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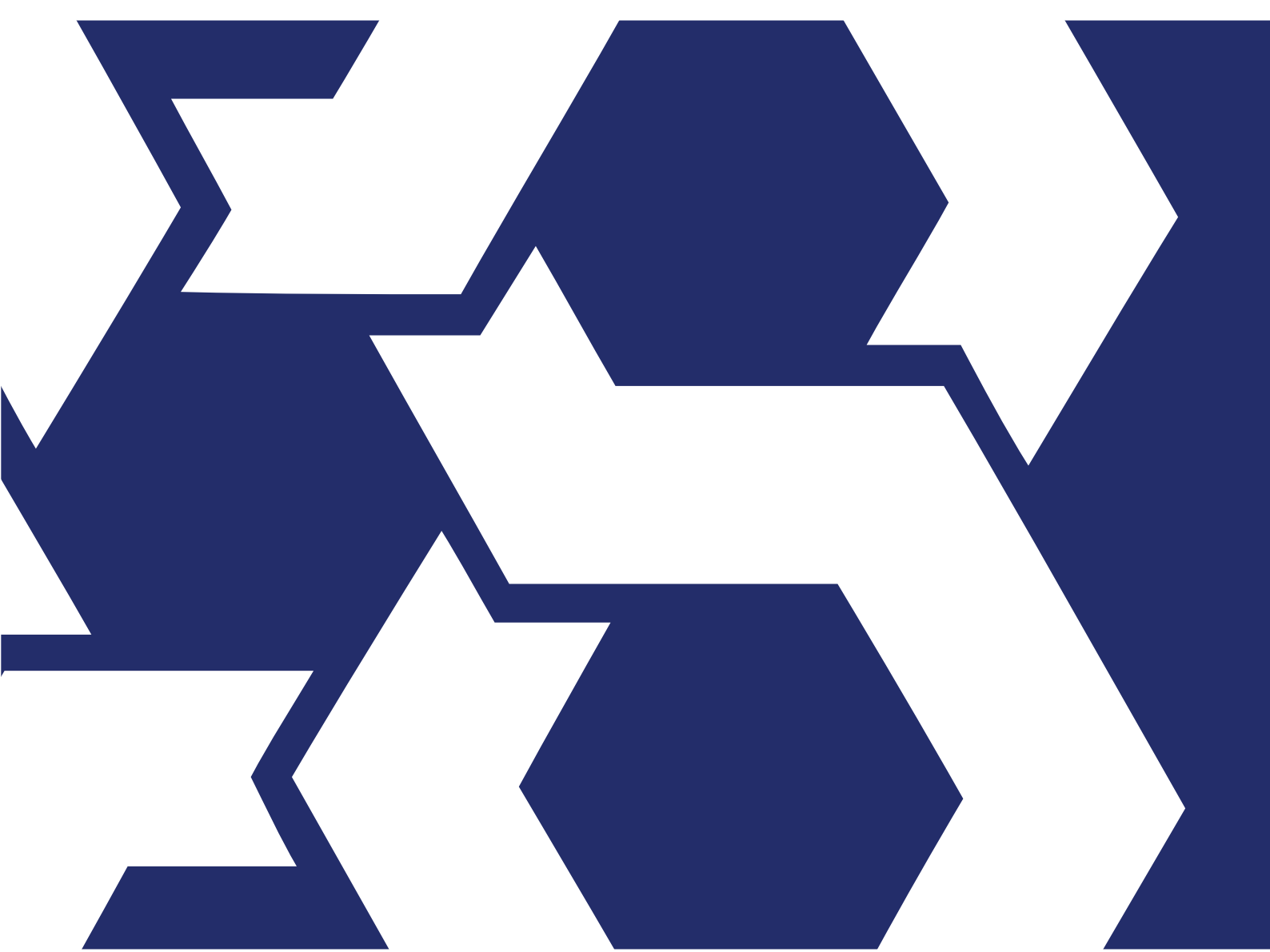
Exposure Draft

IFRS[®] Accounting Standard

Contracts for Renewable Electricity

Proposed amendments to IFRS 9 and IFRS 7

Comments to be received by 7 August 2024



**Exposure Draft
Contracts for Renewable Electricity**

Proposed amendments to IFRS 9 and
IFRS 7

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Exposure Draft *Contracts for Renewable Electricity* is published by the International Accounting Standards Board (IASB) for comment only. Comments need to be received by **7 August 2024** and should be submitted by email to commentletters@ifrs.org or online at <https://www.ifrs.org/projects/open-for-comment/>.

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CONTRACTS FOR RENEWABLE ELECTRICITY

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Introduction

Why is the IASB publishing this Exposure Draft?

- IN1 The IFRS Interpretations Committee (Committee) received a request about how an entity would apply paragraph 2.4 of IFRS 9 *Financial Instruments* to contracts to buy and take delivery of electricity produced from nature-dependent sources. The request said entities experience application challenges when applying the requirements in IFRS 9 to these contracts. These challenges arise due to the combination of:
- (a) the characteristics of the sources of renewable electricity production and the design and operation of the market in which the electricity is sold; and
 - (b) the ‘pay-as-produced’ features of the long-term contracts—commonly referred to as ‘physical power purchase agreements’ (physical PPAs).
- IN2 The Committee referred the matter to the International Accounting Standards Board (IASB) for its consideration. Stakeholders told the IASB during its research that applying the requirements in IFRS 9 to PPAs sometimes provided less useful information to users of financial statements. Additionally, stakeholders said a timely solution was needed because of an expected increase in the use of PPAs due to the increase in the demand for renewable electricity.
- IN3 Stakeholders also told the IASB that if it was to consider narrow-scope standard-setting for physical PPAs, it should also consider how an entity accounts for what is commonly referred to as ‘virtual PPAs’—PPAs that require net settlement of the difference between the prevailing market price and the contractually agreed price for the volume of electricity produced from a referenced production facility. The objective of both physical PPAs and virtual PPAs is to ensure access to renewable electricity and to fix the price per unit of electricity purchased or sold. Consequently, the economic outcomes of the two types of contracts are the same. In many cases, the design and operation of the electricity market determines the types of contracts entities can enter into.
- IN4 The IASB decided to add a narrow-scope standard-setting project to its work plan to propose amendments to IFRS Accounting Standards for contracts to buy or sell renewable electricity that have specified characteristics.

Proposals in this Exposure Draft

- IN5 The IASB proposes to amend IFRS 9 and IFRS 7 *Financial Instruments: Disclosures*, specifically:
- (a) the own-use requirements—to include the factors an entity is required to consider when applying paragraph 2.4 of IFRS 9 to contracts to buy and take delivery of renewable electricity for which the source of production of the electricity is nature dependent and the purchaser is exposed to substantially all of the volume risk;

CONTRACTS FOR RENEWABLE ELECTRICITY

- (b) the hedge accounting requirements—to permit an entity using a contract for renewable electricity with specified characteristics as a hedging instrument:
 - (i) to designate a variable volume of forecast electricity transactions as the hedged item if specified criteria are met; and
 - (ii) to measure the hedged item using the same volume assumptions as those used for the hedging instrument; and
- (c) the disclosure requirements—to add disclosure requirements to enable users of financial statements to understand the effects of contracts for renewable electricity with specified characteristics on an entity’s financial performance and on the amount, timing and uncertainty of the entity’s future cash flows.

IN6 The IASB is also proposing consequential amendments to the forthcoming IFRS 19 *Subsidiaries without Public Accountability: Disclosures* to add similar disclosure requirements.

Who would be affected by the proposals?

IN7 The proposed amendments could affect any entity that enters into contracts for renewable electricity with the characteristics described in this Exposure Draft.

