EY's Financial Reporting Developments Series

IFRS reporting

May 22, 2024

Building a better working world

Today's Presenters

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Today's Agenda

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01

IFRS workplan developments

- Financial instruments with characteristics of equity
- Power purchase agreements

02

A conversation with:

Cameron McInnis

Chief Accountant of the
Ontario Securities Commission

03

Recent IFRS Interpretations Committee developments

- Climate-related commitments
- Disclosure of revenues and expenses
  for reportable segments

01

IFRS workplan developments

Financial instruments with characteristics of equity

Overview

Fixed for fixed

The effects of relevant laws or regulations

Shareholder's discretion

COMPONENTS OF FICE

ED - FICE
November 2023

Obligations to purchase an entity's own equity instruments

Contingent settlement provisions

Re-classification

Disclosures

Comments on Exposure Draft

THE EFFECTS OF RELEVANT LAWS OR REGULATIONS

- To classify an instrument as equity or liability, an issuer should consider:
  - Terms explicitly stated in the contract that give rise to rights and obligations that are *in addition to*, or *more specific than*, those established by applicable law; and
  - Applicable laws that pr*event the enforceability* of a contractual right or a contractual obligation
- Contractual rights and obligations must be considered in their entirety in classifying the financial instrument or its component parts and must not be disaggregated into contractual and non-contractual parts.

Comments on Exposure Draft

THE EFFECTS OF RELEVANT LAWS OR REGULATIONS

Select summary of comments raised:

- Applying the ED may require significant judgment and will result in new application questions arising;
- Clarification of whether the laws and regulations are inclusive of regulatory guidance issued by prudential regulators;
- How would the proposals apply to principle-based regulation?
- How will stakeholders assess what is "in addition to" laws or regulations?
- Potential for unintended effects of reclassifying contractual liabilities as statutory, where the main terms are pre-defined by law and incorporated by reference into the contractual terms
- May result in changes to classification and inconsistent outcomes for similar instruments

Comments on Exposure Draft

CONTINGENT SETTLEMENT PROVISIONS | OBLIGATIONS TO PURCHASE AN ENTITY'S OWN EQUITY INSTRUMENTS

The proposed measurement approach requires entities to ignore the probability and expected timing of contingent events, when measuring contingent settlement provisions.

Select summary of comments raised:

- The proposed amendments provide new measurement requirements embedded in IAS 32
- The new measurement approach is inconsistent with the general measurement requirements of IFRS 9
- Intended scope of the new measurement requirements should be made more clear (i.e. they apply only to those liabilities or components thereof where the contingent settlement provision triggers liability classification, they do not apply to all financial liabilities that contain contingent settlement provisions)
- Written put options over non-controlling interests (NCI puts) will be affected by the proposals

Comments on Exposure Draft

Select summary of comments raised:

SHAREHOLDER'S DISCRETION

- Welcoming the introduction of additional factors to be considered when making the assessment as being helpful to entities.
- Consider providing more application guidance and/or illustrative examples to help entities apply the proposed factors in the ED.

FIXED FOR FIXED

- Requirement of passage-of-time adjustments to fix present value of the consideration on initial recognition is overly restrictive.
- Unclear how to assess what is proportional to the passage of time, further guidance/clarification is necessary
- Proposed requirements on instruments denominated in foreign currencies will change current practice in some multi-currency groups.

RECLASSIFICATIONS

- Ask for the reclassification requirements to give greater priority to representing the contractual substance of financial instruments at each reporting date.

Comments on Exposure Draft

DISCLOSURES

The proposed requirements relate to:

- The nature and priority of claims against a company on liquidation;
- The terms and conditions of financial liabilities and equity instruments; and
- The potential dilution of ordinary shares

