

## FINANCIAL VS. REGULATORY ACCOUNTING: THE CASE OF THE CONTINGENCY TARIFF AT THE DISTRITO FEDERAL WATER SUPPLY SERVICE

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### ABSTRACT

With the critical situation of water scarcity that ravaged Distrito Federal from 2016 to 2017, the local regulatory agency – ADASA – has edited regulations authorizing and disciplining the collection of the contingency tariff for water supply services in the region offered by CESB. However, these regulations generated conflicts of technical and practical guidelines regarding regulatory and accounting aspects. In this context, the present teaching case proposes the analysis of regulatory and corporate standards on the resources raised with this tariff, and the treatment of these resources in the light of the Accounting Theory and the Accounting Technical statements issued by CPC. Built from the financial statements of CAESB, together with documents published by the concessionaire and the regulatory agency, it is pointed out that the company complies with the one established by the regulatory agency, but practices additional operations that are not clarified in explanatory notes. The purpose of this case is to discuss the recognition of the contingency tariff as other revenues. Upon considering that the regulations restrict access to and use of the resources derived from this tariff, recognition as a provision would provide preservation of the concessionaire's economic-financial health. In this teaching case, therefore, it is noteworthy that accounting practices regarding the contingency tariff may not be in compliance with the current accounting statements and the accounting theory, thus allowing discussion and application of key accounting concepts for students of undergraduate and graduate courses in the area.

**Keywords:** Corporate Accounting. Regulatory Accounting. Contingency Tariff.

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## 1 UNDERSTANDING THE CONTINGENCY TARIFF CASE

With the objective of standardizing the concept and establishing national guidelines for basic sanitation, Federal Law no. 11.445 was enacted and sanctioned on January 5<sup>th</sup>, 2007, which became known as the Sanitation Law and universalized the sanitation service, by making explicit all the responsibilities of the companies holding the provision of this service. Another point highlighted by the legislation is that, for the exercise of ownership, companies are subject to the subordination of an official responsible for the regulation and supervision of the service provision. The regulatory agent has the principles of decision-making, budgetary and financial independence; transparency; technicity; and agility and efficiency in decisions (Lei n.º 11.445, 2007).

In the scope of the Sanitation Law, in Distrito Federal, the Distrito Federal Water and Sanitation Regulatory Agency (ADASA) has competence to regulate and supervise the concessionaire's actions in the administrative, accounting, commercial, technical and economic-financial areas. In September 2016, the agency declared a state of restriction on the use of water resources and established the regime for the rationing of water supply service in the DF (Resolução n.º 15, ADASA, 2016). The following month, using the provision of the said law, ADASA established the contingency tariff for the Distrito Federal public water supply services, Provided by the Environmental Sanitation Company of Distrito Federal (CAESB). The objective was to preserve the proper levels of the reservoirs and to reduce consumption until the total recomposition of the supply reservoirs (Resolução n.º 17, ADASA, 2016). In ADASA Resolution no. 17 of October 07<sup>th</sup>, 2016, the method of calculation and accounting recording procedures of the contingency tariff were defined, including the incidence of taxes and the obligation of CAESB to apply the invoiced resources as a contingency tariff.

Considering the specificities of CAESB, ADASA, and the particularities of a public service concession contract, CAESB is governed by the Corporate Law and, therefore, must follow the international accounting standards required by the Brazilian Corporation Law (Law 6.404/76 and its amendments). for treatment and recognition of the contingency fee. However, ADASA argues that regulatory accounting provides “viable information for the study of quantitative and qualitative variations inherent to the activities carried out by the water supply and sanitation services in the country” (ADASA, 2016, p. 10).

In view of the above, there is a conflict of technical and practical guidelines regarding the regulatory and accounting aspects (corporate and, including, inspection and tax) of the contingency tariff – this being the focus of the present teaching case. In particular, this stalemate caused, as in the electrical sector, a material for the sanitation sector to be created to assist in these guidelines conflicts. Such as ADASA, at the time, regulatory agencies from other states also created the so-called Regulatory Accounting Manuals to guide the treatment and recognition of contingency tariffs. The intention was to discipline the concessionaires – in DF, CAESB – to adopt new accounting practices, based on corporate legislation, but within the characteristics of the activity and object of the contract, in this case, sanitation (ADASA, 2016).

In the academic literature, some studies in Brazil deal with the analysis of the regulatory environment against accounting standards and practices adopted by public service concessionaires (Brugni, Rodrigues, Cruz, & Szuster, 2013; Dantas, 2013; Ferreira, Ribeiro, Milhomem, & Carmo, 2021; Gouveia, 2010; Hoppe, 2012; Martins & Silva, 2018; Moraes, Souza, & Vendruscolo, 2020). Although there are differences, Hoppe (2012) and Dantas (2013) agree that there is a positive intention of the public service companies – participants in the concession contract – to prepare and disclose the regulatory financial statements in accordance with international accounting practices, since international accounting changes are pertinent and add value to accounting information because they have greater explanatory power in relation to the value of companies (Ferreira et al., 2021; Gouveia, 2010). On the other hand, Hoppe (2012) and Dantas (2013) believe that there is a need for more detail in the information processing and, therefore, care for asymmetry, since the

effects resulting from the adoption of international standards may cause risks to companies. In addition, there are understandings about the difference in the predictive value of accounting information based on the corporate or regulatory model (Flores & Lopes, 2019; Loudder, Khurana, & Boatsman, 1996).

