

Pollutant pricing mechanisms—Questionnaire

Background

Many respondents to the IASB's Third Agenda Consultation, identified a project on pollutant pricing mechanisms as a high priority. Applying its criteria for adding a project to its work plan, the IASB also concluded that this project is a high priority. However, the IASB decided not to add a project on pollutant pricing mechanisms to its work plan, concluding that other projects were of higher priority.

As part of its ongoing activities, the IASB monitors financial reporting developments and practice and stands ready to address urgent or emerging accounting issues that arise between agenda consultations.

Since completing the Third Agenda Consultation, several stakeholders have suggested that we should prioritise a pollutant pricing mechanism project. They argue that pollutant pricing mechanisms are increasing in prevalence and that there are deficiencies in the accounting for these mechanisms.

Purpose of the questionnaire

As mentioned at the December 2023 ASAF meeting, we would like ASAF members' help to gather more information about:

- The prevalence of pollutant pricing mechanisms.
- The types of entities affected by pollutant pricing mechanisms.
- The significance of pollutant pricing mechanisms to the financial position, financial performance and cash flows of IFRS reporters.
- The accounting issues arising from pollutant pricing mechanisms including whether there is diversity in practice or other deficiencies in the accounting.
- The importance of information about pollutant pricing mechanisms to users of financial statements and whether any deficiency in the accounting adversely affects the usefulness of that information.

This information will help the IASB to assess whether the situation has changed since the Third Agenda Consultation such that the IASB now needs to prioritise a project on pollutant pricing mechanisms ahead of other projects on its work plan.

Structure of the questionnaire

There are three sections to the questionnaire:

- **Section 1: Compliance schemes**— seeks information about pollutant pricing mechanisms that IFRS reporting entities within your jurisdiction are required to participate in by law or other means. Examples of such schemes include carbon taxes and emissions trading schemes—for example, the European Union Emissions Trading Scheme.
- **Section 2: Voluntary schemes**—seeks information about pollutant pricing mechanisms that IFRS reporting entities within your jurisdiction participate in on a voluntary basis, for example through the voluntary purchase of carbon credits.
- **Section 3: Entities that generate or issue credits**— seeks information about IFRS reporting entities that generate or issue credits that can be used to offset emissions made by other entities.

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Next steps

Please provide your response to the questionnaire to Rachel Knubley (rknubley@ifrs.org) by **29th March 2024**.

If you have any questions on any aspects of the questionnaire, please also contact Rachel Knubley.

We plan to present the results of the questionnaire to a future ASAF meeting.

We would like to thank you very much for your help in completing this questionnaire.

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Section 1: Compliance schemes

This section seeks information about pollutant pricing mechanisms that IFRS reporting entities within your jurisdiction are required to participate in by law or other means (compliance schemes). Examples of such schemes include carbon taxes and emissions trading schemes—for example, the European Union Emissions Trading Scheme.

If you are responding on behalf of more than one jurisdiction, it would be helpful to have the information separately for each jurisdiction.

Question 1.1

Please provide a brief description of any compliance schemes that operate in your jurisdiction, including a description of the rights and obligations that arise for IFRS reporting entities that participate in these schemes. Alternatively, please provide a link to where information about such schemes can be found (ideally in English).

Answer 1.1:

There is a significant increase in compliance schemes worldwide and this expansion has multiple dimensions:

- a) Increase in number of countries/jurisdictions introducing such schemes; as you are probably aware, the World Bank's online tool (with "State and Trends of Carbon Pricing Dashboard") provides an overview [<https://carbonpricingdashboard.worldbank.org>]
- b) Increase in scope of the products/services covered by existing schemes – as an example, the European ETS will soon also include maritime shipping. The EU Green Deal includes numerous further proposals to use the ETS mechanism also in new areas such as building decarbonisation, etc.
- c) Indirect effects via complementing mechanisms like the CBAM for ETS: CBAM requires that importers purchase and hold certificates covering at least 80% of the 'imported emissions'. It was brought to our attention that the indirect effect via CBAM potentially expands the scope and magnitude of the accounting issues arising from a lack of guidance in the IFRS.

