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## Emerging Economies Group meeting

Date	<b>May 2024</b>
Project	<b>Pollutant Pricing Mechanisms</b>
Topic	<b>Update on horizon scanning</b>
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## Purpose of this session

- Provide EEG members with an update on horizon scanning activities in relation to pollutant pricing mechanisms
- Seek feedback on the prevalence of pollutant pricing mechanisms in your jurisdiction and your views on whether the IASB should prioritise a project on this topic



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## Information for participants

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## What are pollutant pricing mechanisms?

Mechanisms, also known as 'schemes', designed to achieve a reduction of greenhouse gases (GHG) through the use of tradable emissions allowances or carbon credits



### Compliance market

- Established and regulated by governments
- Emissions trading schemes (ETS) are used as a means to limit GHG emissions
- Participation is mandatory for entities covered by the ETS



### Voluntary market

- Operates outside of the compliance market
- Enables carbon emitters to offset emissions by purchasing carbon offsets on a voluntary basis
- A project-based system is used, where carbon offsets are created through the development of projects that remove or reduce GHG emissions from the atmosphere

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## Compliance market

Two main types of compliance schemes exist:

### Cap-and-trade scheme

- Overall cap set on total volume of GHG emissions that can be released during a specified commitment period
- Overall cap is then allocated across participants by distributing or selling allowances. Over time cap is reduced
- Participants must remit allowances to cover GHG emitted

### Baseline and credit scheme

- Total emissions are not fixed, instead a baseline is established that serves as a limit on the emissions for participating entities
- Participants may emit up to the level of the baseline without incurring additional costs
- Credits are issued to entities that have reduced emissions below baseline level



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## Voluntary market

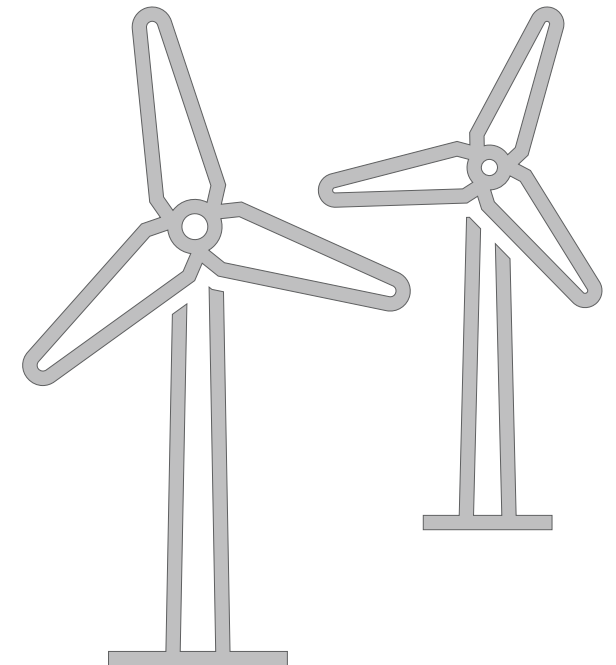
Two main types of voluntary schemes exist:

### Avoidance/ Reduction

- Carbon offsets are generated by measuring GHG emissions that were avoided or reduced as a result of implementing a project
- Examples include renewable energy projects, energy efficiency improvements, waste management initiatives

### Removal/ Sequestration

- Carbon offsets are generated by measuring the amount of GHG emissions removed by a project by means of afforestation, reforestation or carbon capture and storage technologies
- Examples include forestry projects which capture carbon, and direct air capture and storage technologies which use chemicals to trap carbon from the air



## Compliance market – diversity in accounting

Three approaches observed in practice

### ‘Emissions rights’ approach\*

- Allowances or credits are recognised as intangible assets and initially measured at fair value
- As emissions are made, a liability is recognised and measured in accordance with IAS 37
- Any difference between the amount paid for allowances or credits and their fair value is accounted for as a government grant applying IAS 20

### ‘Government grant’ approach

- Accounting is similar to the ‘Emissions rights’ approach except the liability is measured based on the carrying amount of the allowances or credits held
- If emissions are in excess of the allowances or credits held the liability for the excess is measured based on the market value of those allowances or credits

### ‘Net presentation’ approach

- Allowances or credits are recognised as intangible assets measured at cost (for granted allowances or credits this is usually a nominal amount)
- As emissions are made a liability is recognised and measured based on the carrying amount of allowances or credits held
- If the entity holds allowances or credits equal to the emissions liability the effect on net assets is nil.

\*This approach was the approach required by IFRIC 3 *Emissions Rights* which was withdrawn because of concerns about accounting mismatches

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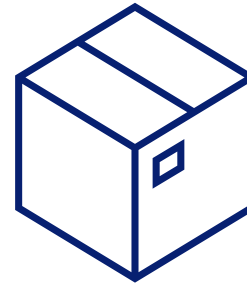
## Voluntary market – accounting considerations



### Are carbon credits assets?

Things to consider:

- Control: Can the entity direct the use of the carbon credits and obtain the economic benefits that flow from them?
- Potential to produce economic benefits: can the entity sell the credits or use them to settle an emissions liability?