The Regulatory Accounting Manual of the concessionaire of Distrito Federal Public Water Supply and Sanitation Services, elaborated by ADASA, is considered as an “essential support to ensure the financial supervision of the public service provider, The economic-financial balance of the Contract for granting services and the tariff modification for the consumer” (ADASA, 2016, p. 10). The Manual and the Regulatory Accounts Plan became mandatory for CAESB, starting January 01st, 2019, but were already used as a reference since the beginning of the 2017 social exercise.

Whereas the contingency tariff, as mentioned, was in force, starting with Resolution number 17, of October 07th, 2016. This resolution determined that the use of financial resources from the contingency tariff would depend on prior authorization from ADASA, but stipulated that the resources should be intended to cover additional operating costs and capital costs. Among others, the concessionaire would also have an obligation to provide specific assistance to claims on the application of the contingency tariff; to promote advertising campaigns and actions; to discriminate separately on invoices issued for the amounts invoiced due to the contingency tariff; etc. in cases of resource existence at the end of the critical state of water scarcity, the resolution provided for authorization for future investments and the possibility of tariff reversal, reducing the next tariff adjustment.

Also in this resolution, it was defined that the net contingency tariff revenue would correspond to the values accounted for under the heading “contingency tariff revenue” deducted the tax incidents on the turnover. In particular, the resources of the contingency tariff would correspond to the net contingency tariff revenue, deducted from the balance of net accounts receivable of the estimated losses in doubtful settlement credit, increased income generated by the financial investment of available balances originating in their collection (Resolução n.º 17, ADASA, 2016).

During the six months in which the contingency tariff authorized by ADASA was in force in Distrito Federal, between December/2016 and May/2017, the amount invoiced by CAESB with this tariff was approximately R\$ 86 million (including taxes). In this context, the present teaching case has as its object the discussion of these resources raised by CAESB as a contingency tariff. Although ADASA regulates the accounting and financial treatment of these resources, the adequacy of the treatment is questioned in the light of the Accounting Theory and the Accounting Technical statements edited by CPC. Thus, the general objective is to promote a discussion based on the analysis of the rules governing the amounts charged as a contingency tariff, and the treatment of these resources. Specifically, the aim is to discuss the adequacy of registration and treatment, as well as the quality of the reports released, while considering the following perspectives: (1) initial record (in the turnover) based on the classification of revenue, whether operational or non-operational; (2) initial record (in the turnover) based on the classification as provision; (3) record when receiving the values; and (4) record when applying the collected values.

The motivation of this teaching case is due to the understanding of the relevance of the discussion about the resources collected via the contingency tariff. Therefore, the following scenarios are taken as a basis for discussion: (i) in the light of corporate accounting – since CAESB is a mixed-economy company governed by the Corporate Law; and (ii) in the light of regulatory accounting – considering the competence of ADASA for regulation and inspection of concessionaire shares in the administrative, accounting, commercial, technical and economic-financial areas. To this end, the concepts and regulations pertinent to the topics of revenue, concession and provision should be raised, since these topics are relevant to the discussion about the collection and application of resources related to the contingency tariff.

Based on these concepts and regulations, two lines of reasoning are outlined on the treatment and recording of the invoiced values received as a result of the water contingency surcharge, specifically: (i) the contingency tariff is a non-operational revenue of CESB; and (ii) the contingency tariff should be recorded through a provision.

The teaching case here involves a mixed economy society (CAESB) and a sanitation regulatory agency (ADASA), both representatives of Distrito Federal water, sewage and sanitation system. Despite dealing with specific agents, all discussions and data processing involve public and widely disclosed information on corporate electronic sites and news media. For this reason, there was no appraisal of this study by the companies and the information discussed here is available for consultation during the application of the teaching case.

## 2 DATA ON THE CONTINGENCY TARIFF

As a way of illustrating – by means of real values – the discussion on the contingency tariff, there is a brief description and analysis of the financial statements and some financial reports of CAESB, where it is possible to identify accounting practices adopted for the contingency tariff mechanism by CAESB in 2017.

Table 1 shows the invoiced and collection values of the contingency tariff for the period of its duration. Such values were available on the company's electronic site. However, when analyzing the financial statements of the company's 2017 year, the contingency tariff was mentioned, but its values were not described in detail.