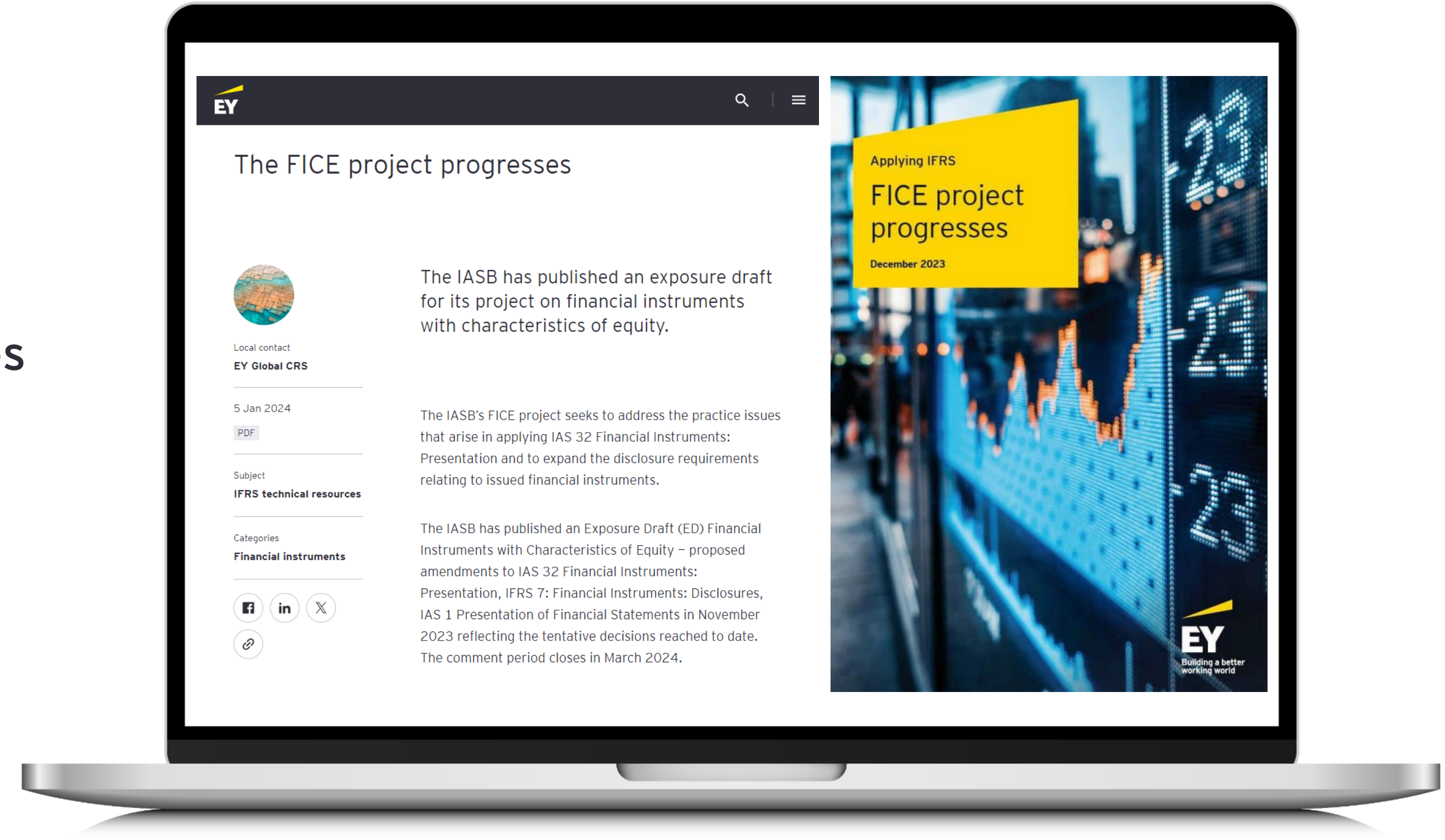
Select summary of comments raised:

- Could lead to significant additions to existing IFRS 7 disclosure requirements.
- Will the cost of compliance exceed the perceived benefits for users?
- The availability and effort required to prepare such information will be affected by the reporting regimes under which entities operate.
- Specify how the disclosures on priority on liquidation would be applied by an entity that operates in multiple jurisdictions, each with different liquidation rules.
- Clarification on how disclosures may be aggregated could be beneficial.
- There may be overlap both within these disclosure requirements and, moreover, with other reporting and disclosure requirements outside the financial statements.

Resources

Applying IFRS: FICE project progresses

View project



01

IFRS workplan developments

Power purchase agreements

Overview

What is a Power Purchase Agreement (PPA)?

- Long-term energy supply
- Usually fixed price
- Most common for renewable energy
- Physical vs virtual PPAs

Focus on **usefulness** of information for users,
as well as a **timely** solution.