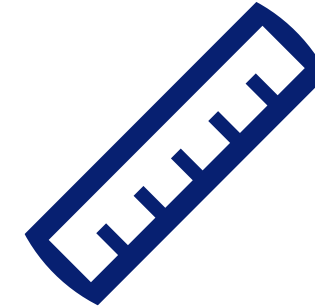
### Intangible assets or inventory?

Inventory:

- If held for sale in ordinary course of business or if considered supplies to be consumed in production process

Intangible assets:

- If it is probable that the future economic benefits will flow to the entity and costs can be measured reliably (excludes credits that meet inventory definition)



### How should they be measured?

Inventory:

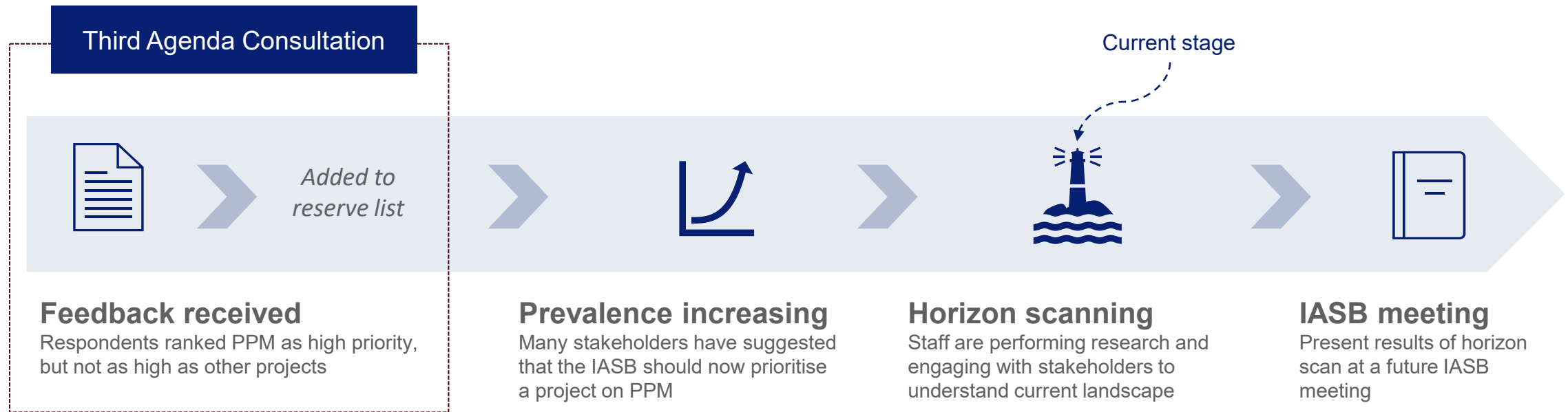
- At the lower of cost and net realizable value. If they have similar economic characteristics to commodities they may be measured at fair value through profit or loss (broker-trader)

Intangible assets:

- Using either the cost model or the revaluation model if an active market exists



## Status on IASB work plan



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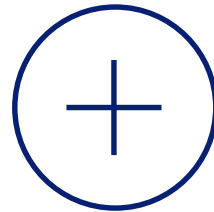
## Accounting Standards Advisory Forum

### Preliminary survey results – compliance schemes

As part of our horizon scanning, we asked ASAF members to complete a survey about pollutant pricing mechanisms in their jurisdiction



**Most** respondents stated that some form of compliance scheme exists in their jurisdiction



**Almost all** respondents noted that there are plans to introduce new schemes in the future



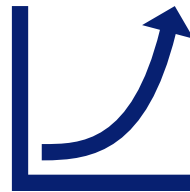
About **half** of respondents indicated that they are aware of diversity in practice or other deficiencies in the accounting for compliance schemes

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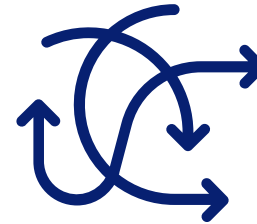
## Accounting Standards Advisory Forum Preliminary survey results – voluntary schemes



**Almost all** respondents indicated that IFRS reporting entities in their jurisdiction participate in the voluntary market



**More than half** of respondents noted that the prevalence of voluntary schemes is increasing



**More than half** of respondents indicated that these schemes give rise to accounting issues that are difficult to resolve

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## Questions for EEG members

- Do you have any comments or questions on the IASB's horizon scanning activities?
- How prevalent are pollutant pricing mechanisms in your jurisdiction?
- Do you think the IASB should prioritise a project on pollutant pricing mechanisms?



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