



EFRAG  
35 Square de Meeûs (fifth floor)  
1000 Brussels  
Belgium  
Essen, April 23, 2013

*Comment Paper Emissions Trading Schemes*

Dear Sir or Madam,

The International Energy Accounting Forum (IEAF) consists of the major European companies in the energy business (see the list of our members in appendix 1).

The goal of the IEAF is to discuss and formulate best practices, to reduce areas of difference in accounting in the sector, to advocate the energy industry's point of view, and to make specialist energy industry knowledge available to the International Accounting Standards Board and other standard setters.

We are writing to you with respect to your Draft Comment Paper Emissions Trading Schemes.

The European companies in the energy sector already focused on this important issue several years ago with the aim to document best practice principles for the accounting treatment of emission allowances for the energy industry. The deliberations by the IEAF have resulted in a best practice paper which is published on our homepage [www.ieaf-energy.com](http://www.ieaf-energy.com).

**We believe that no specific accounting guidance is needed as the implemented accounting approaches in the energy industry and beyond lead predominantly to the same result in the income statement and ensure a fair presentation of the underlying business model.**

Afterwards we would like to convey our comments to your Draft Comment Paper.



No. 28: Do you agree that specific accounting guidance is needed? Please explain why.

Several years ago IEAF published a paper “Accounting for Emission Allowances” (IAS 39 Paper – No. 4) which has the objective to establish best practise principles applicable to the recognition and measurement of emission allowances of the EU Greenhouse Gas Emission Trading Scheme (EU ETS) that lead to a fair presentation of the business models of the energy industry in the financial statements.

This paper is based on and complies with current International Accounting Standards (“IAS”). In detail the following standards are used: IAS 2 ‘Inventories’, IAS 20, ‘Accounting for Government Grants and Disclosure of Government Assistance’, IAS 37 ‘Provisions, contingent liabilities and contingent assets’, IAS 38, ‘Intangible Assets’, and IAS 39 ‘Financial Instruments: Recognition and Measurement’.

The basic principles of the IEAF best practice paper are applied to our knowledge by all major energy entities, therefore the effects on the income statements are comparable within the energy industry.

As a consequence there is no urgent need to come to a new standard. However, if the IASB decides to develop a new accounting standard it is important to us that this new standard ensures a fair presentation of the underlying business model especially regarding the income statement. In this respect we strongly support your statement that the link between the emission allowances held and the obligation to redeem allowances to the authorities has to be taken into account when measuring the provision to redeem allowances.

No. 29: Do you agree with the arguments presented above? Should any other arguments be included?

We agree with EFRAG that emission allowances do not meet the definition of financial assets. From IEAF’s perspective emission allowances are intangible assets, so that IAS 38 on the one hand could be applicable. On the other hand they have some features (e.g. they are used in the production process in the normal operating cycle) which suggest that they are in the scope of IAS 2 ‘Inventories’.

As a consequence, emission allowances are intangible inventories, i.e. a hybrid, which has some similarities to intangible assets under IAS 38 and inventories under IAS 2. Therefore we feel that the conceptual debate is endless.

However, if emission allowances are held for broker-trader purposes they are in the scope of IAS 2.



No. 39/ No. 40: Do you agree with the analysis of information needs of users for each business model?

Do you agree that this should result in different accounting requirements?

IEAF totally agrees with EFRAG's view that consideration should be given to how an entity expects to use the emission allowances and that the information should result in different accounting requirements.

Generally, emission allowances are held for production purposes as well as for trading purposes in the energy industry. Emission allowances for production purposes are held in order to cover the entity's obligations from emissions made in the framework of the EU ETS. In this context, emission allowances are managed by the entities in the same way as any other commodity used for the production of electricity (e.g. coal, gas, oil). The basic principle of the entity's business model is to hedge the margin of the electricity production. In order to reduce their dependency on spot prices in the energy markets which may be of high volatility, the entities often sell their electricity capacity several years before production on a forward basis. To hedge the margin, raw materials like coal, gas or oil are purchased at the same point in time, usually also on a forward basis.

CO<sub>2</sub> emission allowances are managed in the same way as raw materials. This implies that the entities make sure to purchase emission rights on a forward basis at the same time when the electricity is sold, and not when emissions are made or the obligation to return emission to the relevant authorities has to be settled.

According to IAS 39 CO<sub>2</sub> emission allowances often meet the requirements of the own use exemption (cf. Paper on the accounting for own use contracts, IAS 39 Paper No. 2, IEAF). If the own use exemption in accordance with IAS 39.5-7 is not applied forward and future contracts for emission allowances are derivatives which shall be fair valued through profit or loss or might be used as hedging instruments.

Emission allowances held for trading purposes may be held as spot rights or – more usual – as forwards/futures. Derivatives held for trading purposes have to be fair valued through profit and loss under IAS 39. Inventories which meet the requirements under IAS 2.3 b are normally also fair valued through profit and loss by commodity broker-traders.

No. 56/ No. 57: Do you agree that free allowances should be measured at fair value at inception, this fair value being their deemed cost?

If not, what arguments detailed above do you not find convincing? How do you respond to them?

From our point of view measuring free allowances at fair value at inception is one possible option.



The allowances received for free are economically to be considered as grants and should as a consequence be accounted for as such in accordance with IAS 20, i.e. the recognition of these grants should not lead to a day-one gain as they relate to the whole year.

