23—Uneven interest rates

IE250 Example 23 illustrates how an entity applies IFRS 20 requirements to measure a regulatory asset or regulatory liability that has uneven interest rates.

Fact pattern

IE251 During Year 1, Entity A recognises expenses of CU1,000. The regulatory agreement entitles Entity A to recover these expenses through regulated rates charged to customers evenly over Years 4–5, together with interest at 10% on the unrecovered regulatory balance at the beginning of Years 4–5. The regulatory agreement specifies no interest for Years 1–3.

IE252 Accordingly, at the end of Year 1, Entity A estimates it will recover the regulatory asset by including CU600 in the regulated rates charged in Year 4 and CU550 in Year 5—no recovery takes place in Years 2–3. Table 23.1 shows the estimated changes in the unrecovered regulatory balance.

Table 23.1—Regulatory balance					
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening balance	—	1,000	1,000	1,000	500
Addition	1,000	—	—	—	—
Regulatory interest	—	—	—	100	50
Recovery	—	—	—	(600)	(550)
Closing balance	**1,000**	**1,000**	**1,000**	**500**	**—**

Analysis

IE253 Applying paragraph 45 of IFRS 20, Entity A is required to discount the estimates of future cash flows, including regulatory interest, using the implied regulatory interest rate. In this example, the implied regulatory interest rate is the rate that at initial recognition discounts the estimated future cash flows of CU600 and CU550, which are expected to occur in Years 4–5, back to CU1,000 in Year 1—that is, back to the amount that equals the sum of the estimated future cash flows, excluding regulatory interest. The implied regulatory interest rate derived from the terms of the regulatory agreement that Entity A is required to use throughout the life of the regulatory asset is calculated to be 4.11%.

IE254 Table 23.2 shows the reconciliation of the regulatory asset, using a rate of 4.11% as the discount rate.

Table 23.2—Reconciliation of the carrying amount of the regulatory asset					
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening carrying amount	—	1,000	1,041	1,084	528
Addition	1,000	—	—	—	—
Regulatory interest income	—	41	43	44	22
Amount recovered	—	—	—	(600)	(550)
Closing carrying amount	**1,000**	**1,041**	**1,084**	**528**	**—**

IE255 If the regulatory agreement were to subsequently change the interest rate, the new implied regulatory interest rate would be the rate that discounts all the updated estimated future cash flows back to the carrying amount of the regulatory asset or regulatory liability immediately before the new interest rate is applied.

IE256 To illustrate this, assume the same fact pattern as in paragraphs IE251–IE252 except that, at the end of Year 4, the regulatory agreement changes the interest rate for that regulatory asset from 10% to 9.5% (see Table 23.3).

Table 23.3—Regulatory balance		
In CU	**Year 4**	**Year 5**
Opening balance	1,000	500
Addition	—	—
Regulatory interest	100	47
Recovery	(600)	(547)
Closing balance	**500**	**—**

IE257 Table 23.4 shows the reconciliation of the regulatory asset using the original implied regulatory interest rate of 4.11% as the discount rate for Year 4 and using the updated implied regulatory interest rate of 3.63% as the discount rate for Year 5.

Table 23.4—Reconciliation of the carrying amount of the regulatory asset					
In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**
Opening carrying amount	—	1,000	1,041	1,084	528
Addition	1,000	—	—	—	—
Regulatory interest income	—	41	43	44	19
Amount recovered	—	—	—	(600)	(547)
Closing carrying amount	**1,000**	**1,041**	**1,084**	**528**	**—**

Applying IFRS 20 with IFRIC 12 *Service Concession Arrangements*

IE258 Examples 24A–26 illustrate how an entity applies IFRS 20 with IFRIC 12. In these examples, a regulatory agreement takes the form of a service concession arrangement within the scope of IFRIC 12.

Example 24A—Relationship between an entity's regulatory capital base and an intangible asset

IE259 Example 24A illustrates how an entity operating under a service concession arrangement considers the methodology the regulator uses to determine the regulatory capital base and regulatory depreciation in determining the relationship between its regulatory capital base and an intangible asset.