More specifically, for German companies, the most relevant scheme is the EU Emission Trading System (EU ETS), mentioned above, a 'cap and trade' system. In 2023 an additional ETS was created (EU ETS 2). The ETS limit the total allowed emissions which are allocated to participating companies. For an overview of this program and the participating companies see: [Scope of the EU Emissions Trading System - European Commission \(europa.eu\)](#).

However, German companies – like many others – operate globally. Therefore, various other (national) ETS are potentially relevant (depending on the operations of the companies), e.g. UK ETS or Carbon Credit Systems in the US, Canada or China.

As for the rights and obligations arising from the EU ETS and their accounting under IFRS: Companies typically recognise acquired emission rights either as inventories or intangible assets (emission rights that are allocated to the companies for free are not recognised on the balance sheet due to the cost value approach). Therefore, emission rights are presented as either current or non-current assets. Lately, some companies have decided to present emission rights as "Other assets – current assets". Measurement is usually at cost. In addition, companies present short-term provisions for the obligation to deliver CO₂ emission allowances / certificates for renewable energies.

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While there is some diversity in practice regarding the accounting for ETS emission rights companies generally clearly depict their accounting policy (if this topic is addressed at all). In addition to those legally required compliance schemes companies engage in additional voluntary emission certificate projects to voluntarily offset emissions by investments in (global) offsetting projects. There is no established accounting policy for the accounting for these various voluntary schemes (see section 2 below).

Question 1.2

Do significant numbers of IFRS reporting entities in your jurisdiction participate in compliance schemes? If possible, please indicate the percentage of companies in your jurisdiction that participate in these schemes.

Answer 1.2:

Whether a company participates in compliance schemes depends on the industry that they operate in. We do not have an indication of the percentage of IFRS reporting entities that participate in compliance schemes.

Question 1.3

Please describe the types of IFRS reporting entities that are required to participate in these compliance schemes. For example, what industry do they operate in, are they listed or unlisted entities, what size of entity is required to participate?

Answer 1.3:

See the link above to the EU website laying out the scope of the EU ETS.

As of 2024 emissions are covered from installations in the energy sector, manufacturing industry, aircraft operators flying within the EU and departing to Switzerland and the United Kingdom and from maritime transport.

Question 1.4

How significant are the financial effects of these schemes to the financial position, financial performance and cash flows of the entities affected?

Answer 1.4:

For some industries there can be significant financial effects (e.g. energy sector), but that is not yet widely spread due to various reasons. Nevertheless, (different) ETS will be of increasing importance for companies worldwide and financial effects will increase. Which is why a common understanding of the nature of those ETS as well as voluntary schemes in terms of accounting guidance is necessary.

So far, financial effects are not comparable due to several reasons: scope of participating companies; certificates that are provided for free versus certificates bought at market rates; different accounting treatments across the world (not just the various accounting treatments mentioned above, but also regarding gross or net presentation, see research from the TU München, link: <https://ssrn.com/abstract=4752533>); differences between compliance schemes on the one side and voluntary schemes on the other.

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Question 1.5

Are there plans to introduce new compliance schemes or expand the scope of existing compliance schemes in your jurisdiction?

I'm not aware of such plans.

Yes, there are such plans.

If the answer is Yes, please provide details:

Answer 1.5:

As part of the 2023 revisions of the ETS Directive, a new emission trading system (ETS 2) was created. This will cover CO2 emissions from fuel combustion in buildings, road transport and additional sectors (mainly small industries not covered by existing EU ETS).

Therefore, harmonized, transparent accounting rules are even more important.

Question 1.6

Is there guidance in your jurisdiction on how to account for these schemes?

No (then go to Question 1.7)

Yes

If the answer is Yes, please describe or provide a link to any such guidance (ideally in English):

Answer 1.6:

There is some guidance, but not sufficient (therefore, yes/no):

- Publication of Institute of Public Auditors in Germany, IDW RS HFA 15 of 1.3.2006 (regarding accounting for emission trading schemes under German GAAP)
- Some additional literature
- However, no clarification in IFRS which companies feel is needed. In particular, clarification by the standardsetter seems necessary since there is an increasing focus on these aspects. For example, ESMA declared „Emission Trading Schemes“ as an Enforcement Priority. In order to evaluate the accounting for ETS during enforcement audits ESMA and the national enforcement authorities will have to develop an understanding of adequate accounting. While enforcement activities are meant to not to result in accounting interpretations, it is possible that those findings will provide the frame for further discussions – considering the lack of IASB guidance.

