



**INSTITUTE OF
CERTIFIED PUBLIC ACCOUNTANTS
OF UGANDA**

Our Ref: STA/001

30 July 2021

IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Sir/Madam

EXPOSURE DRAFT REGULATORY ASSETS AND REGULATORY LIABILITIES

The Institute of Certified Public Accountants of Uganda (ICPAU) is pleased to submit comments on the proposed accounting for regulatory assets and regulatory liabilities.

In Uganda, rate regulation is particularly common for the distribution of electricity. Hence the importance of this Exposure Draft and the overall outcome of the project.

Our responses to the questions in the Exposure Draft are provided in **Appendix 1**.

We are hopeful that the Board finds them helpful.

For any inquiries relating to this comment letter, kindly contact CPA Charles Lutimba by email at clutimba@icpau.co.ug

Yours faithfully,

A handwritten signature in purple ink, consisting of stylized, overlapping loops and lines, enclosed within a circular border.

CPA Mark Omona
DIRECTOR STANDARDS AND REGULATION
For: **SECRETARY/CEO**

Encl (ICPAU's Responses to Exposure Draft and Comment Letters: Lease Liability in a Sale and Leaseback)

NNN/.....

Appendix 1

Question 1—Objective and scope

Paragraph 1 of the Exposure Draft sets out the proposed objective: an entity should provide relevant information that faithfully represents how regulatory income and regulatory expense affect the entity's financial performance, and how regulatory assets and regulatory liabilities affect its financial position. Paragraph 3 of the Exposure Draft proposes that an entity apply the [draft] Standard to all its regulatory assets and all its regulatory liabilities. Regulatory assets and regulatory liabilities are created by a regulatory agreement that determines the regulated rate in such a way that part of the total allowed compensation for goods or services supplied in one period is charged to customers through the regulated rates for goods or services supplied in a different period (past or future). The [draft] Standard would not apply to any other rights or obligations created by the regulatory agreement—an entity would continue to apply other IFRS Standards in accounting for the effects of those other rights or obligations.

Paragraphs BC78-BC86 of the Basis for Conclusions describe the reasoning behind the Board's proposals. They also explain why the Exposure Draft does not restrict the scope of the proposed requirements to apply only to regulatory agreements with a particular legal form or only to those enforced by a regulator with particular attributes.

- a) Do you agree with the objective of the Exposure Draft? Why or why not?

Yes, ICPAU agrees with the objective of the standard to provide relevant information that faithfully represents how regulatory income and regulatory expenses affect the entity's financial performance, and how regulatory assets and regulatory liabilities affect its financial position.

We welcome the proposed requirement because financial statements that include such information would be more relevant and helpful for users to understand how financial performance and position are affected by rate-regulated activities.

- b) Do you agree with the proposed scope of the Exposure Draft? Why or why not? If not, what scope do you suggest and why?

Yes, ICPAU agrees with the proposed scope within the Exposure Draft.

- c) Do you agree that the proposals in the Exposure Draft are clear enough to enable an entity to determine whether a regulatory agreement gives rise to regulatory assets and regulatory liabilities? If not, what additional requirements do you recommend and why?

Please refer to our response in **b** above.

- d) Do you agree that the requirements proposed in the Exposure Draft should apply to all regulatory agreements and not only to those that have a particular legal form or those enforced by a regulator with particular attributes? Why or why not? If not, how and why should the Board specify what form a regulatory agreement should have, and how and why should it define a regulator?

Yes, ICPAU agrees that the requirements proposed in the Exposure Draft should apply to all regulatory agreements, and not only to those that have a particular legal form or those enforced by a regulator with particular attributes.

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However, it would be helpful for the Board to provide definition and further guidance on the terms “regulator” and “regulatory agreements” in order to limit divergence in interpretation and application. We invite the Board to define a “regulator” using a broad characteristics approach.

- e) Have you identified any situations in which the proposed requirements would affect activities that you do not view as subject to rate regulation? If so, please describe the situations, state whether you have any concerns about those effects and explain what your concerns are.

No.

- f) Do you agree that an entity should not recognise any assets or liabilities created by a regulatory agreement other than regulatory assets and regulatory liabilities and other assets and liabilities, if any, that are already required or permitted to be recognised by IFRS Standards?

Yes.

Question 2—Regulatory assets and regulatory liabilities

The Exposure Draft defines a regulatory asset as an enforceable present right, created by a regulatory agreement, to add an amount in determining a regulated rate to be charged to customers in future periods because part of the total allowed compensation for goods or services already supplied will be included in revenue in the future. The Exposure Draft defines a regulatory liability as an enforceable present obligation, created by a regulatory agreement, to deduct an amount in determining a regulated rate to be charged to customers in future periods because the revenue already recognised includes an amount that will provide part of the total allowed compensation for goods or services to be supplied in the future.

