ASCG • Joachimsthaler Str. 34 • 10719 Berlin

Dr Andreas Barckow
Chair of the
International Accounting Standards Board
Columbus Building
7 Westferry Circus / Canary Wharf
London E14 4HD

Financial Reporting Technical Committee
Phone: +49 (0)30 206412-20
E-Mail: info@drsc.de

Berlin, 7 August 2024

Dear Andreas,

ED/2024/3 – *Contracts for Renewable Electricity (Proposed amendments to IFRS 9 / IFRS 7)*

On behalf of the Accounting Standards Committee of Germany, I am writing to comment on ED/2024/3 *Contracts for Renewable Electricity (Proposed amendments to IFRS 9 / IFRS 7)*, issued on 8 May 2024 (herein referred to as 'ED'). We appreciate the opportunity to comment on the proposals.

Overall, we support the IASB's efforts to clarify and amend existing IFRS 9 / IFRS 7 requirements on the own-use exemption (OuE) in the context of energy contracts with a renewable source.

First of all, we acknowledge that a narrow scope was deliberately chosen to encourage a swift development of the proposals. On this basis, we support the IASB's approach for scoping and ring-fencing the proposed amendments. Further, we acknowledge that the IASB is proposing amendments on how to apply the own use exemption under IFRS 9.2.4 as well as providing a relief for applying cash flow hedge accounting. This allows addressing concerns raised by constituents over two different, but equally relevant types of contracts for renewable electricity (namely physical and virtual power purchase agreements). We fully agree with this approach.

As regards the specific proposals in the ED, we like to confirm our general support. However, we have identified some room for improvement as regards the wording, and we have reservations as regards some of the proposed characteristics or features. In particular, we

- generally agree with the proposed scope (issue/question #1), but suggest further specification or amended wording, mainly for the "pay as produced" characteristic in para. 6.10.1(b);
- are not convinced about the factors to be considered in applying the OuE (#2), in particular we have reservations against the "purchase" criterion in para. 6.10.3(b)(iii);
- overall agree with the hedge accounting proposals (#3);

- have <u>some reservations</u> against the proposed disclosures (#4 and 5);
- <u>overall agree</u> with the transition requirements (#6);
- <u>suggest</u> 1 January 2026 as effective date (#7).

Further, we like to note that in the ED amended guidance is located within the hedge accounting section (Sec. 6.10.) of IFRS 9. We support, what the IASB have already indicated, relocating the final requirements to appropriate sections, thereby necessarily splitting the requirements' location.

For more details on our remarks on the specific proposals in the ED, we refer to our responses to the questions which are laid out in Appendix A to this letter.

In addition to our comments that directly relate to the ED, we like to touch again on the narrow approach that the IASB has chosen for developing amendments. Although supporting this narrow approach to allow for a timely solution, we like to state that it excludes other contracts which have been – and still are – under discussion, e.g. oversized contracts, as portrayed in the respective submission to the IFRS IC. We are aware that similar application questions arise as those other contracts are, and might become increasingly, prevalent.

This said, we deem it worth providing some comments and remarks we received as part of our outreaches on those contracts that are beyond the scope of this ED. Since a swift process for developing and finalising the proposed amendments is desired, we suggest that our additional findings be considered separately, i.e. for potential future deliberation. Therefore, our comments on those issues are laid out in a separate Appendix B to this letter.

It should also be noted that the proposed amendments create rule-based exceptions to some of the basic principles of IFRS 9. Individual IASB members have also taken a critical stance on the ED. In this respect, it may be appropriate to first finalise these amendments and then, at a later stage, to review these rules in a separate project for their adherence to the IFRS 9 accounting principles and, if necessary, to develop those principles further.

If you would like to discuss any of our comments further, please do not hesitate to contact Jan-Velten Große (grosse@drsc.de) or me.

Yours sincerely,

Sven Morich

Vice President

Appendix A – Answers to the questions in the ED

Question 1 – Scope

Paragraphs 6.10.1–6.10.2 … would limit the application of the proposed amendments to only contracts for renewable electricity with specified characteristics.

Do you agree that the proposed scope would appropriately address stakeholders' concerns … while limiting unintended consequences for the accounting for other contracts? Why or why not?

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

Overall, we acknowledge that contractual characteristics are an essential element for determining the scope of any proposed amendments or clarifications. During our discussions, we have recognised that these characteristics relate directly to the source of electricity and the volume produced (i.e. they focus on an *absolute* volume risk). However, for many contracts – i.e. those that potentially qualify for applying the own use exemption (OuE) – the crucial point is whether, and why, contractual features may lead to excess or shortfall quantities produced compared to the quantity needed (i.e. this constitutes a *relative* volume risk). Therefore, it is partially difficult to link our respective comments directly to either issue #1 (scope) or to issue #2 (OuE). Hence, our comments on issues/questions #1 and #2 are interconnected.