Again, we would like to draw your attention to the research from TU München analysing the regulations of certain national standard setters: Spain, France, Austria, Portugal, Italy (see link above). According to that research all of these local standards provide some guidance, but neither offers a comprehensive accounting model. This circumstance rather fuels the divergence in practice than leading to convergence or consistency.

Question 1.7

If there is no guidance on how to account for these schemes, please describe the main accounting approaches used in your jurisdiction to account for these schemes.

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Answer 1.7:
See above, question 1.

Question 1.8

Are you aware of diversity in practice or other deficiencies in the accounting for these schemes in your jurisdiction?

- I'm not aware of diversity in practice or other deficiencies.
- Yes, I'm aware of diversity in practice or other deficiencies (then go to Question 1.9).

Question 1.9

If diversity in practice or other deficiencies exist, do you have evidence that these deficiencies adversely affect the usefulness of information provided to users of financial statements?

- I don't have such evidence.
- Yes, I have such evidence.

If the answer is Yes, please describe that evidence:

Answer 1.9:
While we analysed the answers and annual reports of some preparers, we did not get a chance to involve users in this process so far. Therefore, we cannot provide insight on the (adverse) affect on the usefulness of the information provided. However, the research that was brought to our attention (conducted by TU München) analysed 34 steelmakers participating at the ETS (thereof 15 IFRS preparers). The study fully confirmed diversity in practice.

In addition, the FASB's active agenda includes a project on Environmental Credit Programs which underlines the demand for accounting guidance. Furthermore, while the FASB project is still ongoing, IFRS preparers could be asked to consider FASB guidance via IAS 8 if IFRS lack specific guidance on the subject. However, IFRS preparers prefer a specific solution in the context of IFRS.

Question 1.10

Have you conducted, or do you plan to conduct, any research in this area?

- No
- Yes

If the answer is Yes, please describe the research conducted or planned:

Answer 1.10:

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Section 2: Voluntary schemes

This section seeks information about pollutant pricing mechanisms that IFRS reporting entities within your jurisdiction participate in on a voluntary basis—for example, through the voluntary purchase of carbon credits (voluntary schemes).

If you are responding on behalf of more than one jurisdiction, it would be helpful to have the information separately for each jurisdiction.

Question 2.1

Do IFRS reporting entities in your jurisdiction participate in voluntary schemes to reduce or offset their emissions?

No

Yes

If the answer is Yes, please describe the main types of schemes that operate in your jurisdiction including a description of the rights and obligations that arise for entities that participate in these schemes:

Answer 2.1:

There is a very wide range of voluntary schemes worldwide and companies have purchased extensive volumes of 'carbon credits' (sometimes labelled as 'offsets').

However, with the forthcoming IFRS S2 and ESRS regulations (and potentially the SEC's climate rule), there should be an increase in disclosure transparency and rigor via the more robust standards. Some see a potential decrease in the volume of voluntary schemes because some of the credits/offsets might not fulfil the necessary criteria.

The question remains, how these voluntary schemes are to be depicted (if at all) in the balance sheet and whether recognition criteria have to be defined to prevent diversity in practice.

Question 2.2

Do significant numbers of IFRS reporting entities in your jurisdiction participate in voluntary schemes? If possible, please indicate the percentage of companies in your jurisdiction that participate in these schemes.

Answer 2.2:

Yes. But we are not able to provide an indication of the percentage of companies that participate in voluntary schemes.

Question 2.3

Is the prevalence of voluntary schemes in your jurisdiction increasing?

No

Yes

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Question 2.4

Please describe the types of IFRS reporting entities that participate in these voluntary schemes. For example, what industry do they operate in, are they listed or unlisted entities, what size of entity participates?

Answer 2.4:

We are not aware of research on the types of IFRS reporting entities that tend to participate in these voluntary schemes in Germany.

Question 2.5

How significant are the financial effects of these schemes to the financial position, financial performance and cash flows of the entities affected?