Under IAS 20 emission rights allocated for free could alternatively be measured at nil, i.e. that emission allowances received free of charge are recognised as government grants in accordance with IAS 38.44, as there are no specific rules in IAS 2 for emission allowances, in conjunction with IAS 20.23. In this case deferred income is recognised in the same amount either fair value or nil.

No. 70: Which of the above options would you support? Please explain why.

In the logic of the current accounting standards recognising deferred income is an adequate accounting approach. In this case emission allowances received free of charge should be recognised as government grants similarly to intangible assets in accordance with IAS 38.44, as there are no specific rules in IAS 2 for emission allowances, in conjunction with IAS 20.23.

With regard to a future standard we support not to recognise a Day-1 gain. From our point of view deferred income should still remain the preferred option.

No. 76/ No. 77/ No. 78: Do you agree that in a compliance model an entity should not offset the asset and the liability separately, because separate presentation provides more relevant information?

Do you agree that the liability should not be derecognised before the entity surrenders the rights to the Regulator (i.e. surrendering rights affects the entity's financial position and is not solely a compliance exercise)?

Do you agree that the entity's value changes with the act of emitting and that settling the obligation to the Regulator has economic value? Do you agree that balance sheet presentation is relevant to users?

IEAF's point of view is that recognition and presentation of income is of most importance.

With regard to the balance sheet presentation there are different alternatives.

On the one hand the gross presentation of asset and liability seems appropriate because the emission allowances are physically still existent and not consumed. On the other hand a net liability presentation where the emission rights held are "flagged" to settle the obligation is also an adequate alternative to the separate presentation of the asset and the liability.

In the end the balance sheet presentation is from our point of view not crucial. As long as both alternatives lead to the same result in the income statement and ensure a fair presentation of the underlying business model, the concurrent use of both described models should be possible.



No. 88: Do you agree or disagree with EFRAG's proposal on the subsequent measurement of assets and liabilities? Please explain why.

As to No. 79a: As we classify emission allowances as intangible inventories under IAS 2 they are measured at the lower of cost and net realisable value if they are deemed to be in the scope of IAS 2 and at cost less any accumulated impairment losses if they are deemed to be in the scope of IAS 38.

From our perspective, the assignment to IAS 38 or IAS 2 respectively, will not have any material impact on profit and loss and balance sheet.

It has to be taken into consideration that the net realisable value is not written down below cost if the finished products, e.g. electricity, in which they will be incorporated are expected to be sold at or above cost.

As to No. 79b: We agree.

As to No. 79c: We agree with regard to your approach regarding year end numbers.

As to No. 79d: We agree with EFRAG on condition that a gross presentation of asset and liability is applied.

No. 102: Which of the above alternatives would you support? Please explain why.

IEAF strongly supports the alternative that when an entity ends up with excess rights because of an unexpected lower consumption, selling the excess is not a change in the business model but it is simply an adjustment to the actual emissions (cf. No. 96).

No. 107: Which of the above alternative approaches would you prefer and why?

The IASB has classified "Emission Trading Schemes" within the context of their feedback statement to the IASB agenda consultation 2011 in December 2012 as a priority research project.

Last but not least we propose that EFRAG highlights the accounting treatment of CERs/ERUs which from our perspective should basically not differ from EUAs in respect of the issues raised in the EFRAG paper.

In case a project on emissions trading schemes started, we would support that its scope also comprises accounting for credit and baseline schemes such as green certificates schemes.

We would be happy to provide you with practical explanations of our industry, should you wish to further analyse these issues.



Yours faithfully

A handwritten signature in blue ink, consisting of a large, stylized loop followed by several vertical strokes and a horizontal line extending to the right.

On behalf of the International Energy Accounting Forum,

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## **Appendix 1: Members of the International Energy Accounting Forum**

Alpiq	<a href="http://www.Alpiq.de">www.Alpiq.de</a>
Axpo	<a href="http://www.axpo.ch">www.axpo.ch</a>
BG Group	<a href="http://www.bg-group.com">www.bg-group.com</a>
EDF	<a href="http://www.edf.com">www.edf.com</a>
EnBW	<a href="http://www.enbw.com">www.enbw.com</a>
EWE	<a href="http://www.ewe.de">www.ewe.de</a>
Fortum	<a href="http://www.fortum.com">www.fortum.com</a>
Gas Natural	<a href="http://www.gasnatural.com">www.gasnatural.com</a>
Gazprom Marketing & Trading	<a href="http://www.gazprom-mt.com">www.gazprom-mt.com</a>
GDF SUEZ	<a href="http://www.gdfsuez.com">www.gdfsuez.com</a>
Iberdrola	<a href="http://www.iberdrola.es">www.iberdrola.es</a>
OMV	<a href="http://www.omv.com">www.omv.com</a>
RWE	<a href="http://www.rwe.com">www.rwe.com</a>
Scottish Power	<a href="http://www.scottishpower.com">www.scottishpower.com</a>
Unesa	<a href="http://www.unesa.es">www.unesa.es</a>
Vattenfall	<a href="http://www.vattenfall.com">www.vattenfall.com</a>
Verbund	<a href="http://www.verbund.com">www.verbund.com</a>
Veolia	<a href="http://www.veolia.com">www.veolia.com</a>