Fact pattern

IE260 Entity A (operator) enters into a five-year service concession arrangement with a regulator (grantor) to construct assets in Year 1 (construction phase) and use these assets to supply goods or services to customers in Years 2–5 (operating phase).[2]

IE261 The regulator includes in Entity A's regulatory capital base the items of infrastructure (assets) that arise from the construction services. The regulator measures the assets based on the consideration the entity receives for those services. The regulator determines the classes and depreciation rates for the assets using the requirements in IFRS Accounting Standards. For simplicity, this example assumes that the regulatory capital base comprises only those assets and that all assets have a useful life of five years beginning from Year 2.

IE262 Entity A estimates that the construction costs will be CU9,000 and the consideration for the construction services will be CU10,000. The service concession arrangement entitles Entity A to recover this consideration during Years 2–5 by giving Entity A:

(a) an unconditional right to receive cash from the regulator for the construction services in the form of a guarantee to the entity for a minimum amount of CU2,000. That guaranteed amount is receivable at the end of the service concession arrangement in Year 5. For simplicity, this example assumes that the regulatory agreement does not provide interest for the receivable. Entity A accounts for this right as a financial asset by applying IFRS 9 *Financial Instruments*.

(b) a right to charge customers for goods or services supplied to them during Years 2–5 for the remainder of the consideration—that is, CU8,000. Entity A accounts for this right as an intangible asset by applying IAS 38 *Intangible Assets* and amortises the intangible asset over the operating phase of the service concession arrangement of four years.

IE263 For simplicity, this example assumes that Entity A:

(a) includes the amount of regulatory depreciation in the regulated rates charged, and hence in IFRS 15 revenue, in each of Years 2–5; and

(b) incurs no other costs during Years 2–5.

2 In service concession arrangements within the scope of IFRIC 12 *Service Concession Arrangements* that might create regulatory assets or regulatory liabilities, the regulator is typically the grantor as described in IFRIC 12. IFRS 20 refers to the grantor as the regulator and the operator as the entity (see paragraph B92 of IFRS 20).

IE264 Table 24A.1 shows the regulatory capital base and the amounts to be included in regulated rates.

Table 24A.1—Regulatory capital base and amounts to be included in regulated rates

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
Regulatory capital base						
Opening balance	—	10,000	8,000	6,000	4,000	
Consideration for construction services included in IFRS 15 revenue	10,000	—	—	—	—	**10,000**
Regulatory depreciation	—	(2,000)	(2,000)	(2,000)	(2,000)	**(8,000)**
Repayment of financial asset	—	—	—	—	(2,000)	**(2,000)**
Closing balance	**10,000**	**8,000**	**6,000**	**4,000**	**—**	
Amounts included in regulated rates—IFRS 15 revenue	**—**	**2,000**	**2,000**	**2,000**	**2,000**	**8,000**
Amortisation of intangible asset	**—**	**(2,000)**	**(2,000)**	**(2,000)**	**(2,000)**	**(8,000)**
Difference	**—**	**—**	**—**	**—**	**—**	**—**

Analysis

IE265 Entity A considers paragraphs B60–B78 and B94 of IFRS 20 to determine the relationship between a part of its regulatory capital base and its intangible asset. Entity A considers the items in the regulatory capital base—specifically, the portion of the assets in the regulatory capital base that relates to the intangible asset, instead of the regulatory capital base as a whole.

IE266 Applying paragraph B62 of IFRS 20, Entity A considers all reasonable and supportable information that is available without undue cost or effort, including:

(a) the regulatory methodology underlying the determination of the regulatory capital base and regulatory depreciation on the portion of the assets in the regulatory capital base that relates to the intangible asset; and

(b) how the regulator monitors whether the regulatory depreciation described in (a) provides compensation for the amortisation expense of the intangible asset.

IE267 The intangible asset reflects the portion of the assets in the regulatory capital base to be recovered over the operating phase of the service concession arrangement. Entity A determines that it is able to track, by amount and reporting period, how regulatory depreciation on that portion of the assets provides compensation for the amortisation expense of the intangible asset.

Therefore, Entity A determines that a part of its regulatory capital base has a direct relationship with its intangible asset.

IE268 Applying paragraph B15 of IFRS 20, compensation for the amortisation expense recognised in a reporting period forms part of the total allowed compensation for the same period. Applying paragraph B94 of IFRS 20, Entity A determines differences in timing arising from the compensation by considering the recovery period and recovery pattern of the portion of the assets in the regulatory capital base that relates to the intangible asset. In this example, that portion of the assets has the same recovery period and recovery pattern as the useful life and amortisation method of the intangible asset—that is, evenly over the operating phase of the service concession arrangement. Therefore, Entity A determines that no difference in timing arises from regulatory depreciation of the regulatory capital base.

