EFRAG RRAWG Chairman Report 12 May 2025

Objective

1 The purpose of the meeting was to present and discuss with the EFRAG RRAWG members the following:

(a) the preliminary results of EFRAG's survey to preparers from European entities that are likely to be in the scope of the forthcoming IFRS 20 *Regulatory Assets and Regulatory Liabilities*; and

(b) the preliminary findings from the ongoing review of regulations across EEA jurisdictions.

2 The findings on the above are part of EFRAG's preparatory work for its endorsement advice. In addition, the EFRAG FR TEG Chair sought the EFRAG RRAWG members' views on whether EFRAG should expedite the endorsement process to cater for those entities wishing to early adopt IFRS 20.

3 The eight new RRAWG members were also introduced at the meeting.

Preliminary results of EFRAG's survey

General aspects

4 Members noted that the preliminary results of the EFRAG's survey were a comprehensive and useful initial input for evaluating IFRS 20 albeit being inconclusive due to the following:

(a) There is a need to substantiate or clarify some of the data (i.e., regulatory balances currently recognised in the financial statements of companies as shown on slide 7 of the presentation).

(b) There was limited coverage of companies from industries other than electricity and gas.

(c) There was a limited response rate for some of the areas where views were sought (e.g. the inflation adjustment to the RCB).

(d) There was a possible misclassification by companies of whether they were in a direct (no direct) relationship (e.g. an entity classified itself as having a no direct relationship while having a cost-based regulatory scheme).

(e) There were areas that needed further exploration with respondents (e.g., many respondents being comfortable with the IFRS 20 unit of account notwithstanding the difficulties they pinpointed).

(f) There is a need to investigate the misalignment of some answers from preparers of the same sector and jurisdiction.

5 It was also noted that, due to the anticipated IASB decisions on sweep issues at its May 2025 meeting, the survey findings and concerns about discounting regulatory assets applying the minimum interest rate if the regulatory interest rate is insufficient or not available were no longer a matter of attention.

6 On the way forward, members underscored the importance of further field testing (based on the final wording of IFRS 20) to assess the practicability of the new Standard. In this regard, they acknowledged that the survey results indicated the areas where further outreach was needed including a) the direct (no direct) relationship classification, b) the unit of account, c) the interplay between inflation adjustment via either a real or nominal interest rate and d) the sources of differences in timing that result in recognised regulatory assets and regulatory liabilities.

Direct / no direct relationship

7 Members observed that for several entities that assessed themselves to have a no-direct relationship in the survey findings, the expected unrecognised regulatory assets and regulatory liabilities arising from the RCB would be material. It should be, however, noted that this assessment of materiality was based on percentage of unrecognised RA(RL) over the total of recognized RA(RL) + unrecognized RA(RL). The result of this materiality assessment would be much different, if unrecognised RA(RL) are assessed out of the total assets of the regulated entity. In the latter case, the percentage of unrecognised RA(RL) over total assets would be much lower and would not be material.

8 Some members questioned how materiality could be assessed in a situation of a no direct relationship. These members were concerned that in no direct relationship materiality would be assessed at a very high level.

9 The UKEB representative mentioned that in the UK most of the differences in timing will go through the RCB and considering that in the UK entities generally had a ‘no direct’ relationship between RCB and PPE, there would only be a proportion of regulatory assets and regulatory liabilities recognised in the financial statements. i.e. differences in timing that are related to revenue. Given that the survey findings showed a significant proportion

of incentive-based schemes, she questioned why companies in the EU were not as concerned about the direct (no direct) relationship criterion.

10 In reply, it was noted that whether there were differences in timing arising from RCB components was what needs to be considered. For instance, for the German TSOs, the differences in timing arise from volume variances, allowable expenses (or revenues) and performance incentives, all of which are highly impacted by energy costs and energy prices, volumes of transferred electricity and many other aspects. The German surcharge and cost allocation mechanisms and other legal obligations are allocated under the allowable expense/revenue bucket as they are not at all connected to the RCB. The RCB does not create differences in timing for Germany TSOs if the TSO has aligned the useful life of its assets to the regulatory scheme. Even in situations, where useful life of assets is not fully aligned, there is a doubt whether regulatory assets or regulatory liabilities in relation to the RCB will be material enough for German TSOs.

11 Furthermore, the IASB staff member outlined the components of the RCB that would lead to differences in timing under a direct relationship but not under a 'no direct' relationship. She also clarified that even if there was a 'no direct' relationship between an entity's RCB and its accounting data, some differences in timing (such as pension costs) were specifically tracked by the regulator and would result in the recognition of regulatory assets and regulatory liabilities. The IASB staff member indicated IFRS 20 would have clear guidance and illustrative examples to further help in the assessment of whether entities were under a direct (no direct) relationship.

