

RRA Outreach Activities Issues Paper

Objective

- 1 Following the issuance of the IASB ED/2021/1 *Regulated Assets and Regulated Liabilities* ('the ED') on 28 January 2021, the objective of this session is to:
 - (a) update EFRAG TEG-CFSS on the pre-ED early-stage effects analysis outreach; and
 - (b) discuss and obtain EFRAG TEG-CFSS views on a proposed extended-outreach plan (objectives and activities).

Early-stage effects analysis outreach (Pre-ED)

- 2 Before the issuance of the ED, EFRAG performed early-stage effects analysis with data from survey-based outreaches to preparers and users of financial statements. The high-level objectives of these outreaches are described below.

Preparers of financial statements

- 3 The outreach to preparers of financial statements of rate-regulated entities (including members of the EFRAG Rate-Regulated Activities Working Group-RRAWG) focused on:
 - (a) the clarity around the scope of the model;
 - (b) the likely effects on financial statements; and
 - (c) a high-level assessment of possible implementation challenges, and anticipated cost-benefit analysis.

- 4 A summary of the results of the early-stage effects analysis outreach to preparers can be found in **Appendix 1**.

Users of financial statements

- 5 The outreach to users that undertake fundamental analysis of rate-regulated entities assessed the usefulness and benefits of information on the effects of rate-regulated activities on the performance, position and prospects of reporting entities. The aim was to ascertain users' information needs and whether the proposed accounting model would meet their needs.
- 6 A summary of the results of the early-stage effects analysis outreach to users can be found in **Appendix 2**.

Extended-outreach plan (Post-ED)

- 7 With the issuance of the ED, the EFRAG Secretariat is planning to extend outreach activities to:
 - (a) further assess the impacts of the proposed model in the ED; and
 - (b) obtain stakeholder views on EFRAG's Draft Comment Letter (DCL).
- 8 A targeted outreach approach will be adopted because of the applicability of the topic being restricted to some sectors and due to its significance being more pronounced in some jurisdictions.
- 9 The outreach will be targeted at the following audiences:

- (a) European National Standard Setters (NSS);
- (b) Preparers of financial statements;
- (c) Users of financial statements;
- (d) Related Industry associations; and
- (e) Academics

European National Standard Setters (NSS)

- 10 The EFRAG Secretariat will aim to collaborate with the IASB staff in planning and hosting outreach events with NSS. The events will aim to obtain stakeholder views on the ED questions and EFRAG's DCL.
- 11 The EFRAG Secretariat will seek the views of NSS' rate-regulated working groups on EFRAG's DCL.

Preparers of financial statements

- 12 The EFRAG Secretariat is planning to conduct follow-up interviews with the preparers that participated in EFRAG's early-stage effects analysis to:
 - (a) update their results from the surveys; and
 - (b) understand the impact of the application of the model based on the detailed proposals of the ED.

Users of financial statements

- 13 The EFRAG Secretariat is planning to conduct follow-up interviews with users that participated in EFRAG's early-stage effects analysis to:
 - (a) update their results from the surveys; and
 - (b) elaborate and emphasise on the detailed disclosure needs of users following the detailed disclosure requirements in the ED.
- 14 The EFRAG Secretariat is also planning to conduct an outreach event with users to understand the usefulness of the disclosure requirements in the ED.
- 15 To the extent feasible, the EFRAG Secretariat will participate in user outreaches conducted by the IASB and the Canadian Accounting Standard Setters Board (AcSB).

Related Industry Associations

- 16 The EFRAG Secretariat also aims to contact related industry associations to obtain their views of the proposed model.

Academics

The EFRAG Secretariat will reach out to academics to obtain any available academic evidence related to the proposals in the ED.

Question for EFRAG TEG-CFSS

- 17 Does EFRAG TEG-CFSS have any comments on the proposed extended outreach activities?
- 18 Are any of the EFRAG CFSS members available to jointly host events in collaboration with EFRAG and the IASB?

Appendix 1: Early-stage effects analysis outreach- preparer feedback

Introduction

- 1 **Appendix 1** summarises the feedback received from 15 preparers that responded to the survey¹ questionnaire-based outreach related to early-stage effects analysis of the ED's proposed model. The respondents were from eight jurisdictions, most (64%) were from utilities sector and the rest from telecommunications and energy sectors. Most of them operate in the European Economic Area and the UK.
- 2 All respondents are preparing their financial statements under IFRS and they manage an asset base which ranges between €15m and €303bn. Respondents noted that they have a mixture of regulatory arrangements in place (i.e., hybrid, cost of service, incentive-based).