IE269 Assuming no other transactions take place in Years 1–5, Entity A's statement of financial performance for these years is shown in Table 24A.2.

Table 24A.2—Statement of financial performance

In CU	**Year 1**	**Year 2**	**Year 3**	**Year 4**	**Year 5**	**Total**
IFRS 15 revenue (Table 24A.1)	10,000	2,000	2,000	2,000	2,000	**18,000**
Regulatory income (regulatory expense)	—	—	—	—	—	**—**
Total revenue	10,000	2,000	2,000	2,000	2,000	**18,000**
Contract costs (construction costs in paragraph IE262)	(9,000)	—	—	—	—	**(9,000)**
Amortisation expense (Table 24A.1)	—	(2,000)	(2,000)	(2,000)	(2,000)	**(8,000)**
Profit	**1,000**	**—**	**—**	**—**	**—**	**1,000**

Example 24B—Regulatory capital base has a direct relationship with an intangible asset—Regulatory recovery period shorter than useful life

IE270 Example 24B illustrates IFRS 20 requirements for identifying a regulatory liability under a service concession arrangement when the regulatory recovery period is shorter than the useful life of an intangible asset.

Fact pattern

IE271 Example 24B assumes the same fact pattern as Example 24A, except that the regulator entitles Entity A to include regulatory depreciation of CU8,000 in determining the regulated rates to be charged over an accelerated period—for example, during Years 2–3.

Analysis

IE272 The recovery period for the portion of the assets in the regulatory capital base that relates to the intangible asset is shorter than the useful life of the intangible asset. Consequently, part of the total allowed compensation for regulatory goods or services to be supplied over Years 4–5 has been included in IFRS 15 revenue for Years 2–3. Therefore, Entity A concludes that a regulatory liability arises from regulatory depreciation of the regulatory capital base during Years 2–3. Entity A fulfils the regulatory liability during Years 4–5 because the regulated rates charged in those years do not include any regulatory depreciation that compensates for the amortisation expense recognised in those years.

Example 24C—Regulatory capital base has a direct relationship with an intangible asset—Regulatory depreciation differs from amortisation expense

IE273 Example 24C illustrates how an entity determines whether a difference in timing arises when regulatory depreciation arising in a period differs from the amortisation expense of an intangible asset Entity A recognises in that period.

Fact pattern

IE274 Example 24C assumes the same fact pattern as Example 24A, except that:

(a) the actual quantities of goods or services supplied to customers differ from the estimates the regulator used to determine the regulated rates charged to customers;

(b) the regulator entitles Entity A to include in determining the regulated rates charged an amount of regulatory depreciation that differs from the amortisation expense of CU8,000; and

(c) the regulator prohibits Entity A from adding or deducting the amount of regulatory depreciation under-recovered or over-recovered in determining the regulated rates to be charged in the future.

Analysis

IE275 A difference arises between the total amount of compensation to be included in IFRS 15 revenue over all periods and the total amount of amortisation expense Entity A will recognise over all periods. Such a difference will not reverse over time. Entity A determines that the difference is not a difference in timing because Entity A does not have a right or obligation to add or deduct an amount in determining the regulated rates to be charged in the future. Instead, applying paragraph B26 of IFRS 20, Entity A determines the difference is a measurement difference.

Example 25A—Applying IFRS 20 with IFRIC 12—Regulatory assets and regulatory liabilities

IE276 Example 25A illustrates IFRS 20 requirements for identifying and recognising a regulatory asset or regulatory liability created by a service concession arrangement.

Fact pattern

IE277 Entity A enters into a 10-year service concession arrangement with a regulator to construct a plant in Years 1–2 (construction phase) and use the plant to supply goods or services to customers in Years 3–10 (operating phase). During the construction phase, the entity provides construction services to the regulator in exchange for an intangible asset—that is, a right to charge customers for the goods or services supplied to them in Years 3–10.

IE278 During the operating phase of the service concession arrangement, Entity A buys an input that is necessary to supply goods or services to customers. The input price is subject to high volatility.

