

Agenda Item 10: Emissions Trading Schemes

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IPSASB Meeting

December 8-11, 2014

Toronto, Canada

Objectives of this Education Session

- Consider background and context for the Emissions Trading Schemes (ETSs) project; and
- Discuss any issues arising

Background

- December 2013—IPSASB project brief approved
 - Task Based Group: Aracelly Mendez, Fabienne Colignon, Ken Warren, Martin Koehler
- Joint project with IASB i.e. collaboration
- October 2014—IASB Emissions Trading Schemes project activated
 - IASB Staff: Jane Pike (Principal) and Natasha Dara (Assistant Technical Manager)

Overview of Session

1. ETSs and recent developments
2. Project brief revisions (timetable)
3. Collaboration with the IASB
4. Overview of financial reporting issues

1. ETSs and Recent Developments

- ETS types: “cap and trade” and “baseline and credit”
- Cap and trade:
 - Most common scheme (e.g. European Union (EU) ETS)
 - *Administrator* (government entity) allocates or sells *allowances* to the scheme *participants*
 - Allowance provides right to emit quantity of polluting gas, e.g. carbon dioxide (CO₂)
 - Allowances are capped, which caps quantity of gas allowed

1. ETSs: Cap and Trade

- Allowances can be traded (buy more, sell extra)
- Scheme participants emit during the period
- At end of period:
 - Participants must submit sufficient allowances to cover quantity of gas emitted
 - EU ETS: Costly fines for failure to submit sufficient allowances and the obligation to submit remains until discharged
- Timing issues: ETS period and reporting period not necessarily aligned

1. Emissions Trading Schemes

- An ETS aims to:
 - Provide economic incentives to reduce emissions (make emissions costly)
 - Allow flexibility so entities reduce in cost-effective ways
- A participant that reduces emissions can sell surplus allowances to other entities
- Public sector entities can be either administrators or participants
- ETS may be at national or subnational level

1. ETSs and Recent Developments

- Are ETSs still important?
 - Future for Kyoto Protocol unknown—discussions continue
 - EU emissions market—prices low, “collapse”

But:

- EU ETS continues, along with other ETS (e.g. in Canada, Japan, New Zealand, U.S.A, etc.)
- New ETSs planned, including Chinese national market planned for 2016

1. Recent Developments—IASB

2014

- ETS project reactivated; on IASB research agenda
- Indications that project will move to standards agenda after research phase

2007 to 2010

- IASB-FASB project; research into ETSs and key accounting issues
- Draft research paper (2010)—project deferred during IASB agenda consultation

2002 to 2005

- IFRIC 3, *Emission Rights*: interpretation of existing standards
- IFRIC 3 issued then withdrawn

1. Recent Developments—IPSASB and GFS

IPSASB—2014

- Conceptual Framework approved
- IPSASB policy; GFS reporting guidelines considered during IPSAS developments

GFS reporting guidelines:

- Administrator’s ETS involvement
- International statistical community agreement in 2012
- “Split asset” approach
- Approach insulates government from impact of trading

1. ETSs and Recent Developments:

Action Requested

Discuss any issues arising from recent developments

2. Project Brief Revisions (Timetable)

- ETS project brief approved, with following revisions:
 - Principles-based approach
 - Also discuss *auctioning* of allowances
 - Consider GFS Manual guidance on ETS reporting
- Agenda Paper 10.2: Revised project brief
- Timetable revised for activation in October 2014
 - Process and phase duration unchanged

2. Project Brief Revisions (Timetable)

Milestones	Completion
Information Session	December 2014
Research (Issues discussion)	March 2015
Approve CP (6 month comment period)	December 2015
Approve ED (4 month comment period)	March 2017
Review responses and develop IPSAS	
Approve IPSAS	Late 2017/ Early 2018

2. Project Brief Revisions:

Action Requested

Indicate whether agree with project timetable

3. Collaboration with the IASB

- “Joint project” during phase 1:
 - Collaboration between project staff
 - Shared information and joint staff discussions
 - Both sides gain from other’s expertise and resources
- Product from phase 1:
 - IPSASB consultation paper/ IASB discussion paper
 - Similar but distinct and different products
 - IPSASB focus includes administrators

3. Collaboration with the IASB

- Collaboration supports inter-entity comparability; consistent treatment between public and private sectors
- Insights from IASB past work (2002 to 2010)
- IASB has outreach into “participant” groups

3. Collaboration with IASB:

Action Requested

Note that ETS project is initially a joint (collaborative) project with IASB

4. Financial Reporting Issues: Administrators

- Involvement with agreements, for example:
 - Kyoto Protocol units received—are these assets?
 - Do treaties and other agreements impose liabilities?
 - Assets/liabilities: Recognition and measurement?
- As issuer of allowances:
 - Does administrator incur expense (and liability) on issuance of allowances? (Distinguish between allowances sold or free?)
 - Revenue when participants submit allowances?
 - Expense/revenue: Recognition and measurement?
 - Split asset approach? (GFS reporting)

Administrator: New Zealand Example

- When NZ Units are issued::
 - Expense (to Administrator); and
 - Liability (obligation to swap NZUs for Kyoto AAUs)
- Participant emits (and surrenders NZUs):
 - Revenue (to Administrator)
 - Liability is reduced
 - Timing; emission activity
- ETS liability is revalued
- Measurement: fair value

Administrator: Split Asset Approach (GFS Reporting Guidelines)

- Emission permit is made up of two types of asset:
 - Financial asset for the cash auction proceeds (prepayment of tax); liability for government.
 - Non-financial (intangible) asset for the changes in market value of permit after issue; value disappears on surrender
- In effect this separates government accounts from impact of trading of permits
 - Permits issued for free not recorded in government accounts (no grants, no liabilities)
 - Government revenue equal to cash received (time adjusted)

4. Financial Reporting Issues: Participants

- Receipt of allowances:
 - Assets and revenue? (Distinguish between allowances purchased versus for free?)
 - Recognition and measurement? (Initial recognition and subsequently.)
- Emissions:
 - Liability as emissions occur or when entity exceeds allowances?
- Presentation on a gross/net basis?
- Unit of account (scheme, allowances/emissions, other?)

IFRIC 3 *Emission Rights* (Withdrawn 2005)

- Apply IAS 38, *Intangibles*:
 - Allowances measured at fair value
 - Not remeasured unless active market
 - Remeasurement (if any) recognised in OCI
- Apply IAS 20, *Government Grants*:
 - Difference between fair value and amount paid recognised as government grant and amortised to income
- Apply IAS 37, *Provisions*:
 - Liability for actual emissions;
 - Remeasure liability (fair value);
 - Remeasurement recognised in income

4. Financial Reporting Issues

- Other issues to consider?
 - Impact of scheme itself (participants are worse off)
 - Fines, impairment of operational assets, financial instruments based on allowances
 - Different ETSs (“baseline and credit” compared to “cap and trade”, other ETS types?)
- More information needed, particularly financial accounting treatments by administrators:
 - EU nations, Canada, Japan, Switzerland, U.S.A.

4. Financial Reporting Issues:

Action Requested

Note:

- (a) Financial reporting issues identified; and,
- (b) More information needed, particularly on administrators' accounting treatments.

5. Next Steps

Develop issues paper for March 2015 IPSASB meeting