IFRIC

- Original submission discussed June 2023
  - Difficulties in applying the "own use" exception to physical PPAs
  - Particular challenges with renewable energy
    - Referred to IASB

IASB

- Discussed during July 2023 – March 2024
  - Investor feedback regarding FVPTL noise
  - Added: hedge accounting for PPAs
  - Added: disclosure requirements under IFRS 7

Exposure Draft – May 2024

- The objective of the Exposure Draft is to ensure that financial statements more faithfully reflect the effects that renewable electricity contracts have on a company
- The proposals amend IFRS 9 *Financial Instruments* and IFRS 7 *Financial Instruments: Disclosures*, specifically:
  - Scope
  - Own-use requirements
  - Hedge-accounting requirements
  - Disclosure and transition requirements

*The deadline for comments on the Exposure Draft is **August 7, 2024** (shortened comment period of 90 days).*

Final amendments anticipated to be published by the **end of 2024**, available for application as soon as possible.

Exposure Draft – May 2024

Scope

Applies to contracts for renewable electricity, for which:

- The source of production is nature-dependent so that supply cannot be guaranteed at specified times/for specified volumes (e.g. wind, solar, hydro); and
- The purchaser is exposed to substantially all of the volume risk (the risk that the electricity produced does not align with demand at that time) through "pay-as-produced" features

Own-use requirements

For contracts for renewable electricity from the contract's inception and throughout its duration, the purchaser will consider:

- The purpose, design and structure of the contract, including the volumes of electricity expected to be delivered over the remaining duration of the contract and how they continue to be in accordance with the entity's expected purchase or usage requirements; and
  - Not required to make a detailed estimate for periods far in the future (reasonable & supportable extrapolation may be allowed)
- The reasons for past and expected sales of unused renewable electricity within a short period after delivery and whether such sales are consistent with the entity's expected purchase or usage requirements

Exposure Draft – May 2024

Hedge-accounting requirements

- For cash-flow hedging relationships in which an in-scope contract is designated as a hedging instrument, an entity is permitted to designate a variable nominal volume of forecast electricity transactions (either sales or purchases) as the hedged item, only if:
  - The hedged item is specified as the variable volume of electricity to which the hedging instrument relates: and
  - The variable volume designated in accordance with this does not exceed the volume of future electricity transaction that are *highly probable*, except:
    - Forecast 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
- To qualify, the hedged item is measured using the same volume assumptions used for the hedging instrument