IE279 The service concession arrangement:

(a) entitles Entity A to recover the actual costs of the input. The regulated rate for a period includes an estimate of the input costs that Entity A is expected to recognise for the period.

(b) requires differences between the actual and estimated input costs to be added to or deducted from the regulated rates to be charged to customers in the following reporting period.

IE280 At the end of Year 3, Entity A recognises higher than estimated input costs.

Analysis

IE281 Applying paragraph B92 of IFRS 20, Entity A applies IFRIC 12 and other IFRS Accounting Standards to account for rights and obligations arising from the service concession arrangement before applying IFRS 20 to any remaining rights and obligations that meet the definition of regulatory assets or regulatory liabilities. Applying IFRIC 12, Entity A recognises as an intangible asset its right to charge customers for the goods or services supplied in Years 3–10.

IE282 The service concession arrangement gives Entity A an enforceable present right to add the difference between actual and estimated input costs incurred in Year 3 in determining the regulated rates to be charged to customers in Year 4. Applying IFRIC 12 and other IFRS Accounting Standards, Entity A does not account for this right as an asset. However, applying paragraph 26 of IFRS 20, Entity A recognises a regulatory asset and regulatory income in Year 3. This reflects Entity A's enforceable present right to add the difference between actual and estimated input costs in determining the regulated rates to be charged to customers in Year 4.

Example 25B—Applying IFRS 20 with IFRIC 12—Guarantee clause

IE283 Example 25B illustrates the application of IFRS 20 with IFRIC 12 if a service concession arrangement includes a guarantee clause for any outstanding amounts relating to differences between the actual and estimated input costs accumulated during the operating phase.

Fact pattern

IE284 Example 25B assumes the same fact pattern as Example 25A, except that the service concession arrangement includes a guarantee clause. Under this clause:

(a) the regulator will reimburse Entity A in cash at the end of the service concession arrangement for any outstanding amount relating to input cost differences accumulated during the operating phase that the regulator has not yet included in determining the regulated rates charged or the entity has not yet collected from customers; and

(b) Entity A will reimburse the regulator in cash at the end of the service concession arrangement for any outstanding amount relating to input cost differences accumulated during the operating phase that the regulator has not yet deducted in determining the regulated rates charged.

IE285 At the end of Year 3, Entity A recognises input costs that exceed the estimated amount by CU100. The service concession arrangement entitles Entity A to add this amount in determining the regulated rates to be charged to customers in Year 4. In addition, the guarantee clause described in paragraph IE284 entitles Entity A to be reimbursed in cash by the regulator for any outstanding amount relating to the input cost differences at the end of the service concession arrangement.

Analysis

IE286 Applying paragraph B92 of IFRS 20, Entity A applies IFRIC 12 and other IFRS Accounting Standards to account for rights and obligations arising from the service concession arrangement before applying IFRS 20 to any remaining rights and obligations that meet the definition of regulatory assets or regulatory liabilities.

IE287 Entity A considers its right arising from the guarantee clause in the service concession arrangement to recover the input cost difference of CU100 arising in Year 3. Entity A applies IAS 32 *Financial Instruments: Presentation* and concludes that the right meets the definition of a financial asset because:

(a) the guarantee means that Entity A has a contractual right to receive cash from the regulator for any outstanding amount relating to input cost differences. In the extreme case, in which Entity A collects nothing from regulated rates charged in Year 4, Entity A would have a present, unconditional, contractual right to receive compensation for the higher input costs incurred in Year 3 from or at the direction of the regulator without bearing credit risk from customers or demand risk. The regulator bears the risk that the cash flows collected from

customers will be insufficient to recover the input cost difference due to credit risk or a fall in demand.

(b) the fact that the input cost differences might be recovered through regulated rates charged to customers does not alter Entity A's contractual right to receive cash from the regulator for the input cost difference. The method of payment is a matter of form only.

IE288 Entity A recognises its right to receive cash from the regulator relating to the input cost difference of CU100 arising in Year 3 as a financial asset. Entity A also concludes there are no remaining rights and obligations arising from the service concession arrangement that meet the definition of regulatory assets or regulatory liabilities in IFRS 20.

Example 26—Boundary of a regulatory agreement

IE289 Example 26 illustrates IFRS 20 requirements for determining the boundary of a regulatory agreement when an entity has an enforceable present right or enforceable present obligation:

(a) to supply regulatory goods or services over a finite period; and

(b) to receive compensation for unrecovered regulatory assets or pay compensation for unfulfilled regulatory liabilities on termination of the regulatory agreement.