Next steps

IN8 The IASB will consider the comments it receives on the proposals in this Exposure Draft and will then decide whether to amend IFRS 9 and IFRS 7.

Invitation to comment

Introduction

The IASB invites comments on the proposals in this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

- (a) respond to the questions as stated;
- (b) indicate the specific paragraph(s) to which they relate;
- (c) contain a clear rationale;
- (d) identify any wording in the proposals that is not clear or would be difficult to translate; and
- (e) identify any alternative the IASB should consider, if applicable.

The IASB requests that comments be confined to the questions asked in this Exposure Draft. However, respondents need not answer all the questions in this invitation to comment.

Questions for respondents

<p>Question 1 – Scope of the proposed amendments</p> <p>Paragraphs 6.10.1–6.10.2 of the proposed amendments to IFRS 9 would limit the application of the proposed amendments to only contracts for renewable electricity with specified characteristics.</p> <p>Do you agree that the proposed scope would appropriately address stakeholders’ concerns (as described in paragraph BC2 of the Basis for Conclusions on this Exposure Draft) while limiting unintended consequences for the accounting for other contracts? Why or why not?</p> <p>If you disagree, please specify with which aspect of the proposals you disagree. What would you suggest instead and why?</p>
<p>Question 2 – Proposed ‘own-use’ requirements</p> <p>Paragraph 6.10.3 of the proposed amendments to IFRS 9 includes the factors an entity would be required to consider when applying paragraph 2.4 of IFRS 9 to contracts to buy and take delivery of renewable electricity that have specified characteristics.</p> <p>Do you agree with these proposals? Why or why not?</p> <p>If you disagree, please specify with which aspect of the proposals you disagree. What would you suggest instead and why?</p>

Question 3 – Proposed hedge accounting requirements

Paragraphs 6.10.4–6.10.6 of the proposed amendments to IFRS 9 would permit an entity to designate a variable nominal volume of forecast electricity transactions as the hedged item if specified criteria are met and permit the hedged item to be measured using the same volume assumptions as those used for measuring the hedging instrument.

Do you agree with these proposals? Why or why not?

If you disagree, please specify with which aspect of the proposals you disagree. What would you suggest instead and why?

Question 4 – Proposed disclosure requirements

Paragraphs 42T–42W of the proposed amendments to IFRS 7 would require an entity to disclose information that would enable users of financial statements to understand the effects of contracts for renewable electricity that have specified characteristics on:

- (a) the entity's financial performance; and
- (b) the amount, timing and uncertainty of the entity's future cash flows.

Do you agree with these proposals? Why or why not?

If you disagree, please specify with which aspect of the proposals you disagree. What would you suggest instead and why?

Question 5 – Proposed disclosure requirements for subsidiaries without public accountability

Paragraphs 67A–67C of the proposed amendments to the forthcoming IFRS 19 *Subsidiaries without Public Accountability: Disclosures* would require an eligible subsidiary to disclose information about its contracts for renewable electricity with specified characteristics.

Do you agree with these proposals? Why or why not?

If you disagree, please specify with which aspect of the proposals you disagree. What would you suggest instead and why?

Question 6 – Transition requirements
<p>The IASB proposes to require an entity to apply:</p> <ul style="list-style-type: none">(a) the amendments to the own-use requirements in IFRS 9 using a modified retrospective approach; and(b) the amendments to the hedge accounting requirements prospectively. <p>Early application of the proposed amendments would be permitted from the date the amendments were issued.</p> <p>Do you agree with these proposals? Why or why not?</p> <p>If you disagree, please specify with which aspect of the proposals you disagree. What would you suggest instead and why?</p>

Question 7 – Effective date
<p>Subject to feedback on the proposals in this Exposure Draft, the IASB aims to issue the amendments in the fourth quarter of 2024. The IASB has not proposed an effective date before obtaining input about the time necessary to apply the amendments.</p> <p>In your view, would an effective date of annual reporting periods beginning on or after 1 January 2025 be appropriate and provide enough time to prepare to apply the proposed amendments? Why or why not?</p> <p>If you disagree, what effective date would you suggest instead and why?</p>

Deadline

The IASB will consider all comments received in writing by 7 August 2024.

How to comment

Please submit your comments electronically:

Online	https://www.ifrs.org/projects/open-for-comment/
By email	commentletters@ifrs.org

Your comments will be on the public record and posted on our website unless you request confidentiality and we grant your request. We normally grant such requests only if they are supported by a good reason, for example, commercial confidence. Please see our website for details on this policy and on how we use your personal data. If you would like to request confidentiality, please contact us at commentletters@ifrs.org before submitting your letter.

[Draft] Amendments to IFRS 9 *Financial Instruments*

Paragraphs 6.10.1–6.10.6, 7.1.12, 7.2.50–7.2.52, the sub-heading before paragraph 6.10.1 and the sub-heading before paragraph 7.2.50 are added. For ease of reading new text is not underlined. Paragraph 2.4 and the headings above paragraphs 2.4, 7.1.12 and 7.2.50 are not added but are included for ease of reference.

Chapter 2 Scope

...

2.4 This Standard shall be applied to those contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments, with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity’s expected purchase, sale or usage requirements. However, this Standard shall be applied to those contracts that an entity designates as measured at fair value through profit or loss in accordance with paragraph 2.5.

...

Chapter 6 Hedge accounting

...

6.10 Contracts for renewable electricity¹

6.10.1 Contracts for renewable electricity can be structured in many ways. Some contracts are structured as a normal purchase or a normal sale (an ‘executory contract’) of renewable electricity. Other contracts require net settlement of the difference between the prevailing market price and the contractually agreed price for the volume of electricity produced from a referenced production facility. An entity shall apply the requirements in paragraphs 6.10.3–6.10.6 to a contract for renewable electricity with both of the following characteristics:

- (a) the source of production of the renewable electricity is nature-dependent so that supply cannot be guaranteed at specified times or for specified volumes. Examples of such sources of production include wind, sun and water.
- (b) that contract exposes the purchaser to substantially all the volume risk under the contract through ‘pay-as-produced’ features. Volume risk is the risk that the volume of electricity produced does not align with the purchaser’s demand for electricity at the time of production.

¹ For ease of reading, all the proposed amendments for contracts for renewable electricity have been drafted within Chapter 6 of IFRS 9 *Financial Instruments*, including those that relate to the application of paragraph 2.4 of IFRS 9. In drafting any final amendments to IFRS 9, the IASB will consider further the location of those amendments.

6.10.2 Paragraphs 6.10.3–6.10.6 apply to only such contracts for renewable electricity that have the characteristics in paragraph 6.10.1 and provide exceptions to only the requirements in IFRS 9 specified in paragraphs 6.10.3–6.10.6. An entity shall apply all other applicable requirements in IFRS 9 to such contracts for renewable electricity. For clarity, an entity shall not apply paragraphs 6.10.3–6.10.6 by analogy to other contracts, items or transactions.

6.10.3 For the purpose of applying the requirements in paragraph 2.4 to contracts to buy and take delivery of renewable electricity that have the characteristics in paragraph 6.10.1, an entity shall consider at inception of the contract and at each subsequent reporting date:

- (a) the purpose, design and structure of the contract including the volumes of electricity expected to be delivered over the remaining duration of the contract. In assessing how the volumes expected to be delivered under the contract continue to be in accordance with the entity's expected purchase or usage requirements, the entity is not required to make a detailed estimate for periods that are far in the future—for such periods an entity may extrapolate projections from reasonable and supportable information available at the reporting date. However, an entity shall consider reasonable and supportable information available at the reporting date about expected changes in the entity's purchase or usage requirements for a period not shorter than 12 months after the reporting date (or the entity's normal operating cycle as described in paragraph B95 of IFRS 18).
- (b) the reasons for past and expected sales of unused renewable electricity within a short period after delivery and whether such sales are in accordance with the entity's expected purchase or usage requirements. A sale of unused renewable electricity is in accordance with the entity's expected purchase or usage requirements only if all the following criteria are met:
 - (i) the sale arises from the entity's exposure to the volume risk, giving rise to mismatches between the renewable electricity delivered and the entity's electricity demand at the time of delivery.
 - (ii) the design and operation of the market in which the electricity is sold results in the entity not having the practical ability to determine the timing or price of the sale.
 - (iii) the entity expects to purchase at least an equivalent volume of electricity within a reasonable time (for example, one month) after the sale.