Answer 2.5:

We are not aware of research on the financial effects of these voluntary schemes in Germany. Currently, more companies seem not to capitalize the expenditures for these voluntary projects, but to recognize those as expenses.

Question 2.6

Do these schemes give rise to accounting issues that are difficult to resolve?

No

Yes

If the answer is Yes, please describe the accounting issues that arise from these schemes:

Answer 2.6:

Accounting issues can potentially arise from the differences of these voluntary schemes and the different accounting approach that companies take (e.g. capitalizing / expenditure or recognition of a liability or not).

In general, these voluntary schemes have similar accounting issues as mandatory schemes. But ultimately the details of the accounting treatment can in fact vary quite significantly from the mandatory schemes, which can be adequate (e.g. if those schemes contain no future benefit or cannot be traded), but for which accounting guidance (e.g., applying the recognition criteria) would be helpful.

Question 2.7

Are you aware of diversity in practice or other deficiencies in the accounting for these schemes in your jurisdiction?

I'm not aware of diversity in practice or other deficiencies.

Yes, I'm aware of diversity in practice or other deficiencies (then go to Question 2.8).

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Question 2.8

If diversity in practice or other deficiencies exist, do you have evidence that these deficiencies adversely affect the usefulness of information provided to users of financial statements?

I don't have such evidence.

Yes I have such evidence.

If the answer is Yes, please describe that evidence:

Answer 2.8:

While we do not have evidence from users of financial statements, the general assumption is that diversity in practice reduces the usefulness of information provided to the users.

Question 2.9

Have you conducted, or do you plan to conduct, any research in this area?

No

Yes

If the answer is Yes, please describe the research conducted or planned:

Answer 2.9:

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Section 3: Entities that generate or issue credits

This section seeks information about IFRS reporting entities that generate or issue credits that can be used to offset emissions made by other entities. In responding to the questions in this section, please exclude information about entities—for example, governmental bodies—that do not report under IFRS Accounting Standards.

If you are responding on behalf of more than one jurisdiction, it would be helpful to have the information separately for each jurisdiction.

Question 3.1

Do IFRS reporting entities in your jurisdiction generate or issue credits (for example, carbon credits) that can be used to offset emissions made by other entities?

No

Yes

If the answer is Yes, please describe the nature of these credits, including the rights and obligations that arise from these credits:

Answer 3.1:

The prevalence or non-prevalence of this issue depends on the underlying definitions. There are 'credits' issued by operators of cap-and-trade schemes, but also 'credits' issued by entities claiming to capture and/or avoid emissions via nature-based or technology-based approaches.

Question 3.2

Do significant numbers of IFRS reporting entities in your jurisdiction generate or issue such credits? If possible, please indicate the percentage of companies in your jurisdiction that generate or issue such credits.

Answer 3.2:

We are not aware that this is an issue for a significant number of IFRS reporting entities, but rather limited to a certain industry (energy industry).

Question 3.3

Is the number of IFRS reporting entities in your jurisdiction that generate or issue credits increasing?

No

Yes

Question 3.4

Please describe the types of IFRS reporting entities that generate or issue credits. For example, what industry do they operate in, are they listed or unlisted entities, what size of entity generates or issues these credits?

Answer 3.4:

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Question 3.5

How significant are the financial effects of these credits to the financial position, financial performance and cash flows of the entities affected?

Answer 3.5:

Question 3.6

Does issuing or generating credits give rise to accounting issues that are difficult to resolve?

No

Yes

If the answer is Yes, please describe the accounting issues that arise from these activities:

Answer 3.6:

Question 3.7

Are you aware of diversity in practice or other deficiencies in the accounting for these credits in your jurisdiction?

I'm not aware of diversity in practice or other deficiencies.

Yes I'm aware of diversity in practice or other deficiencies (then go to Question 3.8).

Question 3.8

If diversity in practice or other deficiencies exist, do you have evidence that these deficiencies adversely affect the usefulness of information provided to users of financial statements?

I don't have such evidence.

Yes I have such evidence.

If the answer is Yes, please describe that evidence:

Answer 3.8:

Question 3.9

Have you conducted, or do you plan to conduct, any research in this area?

No

Yes

If the answer is Yes, please describe the research conducted or planned:

Answer 3.9:

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