Fact pattern

IE290 Entity A is subject to a service concession arrangement. This arrangement requires Entity A to supply regulatory goods or services over 30 years. Entity A operates in a jurisdiction where service concessions are renewed in a public tender process that is highly competitive.

IE291 The service concession arrangement specifies that on termination of the arrangement Entity A would be entitled to receive compensation from the regulator or any incoming operator for any unrecovered balances, including regulatory assets. The regulator has discretion in determining the type of compensation Entity A will receive on termination of the arrangement.

IE292 Entity A recognises a regulatory asset related to a pension liability by applying IFRS 20. Entity A expects the regulatory asset to result in an unrecovered amount at the end of the service concession arrangement.

Analysis

IE293 Entity A measures the regulatory asset related to the pension liability by including all estimated future cash flows that are within the boundary of the service concession arrangement. Entity A determines those cash flows by considering paragraphs B73–B84 of IFRS 20.

IE294 Entity A assesses whether cash flows from regulated rates charged to customers in the future are within the boundary of the service concession arrangement by applying paragraph B74 of IFRS 20. In particular, Entity A assesses whether it has:

(a) an enforceable present right or an enforceable present obligation to supply regulatory goods or services at a future date; and

(b) an enforceable present right to recover regulatory assets or an enforceable present obligation to fulfil regulatory liabilities through regulated rates charged to customers in the future.

IE295 Entity A determines that it has an enforceable present right or an enforceable present obligation to supply regulatory goods or services for the 30-year term of the service concession arrangement. Entity A also considers the new bid process that is required at the end of the 30-year term. Entity A determines that it has neither an enforceable present right nor an enforceable present obligation to supply regulatory goods or services beyond the 30-year term.

IE296 Entity A assesses the terms of the service concession arrangement relating to the determination of the regulated rates. Entity A concludes it has an enforceable present right to recover regulatory assets or an enforceable present obligation to fulfil regulatory liabilities by adding or deducting amounts in determining the regulated rates to be charged up to Year 30.

IE297 Entity A also assesses whether it has an enforceable present right to receive compensation on termination of the arrangement for any unrecovered amounts at the end of Year 30. Entity A concludes that, if the service concession arrangement was terminated at the end of the reporting period for reasons other than its failure to perform as specified in the arrangement, it would have an enforceable present right to receive compensation.

IE298 Entity A concludes that all estimated future cash flows arising from regulatory assets or regulatory liabilities are within the boundary of the arrangement. Those estimated future cash flows include cash flows arising from the regulatory asset related to the pension liability beyond the 30-year term of the service concession arrangement.

IE299 Therefore, Entity A includes in the measurement of the regulatory asset related to the pension liability all estimated future cash flows arising from the recovery of the regulatory asset, including cash flows from compensation on termination of the regulatory agreement.

Classification, presentation and disclosure

IE300 Examples 27A–28 illustrate specific classification, presentation and disclosure requirements in IFRS 20.

Example 27A—Reconciliation of regulatory assets and regulatory liabilities—Aggregation by types of items

IE301 Example 27A illustrates how an entity applies the IFRS 20 requirements to disclose in the notes a reconciliation from the opening to the closing carrying amounts of regulatory assets and regulatory liabilities.

IE302 The example also illustrates how an entity applies the IFRS 20 requirements relating to the aggregation and disaggregation of information considering its facts and circumstances.

Fact pattern

IE303 Entity A operates in the electricity transmission sector in Region X. During Year 1 Entity A recognises regulatory assets and regulatory liabilities.

Analysis

IE304 Applying paragraphs B95–B97 of IFRS 20, Entity A considers its facts and circumstances and decides to aggregate the information required by paragraphs 72–73 of IFRS 20 by the types of items these regulatory assets and regulatory liabilities relate to (for example, cost variances).

IE305 Tables 27A.1 and 27A.2 show reconciliations from the opening to the closing carrying amounts of Entity A's regulatory assets and regulatory liabilities in Year 1.