6.10.4 For the purpose of applying the requirements in Section 6.3 to a cash flow hedging relationship in which a contract for renewable electricity that has the characteristics in paragraph 6.10.1 is designated as the hedging instrument, an entity is permitted to designate a variable nominal volume of forecast electricity transactions (either sales or purchases) as the hedged item, if, and only if:

- (a) the hedged item is specified as the variable volume of electricity to which the hedging instrument relates; and
 - (b) the variable volume of forecast electricity transactions designated in accordance with (a) do not exceed the volume of future electricity transactions that are highly probable, except if paragraph 6.10.5 applies.
- 6.10.5 If an entity designates renewable electricity sales in accordance with paragraph 6.10.4(a), such forecasted sales are not required to be highly probable if the hedging instrument relates to a proportion of the total future renewable electricity sales from the production facility as referenced in the contract for renewable electricity.
- 6.10.6 To account for a qualifying cash flow hedging relationship as required by paragraph 6.5.11, an entity shall measure the hedged item using the same volume assumptions as those used for measuring the hedging instrument. However, all other assumptions and inputs used for measuring the hedged item, including pricing assumptions, shall reflect the nature and characteristics of the hedged item and shall not impute the features of the hedging instrument (see paragraph B6.5.5).

Chapter 7 Effective date and transition

7.1 Effective date

- ...
- 7.1.12 *Contracts for Renewable Electricity*, issued in [Month, Year], added paragraphs 6.10.1–6.10.6 and 7.2.50–7.2.52. An entity shall apply those amendments for annual periods beginning on or after [date to be determined]. Earlier application is permitted from the date these amendments are issued. If an entity applies those amendments for an earlier period, it shall disclose that fact.

7.2 Transition

- ...
- Transition for *Contracts for Renewable Electricity***
- 7.2.50 An entity shall apply paragraph 6.10.3 retrospectively in accordance with IAS 8. An entity is not required to restate prior periods to reflect the application of these amendments. The entity is permitted to restate prior periods if, and only if, it is possible to do so without the use of hindsight. If an entity does not restate prior periods, it shall recognise any difference between the previous carrying amount and the carrying amount at the beginning of the reporting period in which the entity first applies the amendments in the opening retained earnings (or other component of equity, as appropriate) at the beginning of that reporting period.

- 7.2.51 However, if an entity applies paragraph 6.10.3 in a reporting period that includes the date the amendments are issued, the entity shall recognise any difference between the previous carrying amount and the carrying amount **at the date when the amendments are issued** in the opening retained earnings (or other component of equity, as appropriate) at the beginning of that reporting period.
- 7.2.52 An entity shall apply paragraphs 6.10.4–6.10.6 prospectively to new hedging relationships designated on or after the date the amendments are first applied (see paragraph 7.1.12). An entity is permitted to change the designation of the hedged item in a cash flow hedging relationship that was designated before the date the amendments are first applied. For the avoidance of doubt, such a change to the designation of the hedged item constitutes neither the discontinuation of the hedging relationship nor the designation of a new hedging relationship.

[Draft] Amendments to IFRS 7 *Financial Instruments: Disclosures*

Paragraphs 42T–42W, 44LL–44MM and the heading above paragraph 42T are added. For ease of reading new text is not underlined. The heading above paragraph 44LL is not added but is included for ease of reference. The reference to the forthcoming IFRS 19 *Subsidiaries without Public Accountability: Disclosures* in paragraph 44MM is based on the Exposure Draft *Subsidiaries without Public Accountability: Disclosures*.

Contracts for renewable electricity

- 42T An entity that is a party to contracts for renewable electricity (that have the characteristics in paragraph 6.10.1 of IFRS 9) shall disclose information that enables users of financial statements to understand how these contracts affect the amount, timing and uncertainty of the entity’s future cash flows. Specifically, an entity shall disclose:
- (a) the terms and conditions of the contracts. Examples of terms and conditions include the remaining contract duration, the type of pricing (including the reference market and whether the contracts include price adjustment clauses), minimum or maximum volume, cancellation clauses and whether the contracts include renewable energy certificates (or similar attributes).
 - (b) for contracts for renewable electricity that are not measured at fair value through profit or loss, either:
 - (i) the fair value of the contracts at the reporting date, accompanied by the information required by paragraphs 93(g)–(h) of IFRS 13; or
 - (ii) the volume of renewable electricity a seller under the contracts expects to sell or a purchaser under the contracts expects to purchase over the remaining duration of the contracts. An entity is permitted to provide this information as a range for each of these periods: not later than one year; later than one year and not later than five years; and later than five years. An entity shall also disclose the methods and assumptions the entity used in preparing the information, any changes in those methods and assumptions since the previous reporting period, and the reasons for such changes.
- 42U If an entity is a seller under contracts for renewable electricity (that have the characteristics in paragraph 6.10.1 of IFRS 9), the entity shall disclose information that enables users of financial statements to understand how these contracts affect the entity’s financial performance for the reporting period. Specifically, an entity shall disclose the proportion of renewable electricity covered by the contracts to the total electricity sold for the reporting period.

- 42V If an entity is a purchaser under contracts for renewable electricity (that have the characteristics in paragraph 6.10.1 of IFRS 9), the entity shall disclose information that enables users of financial statements to understand how these contracts affect the entity's financial performance for the reporting period. Specifically, an entity shall disclose for the reporting period:
- (a) the proportion of renewable electricity covered by the contracts to the total net volume of electricity purchased;
 - (b) the total net volume of electricity purchased—irrespective of the source of production;
 - (c) the average market price per unit of electricity in the markets in which the entity purchased electricity; and
 - (d) if (b) multiplied by (c) differs substantially from the actual total cost incurred by the entity to purchase the volume of electricity in (b), a qualitative explanation of the key reasons for this difference.
- 42W As required by paragraph B3, an entity shall consider how much detail to disclose, how much emphasis to place on different aspects of the disclosure requirements, the appropriate level of aggregation or disaggregation, and whether users of financial statements need additional explanations to evaluate the quantitative information the entity has disclosed. For example, an entity need not disclose information for each contract separately. An entity also need not duplicate information that is already disclosed in accordance with other IFRS Accounting Standards.

Effective date and transition

- ...
- 44LL *Contracts for Renewable Electricity*, issued in [Month, Year], which also amended IFRS 9, added paragraphs 42T–42W and 44MM. An entity shall apply these paragraphs when it applies the amendments to IFRS 9. If an entity does not restate comparative information when it first applies the amendments to IFRS 9, the entity also shall not present comparative information for the disclosures required by paragraphs 42T–42W.
- 44MM In the reporting period in which an entity first applies *Contracts for Renewable Electricity*, an entity is not required to disclose the quantitative information that would otherwise be required by paragraph 28(f) of IAS 8. Similarly, an entity that applies IFRS 19 *Subsidiaries without Public Accountability: Disclosures* is not required to disclose the quantitative information that would otherwise be required by paragraph 134(f) of IFRS 19.