Paragraphs BC36-BC62 of the Basis for Conclusions discuss what regulatory assets and regulatory liabilities are and why the Board proposes that an entity account for them separately.

- a) Do you agree with the proposed definitions? Why or why not? If not, what changes do you suggest and why?

Yes. ICPAU agrees with the proposed definitions of regulatory assets and regulatory liabilities provided in the ED because we believe that such definitions capture the notion that a regulatory agreement creates an enforceable present right or enforceable present obligation for the entity.

- b) The proposed definitions refer to total allowed compensation for goods or services. Total allowed compensation would include the recovery of allowable expenses and a profit component (paragraphs BC87-BC113 of the Basis for Conclusions). This concept differs from the concepts underlying some current accounting approaches for the effects of rate regulation, which focus on cost deferral and may not involve a profit component (paragraphs BC224 and BC233-BC244 of the Basis for Conclusions). Do you agree with the focus on total allowed compensation, including both the recovery of allowable expenses and a profit component? Why or why not?

We welcome the focus on total allowed compensation, including both the recovery of allowable expenses and a profit component because they reflect what the entity is entitled to charge customers for goods or services that it has supplied. We further note that the allowable expenses in the regulatory agreement may be denominated

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in a currency other than the entity's functional currency. We therefore appreciate the inclusion of the guidance in paragraph 45 on foreign currency amounts.

- c) Do you agree that regulatory assets and regulatory liabilities meet the definitions of assets and liabilities within the *Conceptual Framework for Financial Reporting* (paragraphs BC37-BC47)? Why or why not?

We agree that regulatory assets and regulatory liabilities meet the definitions of assets and liabilities within the *Conceptual Framework for Financial Reporting*.

- d) Do you agree that an entity should account for regulatory assets and regulatory liabilities separately from the rest of the regulatory agreement (paragraphs BC58-BC62)? Why or why not?

We agree that an entity should account for regulatory assets and regulatory liabilities separately from the rest of the regulatory agreement.

- e) Have you identified any situations in which the proposed definitions would result in regulatory assets or regulatory liabilities being recognised when their recognition would provide information that is not useful to users of financial statements?

No.

Question 3—Total allowed compensation

Paragraphs B3-B27 of the Exposure Draft set out how an entity would determine whether components of total allowed compensation included in determining the regulated rates charged to customers in a period, and hence included in the revenue recognised in the period, relate to goods or services supplied in the same period, or to goods or services supplied in a different period. Paragraphs BC87-BC113 of the Basis for Conclusions explain the reasoning behind the Board's proposals.

- a) Do you agree with the proposed guidance on how an entity would determine total allowed compensation for goods or services supplied in a period if a regulatory agreement provides:
- Regulatory returns calculated by applying a return rate to a base, such as a regulatory capital base (paragraphs B13-B14 and BC92-BC95)?
 - Regulatory returns on a balance relating to assets not yet available for use (paragraphs B15 and BC96-BC100)?
 - Performance incentives (paragraphs B16-B20 and BC101-BC110)?
- b) Do you agree with how the proposed guidance in paragraphs B3-B27 would treat all components of total allowed compensation not listed in question 3(a)?
- c) Why or why not? If not, what approach do you recommend and why?
- d) Should the Board provide any further guidance on how to apply the concept of total allowed compensation? If so, what guidance is needed and why?

Yes, we agree with the proposals (a) & (b). In regard to (d), kindly refer to our response to 2 (b) above.

Question 4—Recognition

Paragraphs 25-28 of the Exposure Draft propose that:

- an entity recognise all its regulatory assets and regulatory liabilities; and
- if it is uncertain whether a regulatory asset or regulatory liability exists, an entity should recognise that regulatory asset or regulatory liability if it is more likely than not that it exists. It could be certain that a regulatory asset or regulatory liability exists even if it is uncertain whether that asset

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or liability will ultimately generate any inflows or outflows of cash. Uncertainty of outcome would be addressed in measurement (Question 5).

Paragraphs BC122-BC129 of the Basis for Conclusions describe the reasoning behind the Board's proposals.

- a) Do you agree that an entity should recognise all its regulatory assets and regulatory liabilities? Why or why not?

Yes, ICPAU agrees that an entity should recognise all its regulatory assets and regulatory liabilities existing at the end of the reporting period.