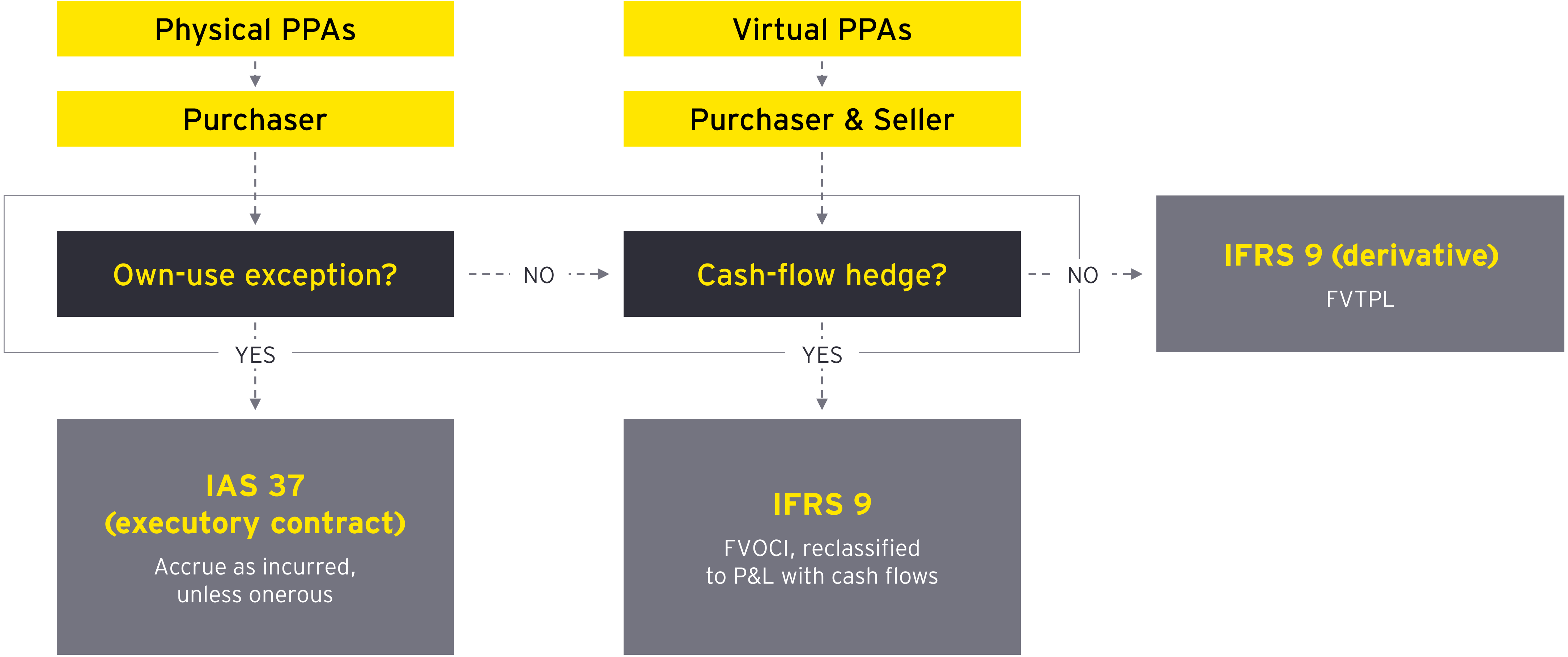
IFRIC AD (2019)
Load Following Swaps

- Solar energy farm sells energy produced in market at spot
- *Hedging instrument* – Load Following Swap with a 3rd party to exchange variable market prices for electricity into fixed prices based on the actual volume of electricity produced

✕ **Does not quality for cash flow hedge**

Forecast energy must be 'highly probable' in order to qualify as a hedged item

Simplified Summary



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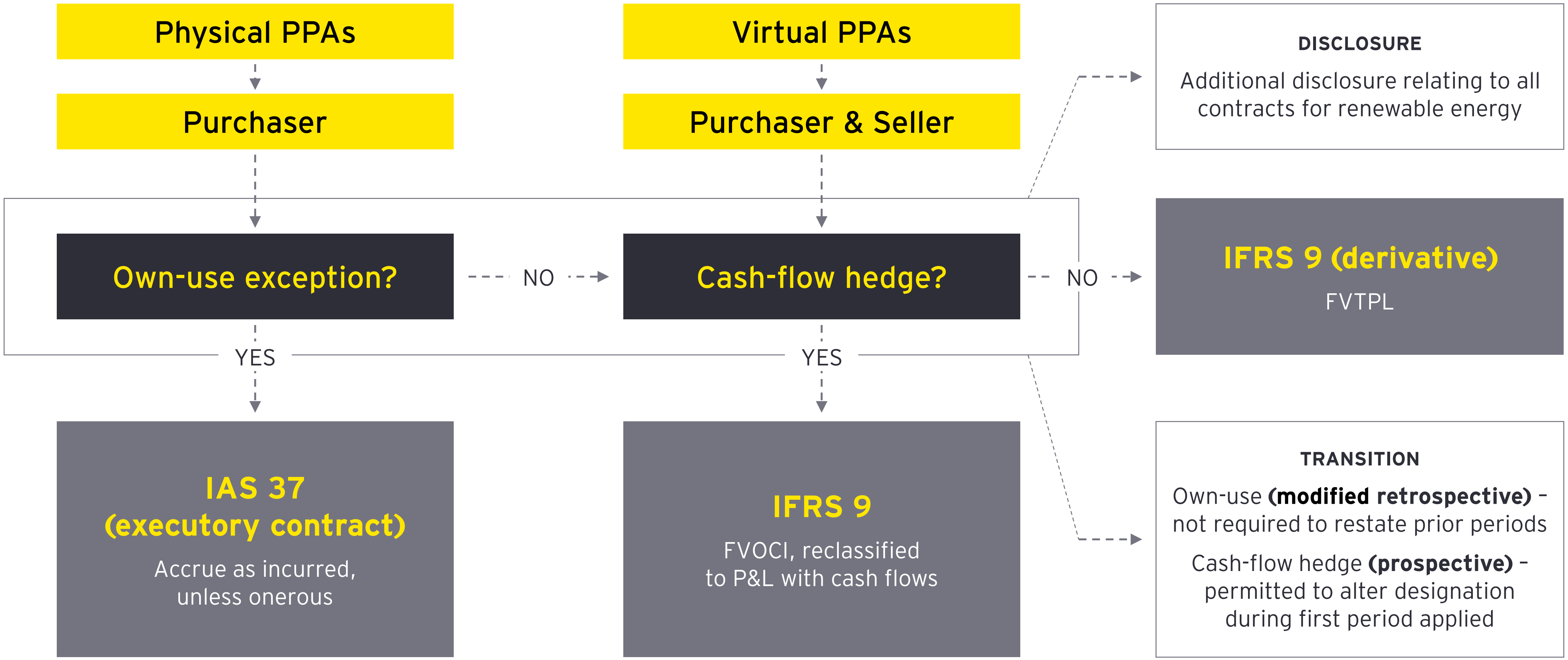