Appendix—[Draft] Amendments to other IFRS Accounting Standards

IFRS 19 *Subsidiaries without Public Accountability: Disclosures*

The amendments proposed in this section are based on the Exposure Draft *Subsidiaries without Public Accountability: Disclosures* and amended for decisions made by the IASB in its project Disclosure Initiative—Subsidiaries without Public Accountability: Disclosures. Paragraphs 67A–67C, B2 and the subheading above paragraph 67A are added. For ease of reading new text is not underlined. The headings above paragraphs 67A and B2 are not added but are included for ease of reference.

Disclosure requirements

...

IFRS 7 *Financial Instruments: Disclosures*

...

Contracts for renewable electricity

- 67A An entity that is a party to contracts for renewable electricity (that have the characteristics in paragraph 6.10.1 of IFRS 9) shall disclose information about how these contracts affect the amount, timing and uncertainty of the entity's future cash flows. Specifically, an entity shall disclose:
- (a) the terms and conditions of the contracts. Examples of terms and conditions include the remaining contract duration, the type of pricing (including the reference market and whether the contracts include price adjustment clauses), minimum or maximum volume, cancellation clauses and whether the contracts include renewable energy certificates (or similar attributes).
 - (b) for contracts for renewable electricity that are not measured at fair value through profit or loss, either:
 - (i) the fair value of the contracts at the reporting date, accompanied by the information required by paragraph 79(c) of IFRS 19; or
 - (ii) the volume of renewable electricity a seller under the contracts expects to sell or a purchaser under the contracts expects to purchase over the remaining duration of the contracts. An entity is permitted to provide this information as a range for each of these periods: not later than one year; later than one year and not later than five years; and later than five years. An entity shall also disclose the methods and assumptions the entity used in preparing the information, any changes in those methods and assumptions since the previous reporting period, and the reasons for such changes.

- 67B If an entity is a seller under contracts for renewable electricity (that have the characteristics in paragraph 6.10.1 of IFRS 9), the entity shall disclose information about how these contracts affect the entity's financial performance for the reporting period. Specifically, an entity shall disclose the proportion of renewable electricity covered by the contracts to the total of electricity sold for the reporting period.
- 67C If an entity is a purchaser under contracts for renewable electricity (that have the characteristics in paragraph 6.10.1 of IFRS 9), the entity shall disclose information about how these contracts affect the entity's financial performance for the reporting period. Specifically, an entity shall disclose for the reporting period:
- (a) the proportion of renewable electricity covered by the contracts to the total net volume of electricity purchased;
 - (b) the total net volume of electricity purchased—irrespective of the source of production;
 - (c) the average market price per unit of electricity in the markets in which the entity purchased electricity; and
 - (d) if (b) multiplied by (c) differs substantially from the actual total cost incurred by the entity to purchase the volume of electricity in (b), a qualitative explanation of the key reasons for this difference.

...

Appendix B—Effective date and transition

...

- B2 *Contracts for Renewable Electricity*, issued in [Month, Year], which amended IFRS 9, added paragraphs 67A–67C. An entity shall apply these amendments when it applies the amendments to IFRS 9. If an entity does not restate comparative information when it first applies the amendments to IFRS 9, the entity also shall not present comparative information for the disclosures required by paragraphs 67A–67C.

Approval by the IASB of the Exposure Draft *Contracts for Renewable Electricity* published in May 2024

The Exposure Draft *Contracts for Renewable Electricity* was approved for publication by 12 of the 14 members of the International Accounting Standards Board (IASB). Messrs Mackenzie and Uhl voted against its publication. Their alternative views are set out after the Basis for Conclusions.

Andreas Barckow	Chair
Linda Mezon-Hutter	Vice-Chair
Nick Anderson	
Patrina Buchanan	
Tadeu Cendon	
Florian Esterer	
Zach Gast	
Hagit Keren	
Jianqiao Lu	
Bruce Mackenzie	
Bertrand Perrin	
Rika Suzuki	
Ann Tarca	
Robert Uhl	

Basis for Conclusions on the Exposure Draft *Contracts for Renewable Electricity*

This Basis for Conclusions accompanies, but is not part of, the Exposure Draft Contracts for Renewable Electricity. It summarises the considerations of the International Accounting Standards Board (IASB) when developing the Exposure Draft. Individual IASB members gave greater weight to some factors than to others.

Background

- BC1 The IFRS Interpretations Committee (Committee) received a request about how an entity would apply paragraph 2.4 of IFRS 9 *Financial Instruments* to contracts to buy and take delivery of electricity produced from nature-dependent sources. The request said entities experience application challenges when applying the requirements in IFRS 9 to these contracts—commonly referred to as ‘physical power purchase agreements’ (physical PPAs).
- BC2 The Committee referred the matter to the International Accounting Standards Board (IASB) for its consideration. Stakeholders told the IASB during its research that applying the requirements in IFRS 9 to PPAs sometimes provided less useful information to users of financial statements (investors). Additionally, stakeholders said a timely solution was needed because of an expected increase in the use of PPAs due to the increase in the demand for renewable electricity.
- BC3 Stakeholders also said that if the IASB was to consider narrow-scope standard-setting for physical PPAs, it should also consider how an entity accounts for what is commonly referred to as ‘virtual PPAs’—PPAs that require net settlement of the difference between the prevailing market price and the contractually agreed price for the volume of electricity produced from a referenced production facility. The objective of both physical PPAs and virtual PPAs is to ensure long-term access to renewable electricity and to fix the price per unit of electricity purchased or sold. Consequently, the economic outcomes of the two types of contracts are the same. In many cases, the design and operation of the electricity market determines the types of contracts entities can enter into.
- BC4 The IASB decided to add a narrow-scope standard-setting project to its work plan to propose amendments to IFRS 9 for contracts to buy or sell renewable electricity that have specified characteristics. These amendments aim to ensure financial statements faithfully represent the effects of these contracts.
- BC5 The IASB also concluded that it was necessary to amend IFRS 7 *Financial Instruments: Disclosures* by adding disclosure requirements for contracts for renewable electricity within the scope of the amendments, enabling investors to understand the effect of these contracts on an entity’s financial statements.

Scope of the proposed amendments (proposed paragraphs 6.10.1–6.10.2 of IFRS 9)

- BC6 Practice in accounting for contracts to buy or sell non-financial items has developed over many years and, other than for PPAs, has not raised concerns among investors or other stakeholders. Therefore, in developing a timely solution for PPAs, the IASB noted the importance of minimising the risk of unintended consequences any proposed amendments could have on how an entity accounts for other contracts to buy or sell non-financial items.
- BC7 Through its research, the IASB concluded that most of the concerns described in paragraph BC2 about the accounting for contracts for renewable electricity arise due to the combination of:
- (a) the nature-dependency of the source of renewable electricity production.
 - (b) the design and operation of the market in which the electricity is purchased or sold.
 - (c) the ‘pay-as-produced’ features of long-term PPAs. ‘Pay-as-produced’ features oblige the purchaser to buy electricity produced from a referenced production facility when the electricity is produced. These features expose the purchaser to substantially all of the risk that the volume of electricity produced does not align with the purchaser’s demand for electricity at the time of production.
- BC8 The IASB concluded that it could define the contracts within the scope of the proposed amendments by using the characteristics described in proposed paragraph 6.10.1 because they adequately describe the nature of the contracts that the IASB intended to include within that scope.
- BC9 The IASB also considered whether to include in the proposed amendments other contracts for electricity. In developing the proposals, the IASB did not receive feedback that other contracts result in the same concerns as contracts that have the characteristics described in proposed paragraph 6.10.1. For example, the IASB did not include contracts for biomass energy and some contracts for hydroelectricity in the scope of the proposed requirements because those contracts might only have one of the characteristics described in proposed paragraph 6.10.1.
- BC10 Consequently, the IASB included in proposed paragraph 6.10.2 that an entity shall not apply the proposed amendments by analogy to other contracts, items or transactions.
- BC11 Contracts for renewable electricity are typically accompanied by renewable energy certificates (RECs) (or certificates, schemes or accreditations with similar attributes). RECs are market-based instruments certifying that the bearer owns electricity produced from a renewable production facility. Therefore, RECs are an important consideration for entities entering into contracts for renewable electricity. The IASB concluded that it can effectively respond to stakeholders’ concerns about contracts for renewable electricity separately from the accounting questions about RECs and how this interacts

with accounting for these contracts. Instead, the IASB concluded a response to accounting questions about RECs might be best placed in a potential project on pollutant pricing mechanisms. If the IASB included RECs within this project about contracts for renewable electricity, that inclusion would unnecessarily delay the project because the IASB would have to consider a broader range of arrangements. Therefore, this Exposure Draft does not propose how to account for RECs.