Table 1  
Detailing of CAESB turnover and contingency tariff collection

| Reference Month | Invoiced Amount   | Collection        | Federal Taxes     | Income           | Contingency Tariff Collection Balance | Additional Efficient Operating Costs | Additional Capital Costs |
|-----------------|-------------------|-------------------|-------------------|------------------|---------------------------------------|--------------------------------------|--------------------------|
| Dec/16          | R\$ 7,183         | R\$ 2,488         | R\$ 1,861         | R\$ 0            | R\$ 627                               | R\$ 0                                | R\$ 0                    |
| Jan/17          | R\$ 17,460        | R\$ 7,138         | R\$ 1,995         | R\$ 0            | R\$ 5,143                             | R\$ 0                                | R\$ 0                    |
| Feb/17          | R\$ 20,357        | R\$ 11,125        | R\$ 2,585         | R\$ 3            | R\$ 11,128                            | R\$ 0                                | R\$ 0                    |
| mar/17          | R\$ 13,069        | R\$ 17,541        | R\$ 2,174         | R\$ 52           | R\$ 15,008                            | R\$ 0                                | R\$ 0                    |
| Apr/17          | R\$ 14,784        | R\$ 12,152        | R\$ 2,703         | R\$ 208          | R\$ 10,186                            | R\$ 0                                | R\$ 0                    |
| May/17          | R\$ 13,229        | R\$ 13,071        | R\$ 2,494         | R\$ 402          | R\$ 10,771                            | R\$ 0                                | R\$ 0                    |
| Jun/17          | (R\$ 144)         | R\$ 9,187         | (R\$ 10)          | R\$ 434          | R\$ 7,127                             | R\$ 0                                | R\$ 0                    |
| Jul/17          | (R\$ 363)         | R\$ 2,628         | R\$ 546           | R\$ 463          | R\$ 3,101                             | R\$ 820                              | R\$ 138                  |
| Aug/17          | (R\$ 146)         | R\$ 1,456         | R\$ 559           | R\$ 471          | R\$ 1,381                             | R\$ 0                                | R\$ 1,633                |
| Sep/17          | (R\$ 294)         | R\$ 920           | R\$ 5             | R\$ 365          | R\$ 725                               | R\$ 160                              | R\$ 2,915                |
| Oct/17          | (R\$ 54)          | R\$ 626           | R\$ 26            | R\$ 358          | R\$ 979                               | R\$ 1,069                            | R\$ 1,888                |
| Nov/17          | (R\$ 25)          | R\$ 483           | R\$ 25            | R\$ 293          | R\$ 749                               | R\$ 0                                | R\$ 4,662                |
| Dec/17          | (R\$ 5)           | R\$ 489           | R\$ 37            | R\$ 271          | R\$ 735                               | R\$ 0                                | R\$ 1,678                |
| <b>Total</b>    | <b>R\$ 85,050</b> | <b>R\$ 79,304</b> | <b>R\$ 15,000</b> | <b>R\$ 3,320</b> | <b>R\$ 67,660</b>                     | <b>R\$ 2,049</b>                     | <b>R\$ 12,915</b>        |

**Note.** Amounts in thousands of reais.

Source: <https://www.caesb.df.gov.br/agua/crise-hidrica-historico/tarifa-de-contingencia.html>

Considering the possibility of reversing the amounts raised with the contingency tariff at the end of the critical situation of water scarcity, CAESB could incur a cash outflow of approximately R\$ 53 million (Net revenue collected excluding efficient and additional capital operating costs – see Table 1).

The contingency tariff has a specific nature, created by regulation, and of interest to the most diverse users, because its use is regulated and there is the possibility of returning this tariff to consumers who have been charged. In an attempt to identify the values in Table 1 in the 2017 financial statements, there was a limitation of presentation and *disclosure* in the information provided by CAESB. In particular, there was difficulty understanding the values related to the

contingency tariff and there was no specific note or values discrimination of the demonstrations themselves. However, in order to comply with the principle of effectiveness and transparency, it should be described – at least in explanatory notes – the treatment and recording of these values (Resolution ADASA number 15, 2016).

The only quote to the contingency tariff relates with the "suppliers and other accounts payable" note. It should be noted that under this heading – under the subclassification of "Special Obligations" – in addition to the values received from the contingency tariff, the amounts received as transfers of the Federal Government under the Growth Acceleration Program (PAC), which should also have specific destination/application. In summary, it is verified that the set of information published by CAESB, in addition to the company's financial statements, did not assist the user in understanding the operational procedures related to the contingency tariff.

With the analysis of the information disclosed by CAESB on the contingency tariff and with the reflection on the normative and conceptual aspects of this subject, it can be assumed that CAESB is following the standards established by the regulatory agency when recording the values raised with the contingency tariff as "other revenues", but it is believed that this is not the most appropriate accounting taking into account the essence of the form and corporate standards.

Also, despite the positive intention to follow the regulatory standards, it is verified that the concessionaire has finally adopted additional procedures to inform about the collection and destination of the contingency tariff resources. However, there is a lack of transparency and consistency with the information disclosed in the financial statements. It should be noted that the accounting practices edited by ADASA, in addition to controversial ones, could be at odds with the current accounting statements. Due to that, it would be up to the regulatory agency to make a normative review in order to modify accounting practices for the treatment and recording of the contingency tariff, so that the economic essence of the fact/act is recorded.