02

A conversation with:

Cameron McInnis

Chief Accountant of the Ontario Securities Commission

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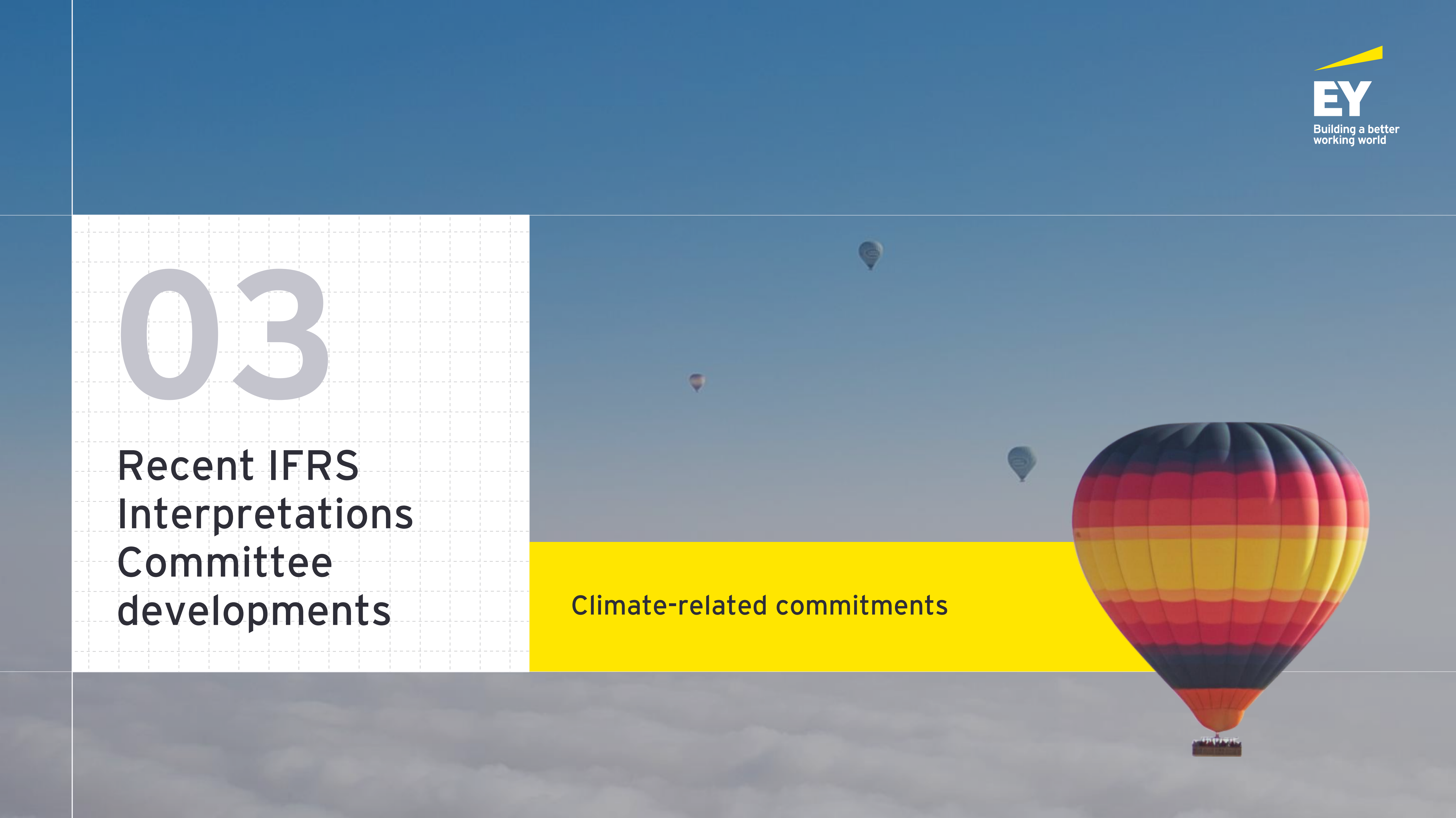