- BC12 The IASB also decided to limit the scope of the proposed amendments to contracts to which the requirements in IFRS 9 apply. Stakeholders did not identify concerns for contracts for renewable electricity that entities account for applying other IFRS Accounting Standards, for example IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IFRS 16 *Leases*, IAS 28 *Investments in Associates and Joint Ventures* and IFRIC 12 *Service Concession Arrangements*.

Own-use requirements (proposed paragraph 6.10.3 of IFRS 9)

- BC13 To address the concerns raised about contracts to buy and take delivery of renewable electricity, the IASB decided to develop new requirements explaining how an entity applies the own-use requirements in IFRS 9 to those contracts. The IASB noted that in May 2005 the Committee issued an agenda decision *Meaning of Delivery (IAS 39)*. In the agenda decision the Committee concluded that an allocation to a customer's account could be regarded as delivery. The IASB considered that the fact pattern in the agenda decision is similar to the delivery of electricity under contracts for renewable electricity because the electricity delivered is allocated to a customer's account. The proposals do not include requirements about the meaning of delivery.
- BC14 Investors informed the IASB that if an entity uses the electricity in its operations, the recognition of the fair value changes in profit or loss for these, typically long-term, contracts does not provide useful information about the performance of the entity. Instead, an entity should account for these contracts in the same way as other procurement contracts. Information about the fair value in the notes would be useful to understand the risks to which the entity is exposed. The IASB concluded that accounting for these contracts at fair value in all circumstances would not provide investors with useful information.
- BC15 Some stakeholders questioned the IASB's conclusion in paragraph BC14 because, for some contracts within the scope of the proposed amendments, management knows—when entering into the contract—that there might be times when it would have to sell electricity delivered to it shortly after delivery. In the view of those stakeholders, measuring the contract at fair value through profit or loss would best represent the risks arising under the contract. Others asked whether amendments to the own-use requirements are necessary. If a contract to buy renewable electricity does not meet the current own-use requirements, an entity would be required to account for that contract as a derivative. These stakeholders suggested the IASB should focus only on ensuring that an entity is able to apply hedge accounting to these

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contracts. An entity would then be able to apply hedge accounting to account for various types of PPAs in the same way, reflecting that these contracts have the same economic outcome for an entity (as described in paragraph BC3).

- BC16 The IASB observed that entities that apply the own-use requirements might already account for other contracts for non-financial items that have the same economic outcome as either a normal purchase or a derivative. (A ‘normal purchase’ has the same meaning here as in paragraphs BCZ2.18 and BCZ2.23 of the Basis for Conclusions on IFRS 9 *Financial Instruments*.) Paragraph AG20 of IAS 32 *Financial Instruments: Presentation* sets out the framework to distinguish between contracts to buy non-financial items that are normal purchases and those that are derivatives. The underlying principle of this distinction is management’s intention (evidenced by facts and circumstances) in entering into a contract. The IASB decided to develop the amendments in a way that maintains this underlying principle.
- BC17 Contracts for renewable electricity are also subject to a market design and operation that, in combination with the characteristics in proposed paragraph 6.10.1, either force the purchaser to sell unused electricity back into the market shortly after delivery or, if a purchaser fails to do so, the market operation will ‘repossess’ the electricity and then require the entity to pay a, sometimes punitive, penalty.
- BC18 The mismatches between the electricity delivered and the entity’s electricity demand at the time of delivery arise from the characteristics of these contracts described in proposed paragraph 6.10.1 and the design or operation of the electricity market. Even though sales occur because of these mismatches, management’s intention in entering into a contract might be to receive electricity in accordance with the entity’s expected purchase or usage requirements. The entities do not buy and sell the electricity for the purpose of generating a profit from short-term fluctuations in price or dealer’s margin.
- BC19 The IASB agrees that an entity—applying the own-use requirements—should not be prohibited from accounting for contracts to buy renewable electricity as normal purchases solely because of sales that arise from the characteristics in proposed paragraph 6.10.1 and the design or operation of the electricity market. The IASB decided that an entity considers the reasons for the sales shortly after delivery to determine whether the contract was entered into and continues to be held in accordance with the entity’s expected usage requirements.
- BC20 However, to ensure the new requirements maintain the underlying principle behind the own-use requirements, to reduce the risk of entities structuring transactions or contracts and to include adequate rigour within the proposals, the IASB decided that an entity would also consider:
- (a) *the purpose, design and structure of the contract*—contracts to buy renewable electricity that are within the scope of the proposed amendments are typically designed and structured to give an entity access to a proportion of the total volume of electricity produced by a referenced production facility. If an entity enters into a contract that is expected to continuously deliver more electricity than the entity

needs, such an ‘oversized’ contract would not be in accordance with the entity’s expected usage requirements.

- (b) *reasonable and supportable information about changes in expected volumes to be used*—many contracts to buy renewable electricity are long-term and therefore subject to high levels of estimation uncertainty. An entity is required to assess the volume of electricity expected to be used over the duration of the contract. This assessment does not require a detailed estimate for periods that are far in the future—for such periods an entity may extrapolate projections from reasonable and supportable information available at the reporting date. However, an entity shall not ignore reasonable and supportable information at the reporting date about changes in the entity’s purchases or usage requirements over a period not shorter than 12 months after the reporting date (or the entity’s normal operating cycle as described in paragraph B95 of IFRS 18 *Presentation and Disclosure in Financial Statements*). This assessment aims to ensure that contracts are timely reclassified as derivatives when the expected volumes to be delivered are no longer in accordance with the entity’s expected purchase or usage requirements.
- (c) *whether it remains a net-purchaser over a reasonable amount of time*—due to the combination of the characteristics and the market design and operation, an entity might have frequent and substantial sales for the duration of the contract. The IASB proposed to require that an entity purchase an equivalent volume of electricity that was sold shortly after delivery in the market within a reasonable time after the sale. ‘Reasonable’ depends on an entity’s operations. The IASB added to proposed paragraph 10.6.3(b)(iii) an example of one month to demonstrate that a reasonable time is typically a short time.

Hedge accounting requirements (proposed paragraphs 6.10.4–6.10.6 of IFRS 9)

Application challenges related to contracts for renewable electricity

- BC21 **Entities are increasingly using contracts for renewable electricity to fix the price at which renewable electricity will be sold or purchased.** For those contracts that are not accounted for as normal sales or purchases (as required by paragraph 2.4 and proposed paragraph 6.10.3 of IFRS 9), entities apply hedge accounting to represent, in the financial statements, the effect of their risk management activities.
- BC22 When applying the hedge accounting requirements in IFRS 9, application challenges arise in designating and measuring the hedged item if a contract for renewable electricity with a variable nominal amount (that is, a PPA) is designated as the hedging instrument.