In some jurisdictions, there may be a time lag between when additional costs are incurred and when they are approved by the regulator to be charged to customers in future periods. In other words, there may be instances where cost recoveries may be subject to further or additional approval by the regulator—a process that is often bureaucratic leading to approval times that go beyond the immediate next annual reporting period. Furthermore, there may be a standard “ceiling” of cost recoveries that replaces actual cost incurred by the rate-regulated entity.

ICPAU appreciates that the Board has not limited recognition to mere existence of a regulatory agreement but has provided additional guidance in paragraph 27 for determining when a regulatory asset or regulatory liability exists. We believe this guidance will be sufficient for preparers in our jurisdiction.

- b) Do you agree that a ‘more likely than not’ recognition threshold should apply when it is uncertain whether a regulatory asset or regulatory liability exists? Why or why not? If not, what recognition threshold do you suggest and why?

Yes, we agree that a ‘more likely than not’ recognition threshold should apply when it is uncertain whether a regulatory asset or regulatory liability exists. We believe this is consistent with the guidance in paragraph 27.

Question 5—Measurement

Paragraph 29 of the Exposure Draft specifies the measurement basis. Paragraphs 29-45 of the Exposure Draft propose that an entity measure regulatory assets and regulatory liabilities at historical cost, modified by using updated estimates of future cash flows.

An entity would implement that measurement basis by applying a cash-flow-based measurement technique. That technique would involve estimating future cash flows—including future cash flows arising from regulatory interest—and updating those estimates at the end of each reporting period to reflect conditions existing at that date. The future cash flows would be discounted (in most cases at the regulatory interest rate—see Question 6). Paragraphs BC130-BC158 of the Basis for Conclusions describe the reasoning behind the Board's proposals.

- a. Do you agree with the proposed measurement basis? Why or why not? If not, what basis do you suggest and why?

ICPAU agrees with the proposed measurement basis. We believe that measuring regulatory assets and regulatory liabilities at historical cost, modified for subsequent measurement by using updated estimates of future cash flows, provides

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relevant information to users in understanding if there were any changes to the expected recovery and fulfilment of those balances.

- b. Do you agree with the proposed cash-flow-based measurement technique? Why or why not? If not, what technique do you suggest and why? If cash flows arising from a regulatory asset or regulatory liability are uncertain, the Exposure Draft proposes that an entity estimate those cash flows applying whichever of two methods—the ‘most likely amount’ method or ‘expected value’ method—better predicts the cash flows. The entity should apply the chosen method consistently from initial recognition to recovery or fulfilment. Paragraphs BC136-BC139 of the Basis for Conclusions describe the reasoning behind the Board’s proposal.
- c. Do you agree with this proposal? Why or why not? If not, what approach do you suggest and why?

ICPAU agrees with the proposed cash-flow based measurement methodology as it suits measurement of regulatory assets and regulatory liabilities.

Question 6—Discount rate

Paragraphs 46-49 of the Exposure Draft propose that an entity discount the estimated future cash flows used in measuring regulatory assets and regulatory liabilities. Except in specified circumstances, the discount rate would be the regulatory interest rate that the regulatory agreement provides. Paragraphs BC159-BC166 of the Basis for Conclusions describe the reasoning behind the Board’s proposals.

- a. Do you agree with these proposals? Why or why not? If not, what approach do you suggest and why? Paragraphs 50-53 of the Exposure Draft set out proposed requirements for an entity to estimate the minimum interest rate and to use this rate to discount the estimated future cash flows if the regulatory interest rate provided for a regulatory asset is insufficient to compensate the entity. The Board is proposing no similar requirement for regulatory liabilities. For a regulatory liability, an entity would use the regulatory interest rate as the discount rate in all circumstances. Paragraphs BC167-BC170 of the Basis for Conclusions describe the reasoning behind the Board’s proposals.

We agree with the proposal to discount the estimated future cash flows using the regulatory interest rate in measuring regulatory assets and regulatory liabilities as this would simplify the measurement model envisaged in the Basis for Conclusions.

- b. Do you agree with these proposed requirements for cases when the regulatory interest rate provided for a regulatory asset is insufficient? Why or why not?

We do not agree with this proposal. The use of a discount rate that is different from the regulatory rate may significantly reduce comparability of financial statements as envisaged in the conceptual framework. It may further give rise to more estimation uncertainties in the preparation of the financial statements, which we believe is not the intention of the Board.