03

Recent IFRS Interpretations Committee developments

Climate-related commitments

IFRIC Agenda Decision

Questions posed to IFRIC regarding the application of IAS 37 for commitments made by an entity to reduce or offset future greenhouse gas emissions

QUESTION 1

Does an entity's commitment to reduce or offset its greenhouse gas emissions create a *constructive obligation* for the entity?

QUESTION 2

Does the constructive obligation satisfy the criteria for recognising *a provision*?

QUESTION 3

If a provision is recognised, is the expenditure required to settle it recognised as an *expense or as an asset* when the provision is recognised?

Fact pattern:

- A manufacturer in 20X0 has committed to reduce its current emissions by at least 60% by 20X9; and
- To offset its remaining emissions in 20X9 and thereafter by buying and retiring carbon credits

Should a liability be recognized today?

IFRIC Agenda Decision

QUESTION 1

Does an entity's commitment to reduce or offset its greenhouse gas emissions create a *constructive obligation* for the entity?

IAS 37.10 defines constructive obligation as an obligation that derives from the following actions:

- The company has published policies or a sufficiently *specific current statement* where the entity has indicated to other parties that it will accept certain responsibilities; and
- As a result, the entity has created a *valid expectation* on the part of those other parties that it will discharge those responsibilities

The Committee concluded:

SPECIFIC STATEMENTS SETTING VALID EXPECTATIONS:

- *Judgement* is required by management to reach a conclusion, considering *facts and circumstances*, as to whether the statements result in a constructive obligation
- If the public statement does not meet the definition of a constructive obligation, no provision is required to be recognized

IFRIC Agenda Decision

QUESTION 2

Does the constructive obligation satisfy the criteria for recognising a *provision*?

IAS 37.14 requires recognition of a provision when:

- The entity has a present obligation (legal or constructive) as a result of a past event;
- It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- A reliable estimate can be made of the amount of the obligation.

The Committee concluded:

PRESENT OBLIGATION

- The commitment is not a present obligation as a result of a past event at the time of the public statement
- The entity will never have a present obligation for future modifications to its manufacturing methods
- Only when the entity has emitted the greenhouse gases it has committed to offset (in 20X9 and later) will it have a present obligation to retire carbon credits

PROBABLE OUTFLOW

- Settling the obligation to reduce greenhouse gas emissions *will not require* an outflow of resources
- Settling the obligation to offset greenhouse gas emissions *will require* an outflow of resources

RELIABLE ESTIMATE

- It is *likely* an entity will be able to make a reliable estimate

IFRIC Agenda Decision

QUESTION 3

If a provision is recognised, is the expenditure required to settle it recognised as an *expense or as an asset* when the provision is recognised?

The Committee concluded the expenditure is recognised as an expense unless the cost gives rise to or forms part of the cost of an item that qualifies for recognition as an asset

COMMENT LETTERS & RATIFICATION

- The committee discussed the comments letters it received on its November 2023 tentative agenda decision
  - Most commentators agreed with the decisions reached by IFRIC
  - IFRIC received a second submission from the original submitter which was determined to not warrant an additional agenda decision
- The IASB ratified the agenda decision in its April 2024 meeting

03

Recent IFRS Interpretations Committee Developments

Disclosure of revenues and expenses for reportable segments

November 2023: Tentative Agenda Decision

Questions posed to IFRIC regarding paragraph 23 of IFRS 8

QUESTION 1

Whether an entity is required to disclose the specified amounts listed in paragraph 23(a)–(i) of IFRS 8 for each reportable segment if those amounts are not reviewed separately by the chief operating decision maker (CODM).