Designating the hedged item

- BC23 IFRS 9 generally requires the hedged item to be designated as a specified nominal amount or volume, or a component of such a nominal amount or volume. For example, an entity may designate the first 100 MWh of electricity sales in June 202X or the bottom layer, measuring 5 million cubic metres of natural gas stored in location XYZ. Any changes to the hedged item, such as a change in the nominal amount or volume to be designated, would result in the discontinuation of the hedging relationship because such changes indicate a change in the entity's documented risk management objective.
- BC24 In most cash flow hedging relationships, the only cash flow variability that arises is resulting from the changes in the hedged risk, for example the market price of a non-financial item. However, when using a contract for renewable electricity as the hedging instrument, cash flow variability also arises because the nominal amount or volume of that instrument is variable. **This volume variability arises because the source for the production of renewable electricity is nature-dependent as described in proposed paragraph 6.10.1 of IFRS 9.**
- BC25 From a risk management perspective, entities want to hedge the cash flow variability arising from the changes in the market price of electricity and are less concerned with the volume uncertainty because the volume uncertainty is largely hedged through the variable nominal in the hedging instrument. In other words, to the extent that the renewable electricity produced under the contract is equal to or less than an entity's actual sales or purchases of renewable electricity, the entity's objective of reducing variability arising from price risk will be achieved.
- BC26 When applying the current hedge accounting requirements, an entity must, however, designate a specified volume of forecast electricity transactions that will occur with enough certainty and consistency throughout the duration of the hedging relationship. This means an entity must define an absolute volume of electricity at inception of the hedging relationship which cannot be changed throughout its duration.
- BC27 Designating from a seller's perspective a consistent volume of renewable electricity as the hedged item might often result in hedge accounting being applied to only a small portion of an entity's forecast renewable electricity sales because the actual volume produced would be expected to be highly variable as a result of the nature-based conditions. For example, although a production facility might have a maximum capacity of 1,000 MWh, the volumes expected to be produced (applying probability-weighted scenario analysis) ranges between 300 MWh and 600 MWh. Nevertheless, the volume of forecast sales that will occur with enough certainty and consistency to meet the requirement for the transaction to be highly probable (as required by paragraph 6.3.3 of IFRS 9) throughout the duration of the renewable electricity contract is only 100 MWh. In this scenario, the entity would be able to designate only 100 MWh as the hedged item for the duration of the hedging relationship, despite the contract for renewable electricity providing a highly effective economic hedge for any volume of electricity the entity produces and

sells. Although the entity might be able to designate a qualifying hedging relationship, the fact that the hedged item has a fixed nominal volume compared to a variable nominal volume in the hedging instrument inevitably results in hedge ineffectiveness. The IASB acknowledged that such a designation will not appropriately consider the contractual link between the hedged item (being the electricity produced and sold) and the hedging instrument (being the contract for renewable electricity), which economically results in all the electricity produced to be fully hedged.

BC28 The IASB also acknowledged that the challenges in hedging forecast electricity purchases are, to a large extent, similar to those described in paragraph BC27 for a seller of electricity. However, an additional challenge relates to the lack of a contractual link between the volume of forecast electricity purchases and the volume of electricity produced under the contract for renewable electricity. Therefore, when looking at the hedged item in isolation, the same volume uncertainty might not exist as that for forecast sales, because electricity demand of an entity and therefore its purchases can generally be reliably estimated.

BC29 While for purchases of electricity the hedged item has no contractual link to the hedging instrument with regards to the volume of electricity produced, the hedged item and the hedging instrument have nevertheless a strong relationship because the contract for renewable electricity will provide an effective economic hedge to the extent that the volume of electricity produced does not exceed the actual spot purchases of electricity. Therefore, the challenge is to specify the volume of the hedged item (which is used to construct the hypothetical derivative (see paragraph B6.5.5 of IFRS 9)) in such a way that it is consistent with the expected (variable) volume of the hedging instrument, for example the contract for renewable electricity.

Measuring the hedged item

BC30 Paragraph 6.5.11 of IFRS 9 requires an entity accounting for a qualifying cash flow hedging relationship to calculate the cumulative change in fair value (present value) of the hedged item from inception of the hedging relationship. Therefore, determining the changes in fair value of the hedged item is based on how the hedged item has been designated, for example whether the hedged item is an entire item, a component of an item or a combination of components of an item. To calculate the change in the value of the hedged item, for the purpose of measuring hedge ineffectiveness, an entity may use a derivative that would have terms that match the critical terms of the hedged item (this is commonly referred to as a 'hypothetical derivative'). Paragraph B6.5.5 of IFRS 9 states that, if an entity is using a hypothetical derivative to calculate the change in the value of the hedged item, the hypothetical derivative cannot include features in the value of the hedged item that exist only in the hedging instrument.

BC31 Taking the example described in paragraph BC27, measurement of the hedged item would be based on the fixed volume of 100 MWh. The IASB concluded that, if the volume delivered under the contract for renewable electricity were instead 600 MWh, hedge ineffectiveness would arise despite the entity's sales

volume of 600 MWh being fully aligned to the volume the contract of electricity net settles on. This is because the entity would be required to measure the hedging instrument based on 600 MWh, which would be variable period-on-period, and compare this with a measurement of the hedged item, which would be based on a fixed volume of 100 MWh. The IASB was of the view that recognising hedge ineffectiveness in such situations would not faithfully reflect the economic effects resulting from using a contract for renewable electricity as the hedging instrument.

Proposed amendments to hedge accounting

Designating the hedged item

- BC32 The objective of hedge accounting as described in paragraph 6.1.1 of IFRS 9 is to represent, in the financial statements, the effect of an entity's risk management activities that use financial instruments to manage exposures arising from risks that could affect profit or loss.
- BC33 The IASB considered that the challenges described in paragraphs BC21–BC31, could be resolved by permitting an entity to designate the hedged item as the variable volume of renewable electricity to which the hedging instrument relates.
- BC34 The IASB was of the view that **permitting such designation of the hedged item will enable the entity to more faithfully describe the forecast transactions it intends to hedge** using the contract for renewable electricity. The IASB also considered that such a designation would prevent cash flow variability **attributable to volume risk** from affecting the hedging relationship while at the same time requiring an entity to recognise the effects of variability attributable to changes in the market price. In the IASB's view, this approach would be consistent with entities' risk management strategy when entering into contracts for renewable electricity as described in paragraph BC25 and therefore would enable an entity to more faithfully represent the economic effects of the hedging relationship in the financial statements.
- BC35 The IASB confirmed that, consistent with the current hedge accounting requirements in IFRS 9, for forecast electricity transactions to be eligible for designation as the hedged item, the forecast transactions must be highly probable. However, the IASB proposed an exception for designated forecast renewable electricity sales that are a proportion of the total future sales from the referenced production facility (as specified in the contract for renewable electricity). The IASB considered that when an entity would proportionately hedge all renewable electricity sales, it would be sufficiently clear to the entity that when any renewable electricity sales from the referenced production facility occur, those sales would be the hedged item.

Measuring the hedged item

- BC36 The IASB noted that the measurement of the hedged item must be based on the item's designation. Therefore, if the hedged item is designated as the variable volume of renewable electricity of the hedging instrument, the measurement of the hedged item must be based on that variable volume. The

IASB therefore proposed that an entity uses the same volume assumptions when measuring the hedged item as those used to measure the hedging instrument. By aligning the volume assumptions between the hedged item and the hedging instrument as far as possible, the hedging relationship would not be affected by hedge ineffectiveness caused by a comparison of a fixed nominal volume with a variable nominal volume—that is, volume uncertainty.