- c. Have you identified any other situations in which it would be appropriate to use a discount rate that is not the regulatory interest rate? If so, please describe the situations, state what discount rate you recommend and explain why it would be a more appropriate discount rate than the regulatory interest rate. Paragraph 54 of the Exposure Draft addresses cases when a regulatory agreement provides regulatory interest unevenly by applying a series of different regulatory interest rates in successive periods. It proposes that an entity should translate those rates into a single discount rate for use throughout the life of the regulatory asset or regulatory liability.

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No.

- d. Do you agree with the proposal? Why or why not? If not, what do you recommend and why?

No comment.

Question 7—Items affecting regulated rates only when related cash is paid or Received

In some cases, a regulatory agreement includes an item of expense or income in determining the regulated rates in the period only when an entity pays or receives the related cash, or soon after that, instead of when the entity recognises that item as expense or income in its financial statements. Paragraphs 59-66 of the Exposure Draft propose that in such cases, an entity would measure any resulting regulatory asset or regulatory liability using the measurement basis that the entity would use in measuring the related liability or related asset by applying IFRS Standards. An entity would adjust that measurement to reflect any uncertainty that is present in the regulatory asset or regulatory liability but not present in the related liability or related asset. Paragraphs BC174-BC177 of the Basis for Conclusions describe the reasoning behind the Board's proposals.

- (a) Do you agree with the measurement proposals when items of expense or income affect regulated rates only when related cash is paid or received? Why or why not? If not, what approach do you suggest for such items and why? When these measurement proposals apply and result in regulatory income or regulatory expense arising from remeasuring the related liability or related asset through other comprehensive income, paragraph 69 of the Exposure Draft proposes that an entity would also present the resulting regulatory income or regulatory expense in other comprehensive income. Paragraphs BC183-BC186 of the Basis for Conclusions describe the reasoning behind the Board's proposal.
- (b) Do you agree with the proposal to present regulatory income or regulatory expense in other comprehensive income in this case? Why or why not? If not, what approach do you suggest and why?

Yes. We agree with this proposal.

Question 8—Presentation in the statement(s) of financial performance

Paragraph 67 of the Exposure Draft proposes that an entity present all regulatory income minus all regulatory expense as a separate line item immediately below revenue. Paragraph 68 proposes that regulatory income includes regulatory interest income and regulatory expense includes regulatory interest expense. Paragraphs BC178-BC182 of the Basis for Conclusions describe the reasoning behind the Board's proposals.

- (a) Do you agree that an entity should present all regulatory income minus all regulatory expense as a separate line item immediately below revenue (except in the case described in Question 7(b))? Why or why not? If not, what approach do you suggest and why?

Yes. We agree with this proposal.

- (b) Do you agree with the proposed inclusion of regulatory interest income and regulatory interest expense within the line item immediately below revenue? Why or why not? If not, what approach do you suggest and why?

Yes. We agree with the proposed inclusion of regulatory interest income and regulatory interest expense within the line item immediately below revenue.

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Question 9—Disclosure

Paragraph 72 of the Exposure Draft describes the proposed overall objective of the disclosure requirements. That objective focuses on information about an entity's regulatory income, regulatory expense, regulatory assets and regulatory liabilities, for reasons explained in paragraphs BC187-BC202 of the Basis for Conclusions. The Board does not propose a broader objective of providing users of financial statements with information about the nature of the regulatory agreement, the risks associated with it and its effects on the entity's financial performance, financial position or cash flows.

- (a) Do you agree that the overall disclosure objective should focus on information about an entity's regulatory income, regulatory expense, regulatory assets and regulatory liabilities? Why or why not? If not, what focus do you suggest and why?
- (b) Do you have any other comments on the proposed overall disclosure objective? Paragraphs 77-83 of the Exposure Draft set out the Board's proposals for specific disclosure objectives and disclosure requirements.
- (c) Do you have any comments on these proposals? Should any other disclosures be required? If so, how would requiring those other disclosures help an entity better meet the proposed disclosure objectives?
- (d) Are the proposed overall and specific disclosure objectives and disclosure requirements worded in a way that would make it possible for preparers, auditors, regulators and enforcement bodies to assess whether information disclosed is sufficient to meet those objectives?

Yes. We agree that the overall disclosure objective should focus on information about an entity's regulatory income, regulatory expense, regulatory assets and regulatory liabilities.

We believe that any other relevant disclosures are already provided for in IFRS 15.

Question 10—Effective date and transition

Appendix C to the Exposure Draft describes the proposed transition requirements. Paragraphs BC203-BC213 of the Basis for Conclusions describe the reasoning behind the Board's proposals.

- a. Do you agree with these proposals?
Yes. We agree with this proposal.
- b. Do you have any comments you wish the Board to consider when it sets the effective date for the Standard?
No comment.