Corroborating previous ideas (Dantas, 2013; Hoppe, 2012), further details are still necessary in the information processing required by the regulatory agencies and, therefore, care for informational asymmetry. This is because, in addition to the effects resulting from the adoption of international standards, the reception of these standards in regulatory accounting may cause risks to companies.

### 3 TEACHING NOTES

#### 3.1 Data Sources

The data collection for teaching case focused on Federal Law number 11.445/2007, Resolutions number 15/2016 and number 17/2016, and on the Regulatory Accounting Manual (ADASA, 2016), sent by ADASA. On the basis of these documents, it is therefore aimed to have an understanding about the adoption of contingency tariff mechanisms in Distrito Federal and the effects on the accounting of the concessionaire of Distrito Federal water and sanitation services, CAESB.

In order to analyze the accounting procedures of the contingency tariff in the light of accounting theory and corporate standards and in the light of tax and tax regulations, the references suggested for reading are:

- i. Hendriksen e Van Breda (2010);
- ii. Gelbcke, Santos, Iudícibus e Martins (2018);
- iii. Technical statements and Interpretations edited by CPC/IASB:
  - a. CPC 00 (R2) – Conceptual Structure for Financial Reporting;
  - b. CPC 25 – Provisions, Contingent Liabilities and Contingent Assets;
  - c. CPC 30 (R1) /IAS 18 – Revenues (repealed as of 01/01/2018);
  - d. CPC 47/IFRS 15 – Contract Revenue with Customer;
  - e. ICPC 01 (R1) /IFRIC 12 – Concession Contracts.

For the discussion of the concepts and standards related to revenue, discussions are brought with the previous standards (CPC 30 and IAS 18) and with the current standards (CPC 47 and IFRS 15), since the case analyzed occurred in 2017, that is, during the duration of the previous standards. The central discussion of the case, however, is current and is therefore also discussed by the views of the current standards. In addition, in a possibility of a return to the contingency tariff, the current rules would be considered. In this sense, it is considered relevant to bring both scenarios to the discussion of the revenue accounting aspect.

Finally, to exemplify the normative-conceptual discussion about the treatment and recording of contingency tariff resources, it is necessary to analyze the financial statements, the independent auditors' report, the management report and the table, disclosed by CAESB for the year 2017, detailing the values regarding the tariff. Among the limitations of the present case, the lack of information disclosed specifically in the financial statements on the contingency tariff is highlighted.

### **3.2 Learning objectives and public indication for use of the teaching case**

The subject of the case is relevant to society in general, due to the fact that CAESB, as responsible for the custody of the funds raised with the contingency tariff, should be supervised not only by the regulatory staff, but by all citizens. Thus, the case opens precedents for future studies, specifically for further analyzes of the standardization on the contingency tariff, and, in general, on the differences between regulatory and corporate accounting, including in the light of the Accounting Theory, in view of the scarcity of studies on this subject. In addition, comparisons with similar situations in other entities in the same sector or even in other sectors can help in regulatory and accounting development as a whole.

The present teaching case can be used to contribute to discussions with undergraduate or graduate level accounting students, specifically in the disciplines of accounting theory, corporate accounting, general accounting and regulatory accounting. Some contributions arising out the discussion are:

- i. Knowledge aggregation: the student shall carry out studies to understand the normative knowledge relevant to the discussion of the case.
- ii. Discussion of concepts and articulation: based on normative studies and the context of the case, the student may discuss accounting concepts – which are not objective and fixed – in order to improve his or her capacity for articulation about the best application of the various concepts.
- iii. Judgment ability: based on the discussion of concepts, the student may exercise his or her professional judgment ability to decide the best scenario, under the theoretical aspects of regulatory and fiscal accounting.

## **4 THEORETICAL EXPOSURE AND QUESTIONS FOR DISCUSSION**

### **4.1 Theoretical exposure**

Discussions about the differences between corporate accounting and regulatory accounting (from specific sectors) are not recent in literature and accounting profession. (D'Souza, 1998, 2000; Louder et al., 1996) Despite this, they continue to be contemporary discussions, both in academic literature and in practical regulatory needs (Jin & Niu, 2021; Martins & Silva, 2018; McCandless, 2016; Scalzer, Rodrigues, Macedo, & Wanke, 2019).

By recognizing the possible specificities of each sector, the international regulatory agency (IASB) conducts processes in order to try to integrate societal issues with regulatory specificities. The relevance of the topic is ratified by observing that there is currently a project focused precisely on activities regulated by means of tariff - *rate-regulated activities* with the application of the

recognition of regulatory assets and liabilities in the corporate financial statements. The project started in 2012 and is currently under *exposure draft* issued and the comments are in the process of analysis (IASB, 2021).