Summary of results

- 3 Respondents were mostly clear on who the regulators are that govern the rate-regulated activities within their jurisdictions. With regards to the scope of the proposed model, some respondents raised some concerns with regards to certain contracts that could be within the scope of the model. However, they have indicated that the scope assessment is dependent on the final wording in the ED. Most were not aware of cases where the enforceable rights (obligations) are recovered (fulfilled) by third parties on behalf of customers.
- 4 Respondents noted mixed views with regards to the impact of the proposed model on the statement of financial position. The most significant contributor was the difference between local GAAP and IFRS. Most respondents noted that they do have other information even not reported under IFRS available. A small group of respondents noted that this information will be significantly different from the proposals expected in the ED mainly due to the mechanics of total allowed compensation.
- 5 Most respondents expect a moderate impact on the statement of financial performance mainly because their local GAAP already requires the recognition regulatory assets and regulatory liabilities. Most respondents also noted that loan covenants will not be significantly impacted by the proposed model as these covenants are normally based on local GAAP information.
- 6 Most respondents noted that rate-regulated information is available elsewhere and more than half consider it will be feasible to use the information to produce IFRS disclosures. However, a small minority noted that significant changes to this information is to be applied to produce the necessary disclosure under IFRS.
- 7 Most respondents are concerned that the IFRS 3 *Business Combination* exemption will have unintended consequences.
- 8 For the initial implementation, some respondents also noted that measurement might be a concern due to the difference in timing specifically with regards to construction contracts, the discount rate being applied and the initial assessment of contracts under the proposed model.
- 9 Most respondents noted that a positive cost benefit relationship will be achieved and highlighted the benefits with regards to transparency and comparability of the proposed model.

¹ On 10 November 2020, EFRAG launched an online survey inviting preparers of financial statements of rate regulated entities to participate in an outreach by completing a survey questionnaire. The deadline was set for 8 January 2021.

Appendix 2: Early-stage effects analysis outreach- user feedback

Introduction

- 10 **Appendix 2** summarises the feedback received from eight users that responded to the survey² questionnaire-based outreach related to the early-stage effects analysis of the ED's proposed model. The feedback included responses from sell-side (3), buy-side (2) and rating agency (2) analysts.
- 11 The users indicated that they mostly focus on the utilities and transport sectors and focus mainly on equity and bonds as asset classes. The users covered mostly the European area, but some also have a global focus. All users indicated that they are covering entities which report under IFRS.

Summary of results

- 12 Users indicated that they are using different sources of information to analyse financial statements of rate regulated entities. Apart from one rating agency analyst that indicated that they focus more on creditworthiness, users noted that their analytical focus is on:
 - (a) Performing an assessment of the enterprise value to influence buy or sell decision; and
 - (b) Assessing the financial return and risk profile including the earnings, the cash flow profile and the ability to recover costs.
- 13 Most users indicated that they do take the effect of rate regulation into account when performing a Purchase Price Allocation (PPA). Users noted that the disclosure for regulatory assets or regulatory liabilities affect the type of analysis they perform on rate-regulated entities and that they normally include reported regulatory assets and regulatory liabilities in their quantitative analytical models.
- 14 The rating agency analyst sought to compute ratios in a comparable way across our global portfolio regardless of the accounting framework being used.
- 15 For supplementary disclosures, users noted that although the financial statements are the main source of information, transparency is key, and judgements and estimates should be disclosed. They also noted their use of non-GAAP metrics and other information in their analysis.
- 16 Most users that responded to the question indicated that recognition of regulatory assets, regulatory liabilities and related regulatory income, regulatory expense improves understanding of regulated entities, improves valuation accuracy and leads to a more efficient allocation of capital in markets.
- 17 Many users indicated that the requirements to recognise regulatory assets and regulatory liabilities have no impact on their reliance on non-GAAP measures.
- 18 Lastly, they consider there to be no drawbacks to the recognition of regulatory assets and regulatory liabilities.

² On 28 October 2020, EFRAG launched an online survey inviting users of financial statements of rate regulated entities to participate in an outreach by completing a survey questionnaire. The deadline was set for 8 January 2021.