BC37 The IASB acknowledged that hedge ineffectiveness caused by volume uncertainty should not arise because economically the volumes of sales and the volume of electricity covered by the contract for renewable electricity are fully aligned (see paragraph BC31). However, the IASB noted that there could be other sources of potential hedge ineffectiveness for forecast electricity transactions, particularly in the case of purchases of electricity. The IASB considered that there could be an economic effect, for example, if there is a difference between:

- (a) the timing of purchases and electricity production resulting in differences in the spot prices.
- (b) the volume of electricity covered by the contract for renewable electricity and the volume of spot purchases. If the volume covered by the contract exceeds the purchased volume, the change in fair value of the hedging instrument would not offset the change in value of the hedged item.
- (c) the basis component of the spot price. In other words, there is basis risk between the spot price in the market where forecast purchases are made (the hedged risk) and the market in which the contract for renewable electricity is settled. Such a scenario would occur, for example, if an entity that purchases electricity in one jurisdiction enters into a contract for renewable electricity with an entity that is based in another jurisdiction.

BC38 IFRS 9 does not require a hedging relationship to be fully effective. As explained in paragraph BC6.241 of the Basis for Conclusions on IFRS 9, many types of hedging relationships inevitably involve some hedge ineffectiveness that cannot be eliminated because of differences in the underlyings or other differences between the hedging instrument and the hedged item that the entity accepts in order to achieve a cost-effective hedging relationship.

BC39 However, the IASB noted that an entity, applying paragraph 6.5.11 of IFRS 9, would include pricing differences or any other differences between the hedged item and the hedging instrument that represent actual economic effects when determining hedge ineffectiveness.

Disclosure requirements

Entities applying IFRS Accounting Standards (proposed paragraphs 42T–42W of IFRS 7)

- BC40 The IASB’s research found that stakeholders want greater transparency about contracts for renewable electricity that would be within the scope of the amendments to IFRS 9 and that would be accounted for as a normal purchase. Contracts accounted for as a normal purchase would not be subject to the disclosure requirements of IFRS 7.
- BC41 As mentioned in paragraph BC3, stakeholders told the IASB that the various types of contracts for renewable electricity result in the same economic outcome and expose the entity to similar risks. The IASB agreed with these stakeholders. The IASB concluded that additional disclosures would be relevant for all contracts for renewable electricity that have the characteristics in proposed paragraph 6.10.1 of IFRS 9.
- BC42 The IASB acknowledges that other IFRS Accounting Standards (for example, IFRS 15 *Revenue from Contracts with Customers*) include disclosure requirements that might apply to contracts for renewable electricity. However, the proposed amendments would not require an entity to duplicate information that it already provides. The IASB is also of the view that the information an entity would disclose in accordance with these proposed disclosure requirements could be compatible to sustainability-related information entities already disclose about these contracts.

Specific disclosure objectives

- BC43 The IASB’s research included discussions with investors and a desktop review of publicly available financial statements. This research identified that investors need to understand the effect that contracts for renewable electricity have on:
- (a) *an entity’s financial performance in the reporting period*—for example, disclosure about what revenue and expenses would have been without these contracts; and
 - (b) *the amount, timing and uncertainty of the entity’s future cash flows*—for example, disclosure of an indication of the fair value of the contract at the reporting date.
- BC44 Therefore, the IASB developed the proposed specific disclosure objectives in proposed paragraphs 42T–42V of IFRS 7. The IASB:
- (a) added no overall disclosure objective for any proposed disclosure requirements because paragraphs 7 and 31 of IFRS 7 already include such objectives.
 - (b) affirmed in proposed paragraph 42W that the proposed disclosures are subject to the aggregation and disaggregation requirements in paragraph B3 of IFRS 7. For clarity, it is not the IASB’s intention that an entity would disclose information for each contract separately.

Items of information

- BC45 Investors listed items of information that entities are not currently required to disclose that would enable them to understand the effect of contracts for renewable electricity on an entity's financial statements, such as:
- (a) the type of pricing (fixed versus variable);
 - (b) the price agreed in the contract (and the prevailing market price as at the reporting date);
 - (c) the proportion of such contracts compared to the total sales or purchases of the same non-financial item;
 - (d) the effect of the contract on the revenue and expenses during the reporting period—for example, what electricity costs for the period would have been without these contracts (that is, if all purchases were made at the prevailing market price); and
 - (e) an indication of the fair value of the contract at the reporting date.
- BC46 However, many stakeholders were concerned about entities disclosing some of the items of information listed in paragraph BC45. Stakeholders were concerned that these amendments might require an entity to disclose:
- (a) commercially sensitive information, for example information about the fixed price agreed in the contract.
 - (b) 'pro-forma' or 'hypothetical' information about what income or expenses would have been without these contracts. Stakeholders said that such information might be complex to prepare and disclose.
 - (c) the fair value of the contracts. Stakeholders questioned whether the costs would outweigh the benefits because determining the fair value for these contracts is complex and subject to high levels of measurement uncertainty.
- BC47 After considering the feedback described in paragraphs BC45–BC46, the IASB proposed to require an entity to disclose the information listed in proposed paragraphs 42T(a) and 42T(b)(ii) of IFRS 7 to enable investors to understand how contracts for renewable electricity affect the amount, timing and uncertainty of an entity's future cash flows. Information about the volume of renewable electricity a seller under the contracts expects to sell or a purchaser under the contracts expects to purchase over the remaining duration of the contracts enables investors to understand the size of the future commitments of the entity—without having to calculate the fair value of the contracts.
- BC48 The IASB also proposed to require an entity to disclose the information listed in proposed paragraphs 42U–42V of IFRS 7 to enable investors to understand how these contracts affect the entity's financial performance. The proportion of electricity covered by the contracts to an entity's total electricity transactions enables investors to understand the relative size of its contracts for renewable electricity. The items of information in proposed paragraph 42V(b)–(d) enable investors to understand the effect contracts for renewable electricity had on the entity's cost for the electricity it consumed

during the reporting period. The proposals were developed so that an entity would not be required to disclose commercially sensitive information.

Costs and benefits

BC49 On balance, the IASB expects that the benefits of the proposed disclosure requirements as set out in paragraphs BC45–BC48 would outweigh the costs of applying the requirements. The IASB considered that information about the terms and conditions of the contracts and average market prices would be readily available to entities. The IASB also considered that information about actual and expected volume of electricity would be available because an entity would need this information to apply the amendments to the own-use requirements. Fair value information would also be available if an entity measures or manages other contracts for renewable electricity on a fair value basis.

Subsidiaries without public accountability (proposed paragraphs 67A–67C to IFRS 19)

BC50 As a consequential amendment, the IASB decided to require an entity applying IFRS 19 *Subsidiaries without Public Accountability: Disclosures* to disclose the same information for its contracts for renewable electricity as those entities that apply the proposed amendments to IFRS 7. The IASB decided not to reduce the disclosures for eligible subsidiaries because:

- (a) the proposed disclosure requirements would provide information about obligations, commitments or contingencies and information on measurement uncertainties. This information is consistent with the broad principles set out in paragraph BC34 of the Exposure Draft: *Subsidiaries without Public Accountability: Disclosures* the IASB is guided by in reducing disclosure requirements.
- (b) the IASB expects that the benefits of the proposed disclosure requirements would outweigh the costs for the same reasons as those set out in paragraph BC49.

Transition requirements (proposed paragraphs 7.2.50–7.2.51 of IFRS 9, proposed paragraphs 44LL–44MM of IFRS 7 and proposed paragraph B2 of IFRS 19)

Entities applying IFRS Accounting Standards

Own-use requirements

BC51 The IASB expects that the proposed amendments to the own-use requirements in IFRS 9 would affect entities that account for their contracts to buy renewable electricity as derivatives. In accordance with the proposed amendments those entities would account for these contracts as normal purchases. Therefore, the IASB proposed to require an entity to apply the proposed amendments to the own-use requirements retrospectively in accordance with IAS 8 *Basis of Preparation of Financial Statements*. However, the

IASB also proposed that an entity is not required to restate comparative information. The IASB proposed to permit an entity to restate prior periods if, and only if, doing so is possible without the use of hindsight. This approach is consistent with the transition requirements in IFRS 9 and IFRS 7.