It is emphasized here that the corporate accounting derived from the International standards (IASB) – which in Brazil are translated by the CPC – is also regulated accounting, but in a *soft-law* model. A distinction is therefore needed on the terms that come from the regulatory discussion. It is understood, in the approaches here, that the international and national accounting standards issued by the IASB and CPC, respectively, are the corporate standards. The standards derived from regulatory accounting are those of specific sectors, such as electricity, financial institutions, pension funds, water and sanitation, among others. In these regulatory standards, there are rules and specific treatments to the sector due to the tariffs collection by companies. Therefore, “prepared and published financial information for regulatory purposes usually differ significantly from other information prepared by companies for statutory reasons” (Wanderley, Cullen, & Tsamenyi, 2011, p. 54).

Understanding that there are differences between the corporate accounting information and the regulatory accounting information of the different sectors, discussions can be treated both under theoretical aspects of recognition, measurement and presentation (as done in this case study) and on the effectiveness of information on different standards. These discussions refer mainly to the recognition or non-recognition of regulatory assets and liabilities due to the possible mismatches of this property information with the recognition of tariff revenues (D’Souza, 2000; Flores & Lopes, 2019; Jin & Niu, 2021; Scalzer et al., 2019).

Considering the difference in understanding this phenomenon, studies have observed that in the Brazilian electricity sector, which has its own accounting model and is recognized by investors, information without the recognition of regulatory assets and liabilities has less *value relevance* when compared to information with the recognition of these assets and liabilities (Flores & Lopes, 2019). This means that the price of the shares has a greater explanation when compared to the information considering the regulatory assets and liabilities than with the current corporate information, in which such assets and liabilities are not recognized. Corroborating this finding, it was identified, in a research carried out with financial analysts, that analysts understand that regulatory statements are more appropriate for analyzes than corporate statements (Martins & Silva, 2018). However, this is not a unified vision, which tends to increase the breadth of the debate (Ferreira et al., 2021).

Based on the differences of understanding for criteria of recognition, measurement and presentation among regulatory bodies in specific sectors (in the case of the present case, ADASA) and corporate accounting, the direction is then to a discussion of the main accounting concepts in order to subsidize the case under analysis.

In the light of the Accounting Theory and considering the accounting regulations in force, there are three central concepts that should be considered for discussion of the contingency tariff case: revenue, concession and provisions.

Different regulations (*e.g.*, international, corporate and fiscal) have been recorded on **accounting revenue**, and the conceptual discussion is relevant because, according to the regulatory agency, the contingency tariff should be recorded as revenue. Therefore, the International Accounting Standard Board (IASB) definition of revenue is initially taken. According to the *International Accounting Standard 18* (IAS 18), revenues are only gross inflows of economic benefits received and to be received by the entity on its own account. The amounts collected on behalf of third parties (*e.g.*, taxes on sales, goods and services and on value added) are not economic benefits and do not result in increases in net worth; therefore, they should be excluded from the revenue. The same reasoning applies to gross amounts inputs collected on behalf of the principal. In that case, the revenue shall be the amount of the commission (IASB, 2009).

In Brazil, the concept given by the Committee for Technical statement – CPC, in convergence with IASB, is presented and expressed in the “Conceptual Structure for Financial Report” (CPC 00-R2). Based on it, revenues are “increases in assets, or reductions in liabilities, which result in increases in net worth, except for those referring to contributions from property rights holders” (CPC, 2019, p. 28).

According to CPC 30 – *Revenues* (effective until Dec/2017), “revenues should be recognized when future economic benefits are likely to flow to the entity and these can be reliably measured” (CPC, 2012, p. 2). The economic benefit refers to the capacity of an action (act or fact) to contribute, directly or indirectly, to the entity's cash flow, in addition to the existence of a temporal limitation in the revenue, because such action should arise in the normal course of activities and cannot be related to the provision of resources from owners and partners.

For the correct treatment of revenues, the principle of the confrontation between revenue and expenditure should also be considered, which, within their respective competence regimes, is of fundamental importance in measuring the correct profit of each social exercise and, consequently, of the company's assets, whatever the activity it performs.

Unlike CPC 30, in the new CPC 47 statement – Contract Revenue with Customer – it presents a principles-based approach with more comprehensive guidance on the subject (Gelbcke et al., 2018). In particular, CPC 47 brings innovations in relation to CPC 30, because it applies to accounting for revenue of all contracts with customers, in which products or services are sold, including construction, which were previously governed by another statement (CPC, 2016). In this technical statement, revenue is represented by the “increase in economic benefits during the accounting period, originated in the course of the entity's usual activities, in the form of inflows or increases in assets or reductions in liabilities resulting in an increase in net worth, and that they do not originate from contributions of the participants' assets” (CPC, 2016, p. 25).