QUESTION 2

How to interpret the meaning of 'material items of income and expense' in the context of paragraph 97 of IAS 1 as referenced in paragraph 23(f) of IFRS 8.

November 2023: Tentative Agenda Decision

QUESTION 1

Whether an entity is required to disclose the specified amounts listed in paragraph 23(a)–(i) of IFRS 8 for each reportable segment if those amounts are not reviewed separately by the chief operating decision maker (CODM).

Specified amounts need to be disclosed when:

Included in the measure of segment profit or loss reviewed by the CODM	OR	Otherwise regularly provided to the CODM

November 2023: Tentative Agenda Decision

QUESTION 2

How to interpret the meaning of 'material items of income and expense' in the context of paragraph 97 of IAS 1 as referenced in paragraph 23(f) of IFRS 8.

IAS 1.97 "When items of income or expense are material, an entity shall disclose their nature and amount separately"

Committee observation	Apply paragraph 7 of IAS 1 (materiality definition)	Apply paragraphs 30-31 of IAS 1 (materiality and aggregation)	Consider both qualitative and quantitative factors
	Without regard to whether that item is presented or disclosed applying a requirement other than paragraph 97 of IAS 1		

November 2023: Tentative Agenda Decision

In summary, the Committee concluded that:

- IFRS provides an adequate basis for an entity to apply the disclosure requirements in paragraph 23(a)-(i) of IFRS 8.
- No standard-setting project will be added to the work plan.

Next Steps:

The Committee is expected to conclude its discussion on the agenda decision at it's June 2024 meeting

Questions?

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Appendix A

IASB workplan (as of May 14, 2024)

Completed Projects

Topic	Related Standard	Effective Date
Subsidiaries without Public Accountability: Disclosures	IFRS 19	January 1, 2027
Presentation and Disclosure in Financial Statements	IFRS 18	January 1, 2027
Lack of Exchangeability (Amendments to IAS 21)	IAS 21	January 1, 2025
Supplier Finance Arrangements (Amendments to IAS 7 and IFRS 7)	IAS 7 and IFRS 7	January 1, 2024
Lease Liability in a Sale and Leaseback (Amendments to IFRS 16)	IFRS 16	January 1, 2024
Classification of Liabilities as Current or Non-current (Amendments to IAS 1)	IAS 1	January 1, 2024
Non-current Liabilities with Covenants (Amendments to IAS 1)		

Standard-setting projects

Topic	Next milestone	Effective Date
Business Combinations – Disclosures, Goodwill and Impairment	Exposure Draft feedback	H2 2024
Dynamic Risk Management	Exposure Draft	H1 2025
Equity Method	Exposure Draft	Q3 2024
Financial Instruments with Characteristics of Equity	Exposure Draft feedback	May 2024
Management Commentary	Decide project direction	June 2024
Rate-regulated Activities	IFRS Standard	2025
Second Comprehensive Review of the IFRS for SMEs (Small and Medium-sized Enterprises) Accounting Standard	IFRS for SMEs Standard	H1 2025