Table 27A.1—Reconciliation of the carrying amount of regulatory assets

In CU	**Cost variances**	**Performance incentives**	**Pension**	**Total**
Opening carrying amount	**7,800**	**570**	**9,000**	**17,370**
Profit or loss				
Origination	7,500	370	6,250	14,120
Recovery	(6,000)	(200)	(1,500)	(7,700)
Regulatory interest income	150	20	250	420
Other components[(a)]	—	40	4,000	4,040
Other comprehensive income				
Remeasurement[(b)]	—	—	2,000	2,000
Changes that do not affect profit or loss or other comprehensive income				
Business combination[(c)]	50	—	300	350
Closing carrying amount	**9,500**	**800**	**20,300**	**30,600**

(a) Other components include (i) CU40 related to the remeasurement of regulatory assets relating to performance incentives; and (ii) CU4,000 related to a change in the boundary of the regulatory agreement.

(b) The balance included in other comprehensive income relates to the remeasurement of the defined benefit pension plan, which is included in other comprehensive income in accordance with IAS 19. In accordance with paragraph 64 of IFRS 20, Entity A also includes the related regulatory income or regulatory expense in other comprehensive income.

(c) During Year 1 Entity A acquired control of a regulated business with regulatory assets of CU350 and regulatory liabilities of CU40 (see Table 27A.2).

Table 27A.2—Reconciliation of the carrying amount of regulatory liabilities				
In CU	**Cost variances**	**Performance incentives**	**Volume variance**	**Total**
Opening carrying amount	**(600)**	**(380)**	**(6,360)**	**(7,340)**
Profit or loss				
Origination	(3,800)	(175)	(4,614)	(8,589)
Fulfilment	2,000	150	2,500	4,650
Regulatory interest expense	(75)	(15)	—	(90)
Remeasurements	—	(20)	—	(20)
Changes that do not affect profit or loss or other comprehensive income				
Business combination[(a)]	(40)	—	—	(40)
Closing carrying amount	**(2,515)**	**(440)**	**(8,474)**	**(11,429)**

(a) During Year 1 Entity A acquired control of a regulated business with regulatory liabilities of CU40.

Example 27B—Reconciliation of regulatory assets and regulatory liabilities—Aggregation by types of activities and by types of items

IE306 Example 27B illustrates how an entity applies the IFRS 20 requirements to disclose in the notes a reconciliation from the opening to the closing carrying amounts of regulatory assets and regulatory liabilities.

IE307 The example also illustrates how an entity applies the IFRS 20 requirements relating to aggregation and disaggregation of information considering its facts and circumstances.

Fact pattern

IE308 Entity A operates in two sectors in Region Y—electricity transmission and electricity distribution. During Year 1 Entity A recognises regulatory assets and regulatory liabilities.

Analysis

IE309 Applying paragraphs B95–B97 of IFRS 20, Entity A considers its facts and circumstances and decides to aggregate the information required by paragraphs 72–73 of IFRS 20 by type of activity (for example, electricity transmission) and by type of items these regulatory assets and regulatory liabilities relate to (for example, cost variances).

IE310 Tables 27B.1 and 27B.2 show reconciliations from the opening to the closing carrying amounts of Entity A's regulatory assets and regulatory liabilities in Year 1.

Table 27B.1—Reconciliation of the carrying amount of regulatory assets

	Electricity transmission (ET)				Electricity distribution (ED)				
In CU	**Cost variances**	**Performance incentives**	**Pension**	**Total ET**	**Cost variances**	**Performance incentives**	**Pension**	**Total ED**	**Total**
Opening carrying amount	**5,226**	**380**	**6,000**	**11,606**	**2,574**	**190**	**3,000**	**5,764**	**17,370**
Profit or loss									
Origination	5,025	250	4,190	9,465	2,475	120	2,060	4,655	14,120
Recovery	(4,020)	(135)	(1,000)	(5,155)	(1,980)	(65)	(500)	(2,545)	(7,700)
Regulatory interest income	100	13	170	283	50	7	80	137	420
Other components[(a)]	—	30	—	30	—	10	4,000	4,010	4,040
Other comprehensive income									
Remeasurements[(b)]	—	—	1,340	1,340	—	—	660	660	2,000
Other changes that do not affect profit or loss or other comprehensive income									
Business combination[(c)]	50	—	300	350	—	—	—	—	350
Closing carrying amount	**6,381**	**538**	**11,000**	**17,919**	**3,119**	**262**	**9,300**	**12,681**	**30,600**

(a) Other components includes (i) CU30 (Electricity transmission) and CU10 (Electricity distribution) related to the remeasurement of regulatory assets relating to performance incentives; and (ii) CU4,000 (Electricity distribution) related to a change in the boundary of the regulatory agreement.