Regarding the inspection and tax regulations, the income Tax Regulation defines gross revenue as the “product of the sale of goods in own account operations, the price of the services provision in general and the result obtained in third-party transactions”, and net revenue such as gross revenue reduced from returns and canceled sales, unconditionally granted discounts, sales tax incidents and the amounts resulting from the adjustment to current value (Decreto n.º 9.580, 2018, art. 208). On a supplementary basis, CPC 47 introduced again the obligation to present the Gross Revenue Billing Account at the DRE. According to Gelbcke et al. (2018)t, Brazil introduced this provision, which does not exist in the original IASB standards, so that tax supervision can carry out its verifications.

Also on accounting standards, it is necessary to highlight the statements that are tangent to the discussion of revenue, whichever ones are relevant to the Concession Contracts. The remuneration received by the concessionaire for its services provided under a concession contract is within the scope of ICPC Technical Interpretation 01 (R1) – Concession Contracts. This document presents the characteristics of these contracts, namely: (a) the nature of the public service; (b) the party granting the service provision contract (grantor) is a public body or public entity, or private entity to which the service has been delegated; (c) the service contract expressly obliges the concessionaire to provide services to the public on behalf of the public body; and, (d) the concession holder is responsible at least for the management of infrastructure and related services, not acting merely as an agent on behalf of the grantor (CPC, 2011).

Due to these specificities of concession contracts, some questions may arise about accounting practices, mainly regarding the recognition of regulatory assets and liabilities by the service provider. In the view of Gelbcke et al. (2018), operations under concession contracts are not a consensus yet among the accounting regulatory bodies. Nevertheless, the ICPC 01 guidance is that the concession holder should account for operating services revenue and costs in accordance with CPC 47. The concession contract enters into the scope of the performance obligation fulfilled over time, and item 35 of CPC 47 clarifies that the entity transfers control of the good or service



and therefore satisfies the performance obligation and recognizes revenues over time, when the customer receives and simultaneously consumes the sanitation services provided by the concessionaire.

Finally, in the case of Distrito Federal, the regulatory agent determined that the concessionaire, from the invoicing of the contingency tariff, should be responsible for the application of the resources based on certain criteria, i.e. the collection had a specific purpose that would not be fully controlled by the concessionaire. For this reason, it is also necessary to discuss the concept and accounting treatment of **provisions**.

CPC 25 – Provisions, Contingent Liabilities and Contingent assets – sets out criteria for the recognition and measurement bases of provisions, liabilities and contingent assets. In addition, the statement seeks to guide the information disclosed in the explanatory notes to be sufficient and allow users to understand the importance of the information presented (CPC, 2009).

CPC 25 reaches all entities that make provision accounting, asset and contingent liability, except when there is another specific CPC on the theme. Based on this statement, recognition of a provision occurs when an event of uncertain value and/or maturity meets the following established criteria: (a) the entity has a present obligation (legal or non-formalized) as a result of past event; (b) an outflow of economic resources to settle the obligation is likely; and (c) a reliable estimate of the value of the obligation can be made (CPC, 2009, p. 5).

As to the formalization of a present obligation, it may be classified as legal when derived from a law, contract or actions of the law; and, not formalized, when there is no signed contract, but the entity announces in the market an action and, as a result, generates in the general public an expectation that the entity will deliver the promised.

Uncertainty guides the concepts of provisions, liabilities and contingent assets. For this reason, it is the responsibility of the entity to make an assessment of the output of resources and of the reliable basis for the estimated value of the obligation. The main question of whether or not to recognize provision is the estimate reliability of the obligation value. Since the reliability of the information disclosed cannot be adversely affected, it is therefore recommended to use conservative bases and the whole structure available for better values estimate (Gelbcke et al., 2018).

#### 4.2 Questions for discussion

The issues discussed here represent the visions that were taken by the analyzed entities, as well as possibilities for recognizing the contingency tariff under the support of accounting theory and corporate accounting regulations, also considering the specificities of the case, such as the form of collection, the use of the collected value and the possibility of returning the collected tariff in whole or in part. Therefore, questions and guided discussions are proposed, but not necessarily, for the application of the teaching case, these must be the only themes and possibilities for discussion.

##### Question 1: Is the contingency tariff a CAESB operating revenue?

Question 1 is relevant because it evokes the discussion about the treatment and recording of the values invoiced and received as a result of the water contingency surcharge; and the adequacy of the classification of these values as a revenue for CAESB. The main points that focus on this discussion refer to the understanding of income as a future economic benefit and to the confrontation of revenue with the expenditure generated to obtain it.

CAESB's operating revenues are direct revenues from the provision of water supply and sanitary sewer system services in all categories (residential, commercial, industrial, public organs and exported water) (ADASA, 2016). Although the water supply service is one of the Company's

business objects and the concession contract, and the surcharge refers to this service, in essence the resources raised with the contingency tariff are not a CESB's revenue, according to corporate standards.

In other words, the essence of charging the contingency tariff is to overcharge the water service temporarily due to water scarcity, and does not refer to the water tariff itself. The legal provision for the adoption of tariff mechanisms (Lei n.º 11.445, 2007) clearly shows that the objective was to ensure the financial balance of service delivery and the management of demand by the concessionaire. Therefore, if there were no financial imbalance, the resources raised as a contingency tariff should, in principle, be returned to taxpayers.