Maintenance projects

Maintenance project		Next milestone	Effective Date
Updating the Subsidiaries without Public Accountability: Disclosures Standard		Exposure Draft	July 2024
Addendum to the Exposure Draft Third edition of the IFRS for SMEs Accounting Standard		Exposure Draft feedback	Q3 2024
Amendments to the Classification and Measurement of Financial Instruments		Final Amendment	May 2024
Annual Improvements to IFRS Accounting Standards	Cost Method (Amendments to IAS 7)	Final Amendment	July 2024
	Derecognition of Lease Liabilities (Amendments to IFRS 9)	Final Amendment	July 2024
	Determination of a 'De Facto Agent' (Amendments to IFRS 10)	Final Amendment	July 2024
	Disclosure of Deferred Difference between Fair Value and Transaction Price (Amendments to Guidance on implementing IFRS 7)	Final Amendment	July 2024
	Gain or Loss on Derecognition (Amendments to IFRS 7)	Final Amendment	July 2024
	Hedge Accounting by a First-time Adopter (Amendments to IFRS 1)	Final Amendment	July 2024
	Introduction and Credit Risk Disclosures (Amendments to Guidance on implementing IFRS 7)	Final Amendment	July 2024
	Transaction Price (Amendments to IFRS 9)	Final Amendment	July 2024
Climate-related and Other Uncertainties in the Financial Statements		Exposure Draft	July 2024
Provisions – Targeted Improvements		Exposure Draft	H2 2024
Power Purchase Agreements		Exposure Draft feedback	Q3 2024
Use of a Hyperinflationary Presentation Currency by a Non-hyperinflationary Entity (IAS 21)		Exposure Draft	July 2024

Research projects

Research project	Related Standard	Effective Date
Post-implementation review of IFRS 15 Revenue from Contracts with Customers	Feedback Statement	Q3 2024
Post-implementation review of IFRS 9 Impairment	Feedback Statement	July 2024
Intangible assets	Review research	Q4 2024

Appendix B

Recent IFRS Discussion Group topics

May 2023 to May 2024

Topic	Meeting Date
IAS 12: Accounting for Deferred Tax Assets under OECD Pillar Two GloBE Rules Discuss the accounting for deferred tax assets when an entity is required to comply with Pillar Two GloBE Rules.	May 2024
IAS 36: Assessment of Cash Generating Units (CGUs) in a Production Facility with Multiple Production Lines When One of the Products Has a Declining Market Demand Discuss the assessment of CGUs in a production facility with multiple production lines when one of the products has a declining market demand. This discussion will focus on identifying CGUs, allocating corporate assets, and other accounting implications.	May 2024

May 2023 to May 2024

Topic	Meeting Date
Revenue Recognition for Carbon Credits Discuss revenue recognition from the sale of carbon credits when the entity is required to make a long-term commitment with a carbon registry to continue its carbon reduction activities as a condition for the certification of the credits.	December 2023
IAS 1: Classification of Liabilities with Covenants when an Entity is Granted a Waiver or Period of Grace Continue discussion on the application of the 2022 amendments to IAS 1, Presentation of Financial Statements on Non current Liabilities with Covenants when an entity is granted a waiver or period of grace.	December 2023
Year-end Financial Reporting Reminders Discuss various financial reporting matters that entities should consider when preparing for their upcoming year-end.	December 2023

May 2023 to May 2024

Topic	Meeting Date
Accounting for the Development of Carbon Credits by a Renewable Energy Generator Discuss how a renewable energy generator classifies and measures renewable energy certificates that it produces and sells or uses to offset its carbon reduction obligations.	September 2023
Unit of Account for Lease Modification Accounting Discuss views on whether lease modifications should be assessed at the contract level or separate lease component level.	September 2023
Accounting for Equity Instruments in a Shares-for-debt Transaction ▸ Discuss factors an entity might consider when determining whether a shareholder-creditor is acting in the capacity of a shareholder. ▸ Discuss the accounting for equity instruments issued and for recognizing extinguishment differences in a shares-for-debt transaction when a shareholder-creditor is acting in such a capacity.	September 2023
IAS 1: Classification of Liabilities with Covenants when an Entity is Granted a Waiver or Grace Period Discuss various practical scenarios and examples of the application of the 2022 amendments to IAS 1 Presentation of Financial Statements on Non-current Liabilities with Covenants when an entity is granted a waiver or grace period.	September 2023

May 2023 to May 2024

Topic	Meeting Date
Accounting for Lending Crypto Assets Raise awareness of the factors an entity might consider when determining the accounting for the lending of crypto assets.	May 2023
Accounting for Earn-in Expenditures Prior To Acquisition of a Mining Interest Discuss how an entity accounts for earn-in expenditures prior to the acquisition of a mining interest, including classification and measurement of earn-in expenditures and disclosure requirements.	May 2023
Accounting for the Development of Carbon Credits that will Ultimately be Sold Discuss how an entity recognizes, measures, and classifies carbon credits that it develops from its already-existing assets carried at fair value.	May 2023

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