- BC52 The IASB proposed to require an entity to recognise any difference between the previous carrying amount and the carrying amount at the date the amendments are first applied in the opening retained earnings (or other component of equity, as appropriate) at the beginning of the reporting period that includes the date on which the amendments are first applied.

Hedge accounting requirements

- BC53 Stakeholders have said the IASB should provide transition requirements for:
- (a) hedging relationships that are already designated and to which an entity could apply the proposed amendments; and
 - (b) potential hedge accounting relationships that did not meet the qualifying criteria under current IFRS 9 hedge accounting requirements but would qualify for designation if an entity applied the proposed amendments.

- BC54 The IASB noted that typically, hedge accounting can be applied only prospectively (see paragraphs 6.4.1(b) and 7.2.22 of IFRS 9). The IASB therefore concluded that prospective application would be appropriate for new hedging relationships designated on or after the date the amendments are first applied. This includes changing the designation of the hedged item in hedging relationships that are already designated at the date when the proposed amendments would be first applied as described in paragraph BC53(a).

- BC55 However, the IASB noted that retrospective designation of a hedging relationship is not possible in the circumstances described in paragraph BC53(b). Paragraph BC6.601 of the Basis for Conclusions on IFRS 9 notes that retrospective application would not allow an entity to reinstate hedging relationships that have already been discontinued at the date the amendments are applied; nor would it allow an entity to designate hedging relationships using hindsight. Therefore, retrospective application would contradict these requirements. Consequently, the IASB proposed to require an entity to apply the proposed amendments prospectively from the date the amendments are first applied.

Disclosure requirements

- BC56 The IASB proposed that an entity need not disclose the quantitative information required by paragraph 28(f) of IAS 8 (paragraph 134(f) of IFRS 19), for the current period and for each prior period presented because the costs of doing so would outweigh the benefits.

First-time adopters

BC57 IFRS 1 *First-time Adoption of International Financial Reporting Standards* includes no exceptions from retrospective application of the own-use requirements in IFRS 9. IFRS 1 does include exceptions to retrospective application for hedge accounting (see paragraphs B4–B6 of IFRS 1). The IASB has identified no reason to add to these requirements in IFRS 1. Therefore, the IASB proposed not to provide additional transition requirements for first-time adopters.

Alternative views on the Exposure Draft *Contracts for Renewable Electricity*

Alternative views of Bruce Mackenzie and Robert Uhl

- AV1 Messrs Mackenzie and Uhl disagree with the proposed expansion of the exception from the scope of IFRS 9 *Financial Instruments* to include some contracts for renewable electricity.
- AV2 Since IAS 39 *Financial Instruments: Recognition and Measurement* became effective (and then continued in IFRS 9), an entity has been required to measure at fair value derivative contracts to buy or sell non-financial items that can be settled net in cash or another financial instrument, unless the purpose of the receipt (or delivery) of the non-financial item is in accordance with the entity's expected usage (or purchase or sale) requirements. The ability to net settle the derivative contract includes situations in which the non-financial item is readily convertible to cash such that, for example, the purchaser can, after receiving the item under the contract, contemporaneously sell the item in a readily available market. In this instance, the purchaser effectively receives or pays a net cash amount as settlement of the contract.
- AV3 It has long been accepted that measurement at fair value through profit or loss provides the most relevant information for derivative contracts that can be settled net. It has also been accepted that measurement at fair value is not the most relevant measure if the purpose of a derivative contract is to purchase the non-financial items for the entity's own use (as required in paragraph 2.4 of IFRS 9), thus providing the basis for the exception. An entity must continually assess this requirement so that if the entity's intention changes—for example because their need for the non-financial items has dissipated—the entity's application of the exception also changes.
- AV4 Entities have applied these requirements to contracts for the purchase (and sale) of electricity since IAS 39 became effective. Although electricity has some different characteristics than other non-financial items—primarily that it cannot be efficiently stored, and market regulations typically require that electricity that will not be used by the entity be resold immediately in the spot market—the requirements in IAS 39 and IFRS 9 have been accepted as relevant and representationally faithful.
- AV5 In this project, the IASB has been presented with contracts for renewable electricity that have particular characteristics. The difference between these contracts and other electricity contracts is that the source of production of the specified electricity is nature-dependent, and the purchaser is required to buy electricity produced from a referenced production facility when the electricity is produced ('pay-as-produced' contracts). In addition, typically the purchaser in these derivative contracts also receives renewable energy certificates (RECs), which are valuable.

- AV6 Messrs Mackenzie and Uhl believe that a further exception from the requirements in IFRS 9 is warranted for situations in which a purchaser intends to use all of the electricity expected to be produced and supplied under the contract, but nature causes an increase in production above such expectation and the entity is forced to sell such unused excess. However, Messrs Mackenzie and Uhl disagree with the proposal in the Exposure Draft because it permits an exception from the requirements in IFRS 9 even when the purchaser knows with reasonable certainty that for some periods during the contract (e.g., certain hours or days) that it will not use, but sell, electricity delivered under the contract. In the proposal, a purchaser in a renewable electricity contract can qualify for the own-use exception even if they know, from inception of the contract, their demand in some periods will be less than expected deliveries and the entity thus expects to sell the electricity supplied under the contract during those periods. Therefore, while applying the exception, the purchaser might sell to the market, at a market price, electricity it knew it would never use, realising the fair value of that portion of the contract provided it intends to purchase, presumably from the market at a different market price, an equivalent amount of electricity.
- AV7 Messrs Mackenzie and Uhl believe the proposed accounting might provide misleading information because when an entity uses the exception from IFRS 9 for a derivative contract, a user would not expect the entity to realise in cash or another financial instrument the fair value for any portion of that contract.
- AV8 Messrs Mackenzie and Uhl are therefore of the view that the proposed further exception as proposed in the Exposure Draft not only raises questions about the accounting for other electricity contracts and contracts for other non-financial items, but appears to be more lenient towards contracts for renewable electricity than those other contracts. For the financial statements to be faithfully representational, accounting should be neutral.
- AV9 Some stakeholders have asserted that the changes in fair value recognised in an entity's statement of financial performance for the contracts for renewable electricity that have particular characteristics do not provide useful information. Similar assertions have been made in the past about other derivative contracts. Messrs Mackenzie and Uhl disagree with providing an exception from IFRS 9 for situations in which an entity knows it will net settle portions of the contract. However, if the IASB believe that the current accounting for particular contracts is not decision useful, Messrs Mackenzie and Uhl believe the way to address this should be through presentation.
- AV10 Mr Mackenzie also disagreed with the scope of the proposals for hedge accounting. In his opinion cash flow hedge accounting applying IFRS 9 works as intended and this assertion will be subjected to a post-implementation review shortly. Over the years, there have been numerous requests from stakeholders to address this aspect of cash flow hedging, but the IASB did not pursue a project. Even with the move from IAS 39 to IFRS 9, the IASB kept the requirements in IFRS 9 the same as those in IAS 39. The proposals in the Exposure Draft introduce a new variant of cash flow hedging for select types

of contracts—being contracts for renewable electricity—which, in his opinion, cannot be justified.

- AV11 Mr Mackenzie does not believe there is any principle-based reason as to why, for these types of contracts, an entity should be allowed to designate a variable nominal amount while being prevented from doing so for other contracts with similar economics. In his opinion there are no unique features of contracts for renewable electricity that justify such a drastic amendment. Mr Mackenzie believes the IASB should rather have looked at a comprehensive solution for potential amendments that would have affected all cash flow hedging relationships and not just those in the scope of the proposals.



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