Without proving that this benefit flows to the concessionaire, the resources of the contingency tariff should not be counted in the Revenue group in the Income Statement for the Fiscal Year (DRE), for corporate purposes. This argument is added to the understanding of Iudicibus (2000, pp. 130–131), by highlighting aspects to be observed in the definition of assets, in which it discusses the essential nature of the economic benefit: “it must be included in the asset, in its concept, some specific right to future benefits [...] or, in a broader sense, the element must present a potential for future services (future cash flows) to the entity”.

Taking the treatment of the essence of how as the main rule for the preparation of financial statements – and considering the *True and fair view* as the basis for the system of accounting rules and statements – it is understood that the economic benefits result from actions with the capacity to contribute to the company's cash flows, either directly or indirectly. The understanding is that the resource can help the entity generate wealth or reduce expenses.

To complement the discussion, the principle of comparing revenues and expenses has to be based on the idea that, in order to generate revenue, the company incurs some expenses; then, for revenue recognition purposes, in accounting records, the revenue must be associated with an expense/cost to obtain it. In the case of CAESB, when the water supply service is overcharged, the concessionaire has an extra collection, which is associated with an obligation with the taxpayer and not with some expense incurred to obtain the contingency revenue.

In short, the amount collected/invoiced via the contingency tariff only has an expense characteristic when ADASA authorizes the use of the resources. In this case, the value was not controlled by the CAESB and has a specific destination. This principle of confrontation states that the revenues and expenses related to an operation are recognized in the same period (Lopes & Santos, 2003), a characteristic that is also not possible when it comes to the contingency tariff adopted in Distrito Federal.

In addition to the collection, it is also necessary to discuss the allocation of funds raised as a contingency tariff. In Article 46 of the Sanitation Law (Lei n.º 11.445, 2007), we can see the forecast of the tariff mechanisms adoption for the situation of scarcity or contamination of water resources and it is evidenced that the objective of the adoption of these mechanisms is to cover additional costs. Moreover, in the specific case of CAESB, the financial resources allocation of the contingency tariff received was predefined in Resolution ADASA number 17/2016, which, in general, limited to covering additional costs of scarcity, investing in the infrastructure of services provision already installed to meet the demands of scarcity, or, finally, return the money to the taxpayer.

Question 2: Considering that it is a revenue, is the contingency tariff an operational or non-operational revenue of CESB?

Considering initially the argument that resources from the water contingency tariff, in light of the essence of the form, was not a revenue that flowed to CAESB, it is understood that this should not be counted as revenue at the time of invoicing. However, since these resources were registered by CAESB, until then, as revenue, as a reflection exercise, the discussion about

classification as operating or non-operational revenue is encouraged, which directly impacts on the concessionaire's tax aspect. This reflection is also valid for possible reformulation of the CAESB account plan, as well as for the legal forecast of the possible full return of the contingency tariff values to the taxpayer. In this case, the return of funds raised as a contingency tariff may be provided by (i) credits in the water account or (ii) tariff readjustment (Resolução n.º 17, ADASA, 2016).

For regulatory purposes, ADASA, through the Regulatory Accounts Plan, established that resources received as contingency tariff are accounted for by CAESB in the account group "3.1 – Water Supply Service Revenues". Thus, the contingency tariff was treated as direct revenue for water supply and sanitary sewer system. Once recorded as Operational Revenue, the contingency resources would be deducted, for example, from services taxes. However, in Resolution number 17/2016, at that time, it was defined that the deductions from the contingency tariff would be PIS and COFINS only (Resolução n.º 17, ADASA, 2016).

In addition to the question of the essence over the form, the contingency tariff treatment recorded as operating revenue by CAESB may not be adequate for deductions from such contributions (*i.e.* PIS and COFINS). This is because the amounts invoiced as a tariff, and received by CAESB, could at some point be returned to the taxpayers. But, if the amounts received were deducted by taxes, the possibility of returning the contingency tariff in its entirety to the taxpayers could generate financial and fiscal imbalance.

Thus, it is understood that the determined accounting, *i.e.*, recording as operating revenue, was contradictory to the legal provision for the adoption of tariff mechanisms (Lei n.º 11.445, 2007), as well as to the fulfillment of the ADASA Resolution itself number 17/2016. In the event that this balance occurred at the end of the water shortage, the concessionaire would need a cash reserve to cover the portion of these resources that were paid in respect of taxes, fees and contributions in the invoicing. As an alternative – and continuing the conceptual reflection – there would be a possibility of recording the contingency tariff as non-operational revenue.

Non-operational revenues are those arising from transactions not included in the main activities that constitute an object of the company. In the case of CAESB, water and sanitary sewage system are known as indirect revenues, for example: connections, reconnections, sanctions, maintenance and repairs of hydrometers, extensions, among others (ADASA, 2016). It should be noted that, for corporate purposes, with the edition of Law number 11.941/2009, the designation "non-operating revenues and expenses" was replaced by the name "other revenues and other expenses".