(b) The balance included in other comprehensive income relates to the remeasurement of the defined benefit pension plan, which is presented in other comprehensive income in accordance with IAS 19. In accordance with paragraph 64 of IFRS 20, Entity A also includes the related regulatory income or regulatory expense in other comprehensive income.

(c) During Year 1 Entity A acquired control of a regulated business with regulatory assets of CU350 and regulatory liabilities of CU40 (see Table 27B.2).

Table 27B.2—Reconciliation of the carrying amount of regulatory liabilities

	Electricity transmission (ET)				Electricity distribution (ED)				
In CU	**Cost variances**	**Performance incentives**	**Volume variance**	**Total ET**	**Cost variances**	**Performance incentives**	**Volume variance**	**Total ED**	**Total**
Opening carrying amount	**(400)**	**(255)**	**—**	**(655)**	**(200)**	**(125)**	**(6,360)**	**(6,685)**	**(7,340)**
Profit or loss									
Origination	(2,545)	(120)	—	(2,665)	(1,255)	(55)	(4,614)	(5,924)	(8,589)
Fulfilment	1,340	100	—	1,440	660	50	2,500	3,210	4,650
Regulatory interest expense	(50)	(10)	—	(60)	(25)	(5)	—	(30)	(90)
Remeasurements[a]	—	(15)	—	(15)	—	(5)	—	(5)	(20)
Other changes that do not affect profit or loss or other comprehensive income									
Business combination[b]	(40)	—	—	(40)	—	—	—	—	(40)
Closing carrying amount	**(1,695)**	**(300)**	**—**	**(1,995)**	**(820)**	**(140)**	**(8,474)**	**(9,434)**	**(11,429)**

(a) The amounts of CU15 (Electricity transmission) and CU5 (Electricity distribution) relate to the remeasurement of regulatory liabilities relating to performance incentives.

(b) During Year 1 Entity A acquired control of a regulated business with regulatory liabilities of CU40.

Example 28—Classification and presentation of regulatory assets and regulatory liabilities

IE311 Example 28 illustrates how an entity applies the classification and presentation requirements in IFRS 20 to the presentation of regulatory income and regulatory expense in its statement(s) of financial performance and the presentation of regulatory assets and regulatory liabilities in its statement of financial position.

Fact pattern

IE312 Example 28 assumes the same fact pattern as Example 27B. Example 27B includes a regulatory asset relating to Entity A's right to recover pension costs in future periods. Entity A operates an unfunded pension plan and pays benefits to employees when the benefits fall due. The regulatory agreement provides Entity A compensation for pension costs in determining the regulated rates in a future period only when the entity pays the benefits and settles its obligations under the plan.

IE313 For simplicity, this example:

(a) assumes that all regulatory assets and regulatory liabilities belong to wholly-owned subsidiaries and thus no amounts are attributable to non-controlling interests;

(b) does not show earnings per share (basic and diluted); and

(c) assumes that there are no discontinued operations.

Analysis

IE314 Applying paragraph 64 of IFRS 20, Entity A includes in other comprehensive income regulatory income or regulatory expense related to the remeasurements of the pension plan.

IE315 Entity A presents profit or loss and other comprehensive income in two statements. Items of other comprehensive income included in the statement presenting other comprehensive income are presented before tax effects, with one amount shown for the aggregate amount of income tax relating to those items in each category of other comprehensive income.

IE316 Entity A also concludes that the most useful structured summary of its expenses is provided by presenting in the operating category of the statement of profit or loss expenses classified by nature.

IE317 Table 28.1 shows the statement of profit or loss for the year ended 31 December Year 1. Table 28.2 shows the statement presenting comprehensive income and Table 28.3 shows the statement of financial position for the same reporting period.