Regulatory balances under current reporting versus regulatory assets (liabilities) expected to be reported under the new requirements

12 The EFRAG Secretariat clarified that there might be a difference between the regulatory assets and regulatory liabilities recognised under the application of IAS 8 or local GAAP and the expected regulatory assets and regulatory liabilities under IFRS 20 (i.e. due to different accounting requirements).

13 A member noted that, based on the inferred quick asset turnover, some of the respondent companies may have misclassified receivables under IFRS 15 as being current regulatory assets. However, other views were expressed that, for the mentioned cases, the classification was likely based on the application of IAS 8.

14 A member pointed to the need to distinguish between what relates to the consolidated financial statements and separate financial statements due to the unbundling arrangements that were in place for some grid operators.

Inflation adjustments

15 Members noted that differences in timing arise when regulatory schemes adjust the RCB for inflation purposes (i.e. a real rate of return is applied). It was noted that in some jurisdictions like the UK, the inflation-related differences in timing could be significant.

Regulation review

16 Members questioned the disconnect between the minimal level of cost-based schemes reported in the regulatory review at an aggregated level versus the higher proportion of these schemes depicted in the survey results. It was explained that the aggregate picture reflected the regulator's characterisation of the schemes at a country level.

Description of motorway regulation in Italy

17 A member described the tariff mechanisms applied in the Italian motorway sector. The effective tariff is a sum of three components: management component, construction component and supplementary charges. The incurred costs are added or deducted from the tariff to linearise/smooth the tariff charged until the end of the concession and avoid unexpected increases/decreases due to changes in investments.

18 The management component includes:

(a) the reimbursement of eligible operational costs, determined based on the financial statements of the previous financial year, which are corrected to take into account the trend of inflation expected at the time and a productivity coefficient; and

(b) the remuneration of non-reversible assets.

19 The construction component is represented by the remuneration of reversible assets. Reversible assets to be realised are remunerated at the weighted average cost of capital (WACC), while reversible assets realised or in progress are remunerated at the internal rate of return (IRR) of the previous tariff system.

20 Supplementary charges are reimbursements of specific charges paid to the state or other identified entities in relation to any legislative/regulatory changes that generate an increase in costs to be paid.

21 The net invested capital is defined in accordance with national accounting standards. There is a reconciliation between the net invested capital and financial reporting, but it is multi-layered.

Endorsement process

22 In response to the EFRAG FR TEG Chair's question about the pace of the endorsement process, a majority of members that spoke agreed that there was no need to speed up the transition to the new requirements for the following reasons:

(a) It was important to have a robust standard, especially as a result of the introduction of the direct (no direct) relationship concept;

(b) It was a complex standard, and time was needed to bring together regulatory schemes, corporate reporting, developing IT processes and educating people;

(c) Some jurisdictions are undergoing changes in their regulatory frameworks so no fast-track endorsement was required; and

(d) the final wording of the proposals was important as the IASB had not tested the standard in its entirety and the direct (no direct) relationship was introduced after the ED.

23 However, several members supported a fast-paced endorsement process to allow early application by EU entities so that they are not disadvantaged relative to other jurisdictions. It would also facilitate the timely financing of infrastructure projects that may otherwise be impacted by the absence of an IFRS Standard.

Next steps

24 In early June 2025, EFRAG will receive for review a confidential draft of IFRS 20 including illustrative examples and the Basis for Conclusions. The IASB representative explained that:

(a) the focus of the review will be the clarity of the drafting and consistency within and across other standards;

(b) comments are welcomed on the illustrative examples, but no comments are needed on the basis for conclusions;

(c) the review draft can be shared with the EFRAG RRAWG members to elicit their comments but only one consolidated response is expected from EFRAG.

25 EFRAG will present the expected key issues of IFRS 20 at the ARC meeting on 24 June 2025.

26 The EFRAG RRAWG chairman proposed a physical meeting of the group in early July to discuss the ballot draft. Tentatively, this meeting will also discuss the May 2025 IASB decisions on sweep issues, the IASB staff's cost-benefit analysis and field-testing results that will be presented at the July ASAF meeting and discussed at the EFRAG TEG-CFSS

meeting, and EFRAG RRAWG members' views on the forthcoming IASB agenda consultation.

27 The EFRAG Secretariat will follow up on the areas of focus identified from the survey and will extend the review of regulations beyond the electricity and gas utilities and to cover a wider set of EU member states.

28 IFRS 20 is expected to be published in H2 2025 and have an effective date of 1 January 2029 with early adoption permitted.

Question for EFRAG FR TEG

29 Does EFRAG FR TEG have any comments on this report?