When it comes to the surcharge as a revenue, in such circumstances, the corporate and regulatory effects were comparable. This is because, according to a note from the Regulatory Accounting Manual, at that time, "all revenues that do not come from the object of the concessionaire, but that also generate cash inflow should be recorded as Other Revenues" (ADASA, 2016, p. 230). Thus, in the possibility of recording contingency tariff resources as other revenues (or non-operational revenue), there would be no deductions of PIS and COFINS, safeguarding compliance with Resolution ADASA number 17/2016 and the Sanitation Law (Lei n.º 11.445, 2007), and thus allowing both the return of resources to the taxpayer in its entirety (*i.e.*, not deducted from services taxes), as well as the maintenance of the concessionaire's financial balance. In addition, it is understood that the specific record should occur in the sub-account of "3.4 – Other Revenues".

Thus, accounting for financial resources related to the contingency tariff as revenue seems to be mistaken because: (1) since it is not an economic benefit, it cannot be considered a revenue; (2) since it did not incur any expenditure and/or cost to obtain the extra revenue, according to the confrontation principle of revenue and expenditure, the revenue cannot be recognized; and (3) the record as operating revenues seems contradictory to regulatory standards.

Question 3: If the contingency tariff is not a CAESB operational and/or non-operational revenue, can you consider the recording a Provision?

Based on the understanding that the contingency tariff is not a service recipe for the concessionaire and in view of the whole discussion about the possible classification of the resources received as a contingency tariff, in light of the essence of the form, it is believed that the contingency surcharge product can adjust to the provision concept.

Together with the authorization to collect the additional percentage on water bill, ADASA linked to the use of the resources received from this surcharge to cover both operational and capital costs arising from the water crisis situation. Examples of operational costs were educational campaigns and drilling of artesian wells; and capital cost divided into two groups: emergency investments (purchase of pumps, replacement of damaged equipment, etc.) and structuring (replacement of networks, new sources of catchment, etc.) (ADASA, 2016).

As the purpose of the contingency tariff recovery was to ensure the financial balance of service provision and demand management, Resolution ADASA number. 17/2016 stipulated that if there were resources that were not committed to mentioned costs, at the end of the water crisis state, CEESB could request new authorization for future investments and, if so, replacement of additional costs; or it should reverse the tariff, reducing the next tariff readjustment (Resolução n.º 17, ADASA, 2016). In other words, CAESB would receive a cash amount, but it would not have decision-making independence on that resource, because it was a resource that was not entirely controlled by it, since it would depend on prior authorization from ADASA. Despite this, this resource would be under the responsibility/ownership of the concessionaire. These conditions set by the regulatory agency characterize a CESB's obligation.

To represent the transaction essence, CAESB could collect the resource and record for specific account until ADASA authorized its use. The balancing entry in the record would be a provision, which, as stated in CVM Resolution number 489/05 and according to international standards, refers to liabilities with uncertain maturity or value. Also, resuming CPC 25, the provision is recognized when: (a) the entity has a present obligation (legal or non-formalized) as a result of past event; (b) an outflow of economic resources to settle the obligation is likely; and (c) a reliable estimate of the value of the obligation can be made. When analyzing the criteria for recognition of the provision, it is noted that the resources of the contingency tariff are in accordance with the three criteria determined by the statement.

Therefore, when ADASA defines the possible destinations of the resources received as a water service surcharge, a CESB's obligation is created concerning this resource. When authorizing the resources applications by the regulatory agency, there would be an outflow from CAESB's economic resources both to cover additional operating costs and capital costs, and to reverse the contingency tariff, if there were accounting balances at the end of the water scarcity.

Still with the objective of advancing this alternative, it is introduced the relation of cash accounting and competence regimes. It is understood that at the first moment (competence), when invoicing the water service surcharge, this value should be provisioned and in return an asset of values to be received – contingency tariff would be generated. At the second moment (cash), when the Company received the amounts, it would lower the right to receive – contingency tariff – and allocate the resource received in a specific bank account, as defined in Resolution ADASA number 17/2016. This resource, still according to the regulation, must remain in bank account until the use is authorized, when the provision would then be reduced, concomitant to the use/application of the resources so far accumulated.

It is noted that the water surcharge resources would not pass through the concessionaire's result at the time of collection, which allows to preserve these values of possible taxations and/or distributions, considering that such resources are not CAESB's revenue. Furthermore, as one of the destinations foreseen by ADASA was the possibility of reversing the contingency tariff to the

customer, CEESB would need to have the full value received. Thus, due to the alternative form of treatment and accounting of the contingency tariff resources, regardless of whether there is a positive bank and accounting balance, the Company's cash flow would be preserved and the setback of Resolution number 17 and the Regulatory Accounting Manual would be resolved.

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