Table 28.1—Statement of profit or loss for the year ended 31 December Year 1		
In CU	**Year 1**	**Year 0**
Revenue from contracts with customers	440,000	420,000
Regulatory income (regulatory expense)	6,831	3,193
Revenue	**446,831**	**423,193**
Other operating income	8,937	8,464
Purchase of electricity	(113,366)	(108,639)
Staff costs	(90,025)	(86,479)
Depreciation and amortisation expense	(53,620)	(50,783)
Maintenance	(38,166)	(42,950)
Other operating expenses	(5,072)	(7,128)
Operating profit	**155,519**	**135,678**
Share of profit of associates	7,090	4,700
Investment income	11,608	11,029
Profit before financing and income taxes	**174,217**	**151,407**
Interest expense on borrowings and lease liabilities	(12,000)	(14,750)
Interest expense on pension liabilities and provisions	(1,470)	(2,151)
Profit before income taxes	**160,747**	**134,506**
Income tax expense	(32,290)	(26,962)
Profit	**128,457**	**107,544**

Table 28.2—Statement presenting comprehensive income for the year ended 31 December Year 1		
In CU	**Year 1**	**Year 0**
Profit	**128,457**	**107,544**
Income and expenses that will not be reclassified to profit or loss:		
Gains (losses) on remeasurements of defined benefit pension plans	(2,000)	(1,700)
Regulatory income (regulatory expense) related to remeasurements of defined benefit pension plans	2,000	1,700
Share of other comprehensive income of associates	702	302

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Table 28.2—Statement presenting comprehensive income for the year ended 31 December Year 1		
In CU	**Year 1**	**Year 0**
Income tax relating to income and expenses that will not be reclassified to profit or loss	(140)	(60)
Other comprehensive income, net of tax	**562**	**242**
Total comprehensive income	**129,019**	**107,786**
Profit attributable to:		
Owners of the parent	102,766	86,035
Non-controlling interests	25,691	21,509
	128,457	107,544
Total comprehensive income attributable to:		
Owners of the parent	103,216	86,229
Non-controlling interests	25,803	21,557
	129,019	107,786

Table 28.3—Statement of financial position as at 31 December Year 1		
In CU	**Year 1**	**Year 0**
Assets		
Non-current assets		
Property, plant and equipment	824,228	833,500
Goodwill	90,800	91,200
Other intangible assets	57,820	58,750
Investments in associates	30,510	26,430
Regulatory assets	27,540	15,640
Total non-current assets	**1,030,898**	**1,025,520**
Current assets		
Inventories	33,190	28,140
Regulatory assets	3,060	1,730
Trade receivables	92,445	106,440
Cash and cash equivalents	202,160	180,570
Total current assets	**330,855**	**316,880**
Total assets	**1,361,753**	**1,342,400**

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Table 28.3—Statement of financial position as at 31 December Year 1		
In CU	**Year 1**	**Year 0**
Equity and liabilities		
Equity attributable to owners of the parent		
Share capital	620,000	600,000
Retained earnings	272,957	164,500
Other components of equity	12,646	21,200
Total equity attributable to owners of the parent	**905,603**	**785,700**
Non-controlling interests	67,604	45,800
Total equity	**973,207**	**831,500**
Non-current liabilities		
Borrowings	225,047	313,721
Lease liabilities	5,953	6,279
Pension liabilities	20,300	9,000
Provisions	26,550	62,870
Regulatory liabilities	10,280	6,600
Total non-current liabilities	**288,130**	**398,470**
Current liabilities		
Borrowings	7,914	7,592
Lease liabilities	1,086	7,408
Provisions	5,000	4,800
Regulatory liabilities	1,149	740
Trade payables	85,267	91,890
Total current liabilities	**100,416**	**112,430**
Total liabilities	**388,546**	**510,900**
Total equity and liabilities	**1,361,753**	**1,342,400**

Appendix
Amendments to the guidance on other IFRS Accounting Standards

IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Paragraph IG8 is amended. New text is underlined and deleted text is struck through.

Guidance on implementing
IFRS 1 *First-time Adoption of International Financial Reporting Standards*

...

IAS 16 *Property, Plant and Equipment*

...

IG8 An entity may elect to use one of the following amounts as the deemed cost of an item of property, plant and equipment:

...

(e) the carrying amount under previous GAAP of an item of property, plant and equipment <u>if the entity is subject to a regulatory agreement that can create regulatory assets or regulatory liabilities within the scope of IFRS 20 *Regulatory Assets and Regulatory Liabilities*</u> ~~that is used, or was previously used, in operations subject to rate regulation~~ (paragraph D8B of the IFRS).

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