Considering the specific proposals as regards the scope, we generally agree with the scope as set out in the ED. However, we have identified some room for further specification.

First, we point to the **term "renewable"**, which is used throughout the proposals without being properly defined. Since this term is not defined, we are not convinced that it is clear beyond doubt what it is supposed to convey. As it is a superordinated feature, placed above the two characteristics in para. 6.10.1(a)-(b), we suggest the IASB consider describing or defining it.

As regards **lit. (a), the "nature-dependent" criterion**, we conclude that this is basically appropriate and convincing. In agreeing with this narrow scope for sources of electricity (namely solar, wind, and water power), it appears coherent that other sources of electricity/energy are excluded from the scope (e.g. gas, biomass). However, we note that this narrow scope excludes other types of contracts that are similarly prevalent. In this respect, we refer to our additional comments in Appendix B.

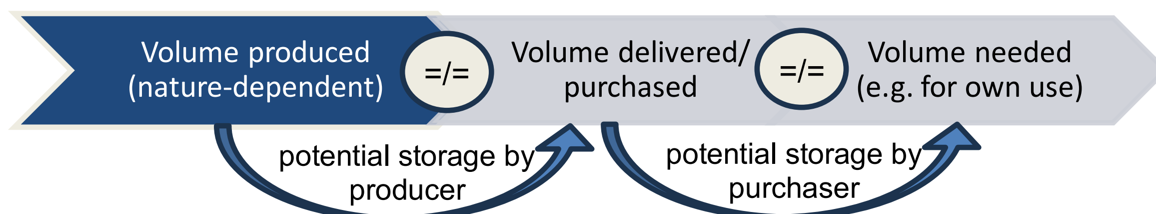
On balance, we agree with this first characteristic (para. 6.10.1(a)).

As regards **lit. (b), the "pay as produced" criterion**, we conclude that it roughly captures the most crucial aspect specific to the types of contracts under discussion. However, we are not convinced that this term is sufficiently appropriate, as it might unintendedly narrow down the population of contracts covered by the clarifications.

"Pay as produced" features are common and widely used for fixing (and transferring) the risk of an uncertain, not guaranteed volume of energy. Hence, it reflects an "uncertain quantity".

However, there are – increasingly – deviating contractual features, often referred to as "pay as nominated" or "pay as forecasted". Those features also fix (and transfer) a volume risk, thus also reflecting an "uncertain quantity" of electricity. All these terms differ from each other depending on the extent or the nature of volume risk effectively transferred. In other words, contractual features differentiate whether the volume risk transferred relates to the volume effectively *produced*, or to the volume *actually delivered* (which may deviate from the volume produced), or to the volume *forecasted to be delivered*, etc. As we understand the overall idea of and reasons behind the IASB's proposals, the "pay as produced" criterion is meant to also cover "pay as nominated" or "pay as forecasted" features. If so, we suggest reconsider and potentially amend the term "pay as produced". If not so, we deem a broader reconsideration of this criterion to be essential.

In addition, we like to point to the fact of increasing **storability of electricity**. We acknowledge this to increasingly influence contractual features intended to capture volume risk. Depending on the extent of storing renewable electricity and depending on which party (the producer or the purchaser) will store it, the volume *produced* might not equal the volume *delivered/ purchased* at specific points in time or during specific periods. Hence, the volume risk (i.e. potential deviations) may occur in two different stages (see graphic below).



The volume risk currently described in the ED as "the risk that the volume … produced does not align with the … demand" (para. 6.10.1(b)) does not mention, thus does not sufficiently clarify, whether (partial) storage is regarded to (partially) reduce this volume risk. This said, we are not sure whether and how (non-)storability has been considered and whether and how it is reflected by the proposals.

Further, we like to note that **cap clauses or "base load contracts"** are also widespread and relevant. It seems unclear whether these are covered by the proposals, as in these cases the volume risk is transferred only partially. Thus, strictly speaking they seem to be excluded. Again, our understanding of the IASB's proposals is that contracts with those clauses are similarly considered, and should be covered, by the proposals. If so, we suggest clarifying this. If not so, considering it would be worthwhile.

Overall, despite our basic support we have some reservations against this second characteristic (para. 6.10.1(b)) as per the current wording in the ED. Thus, we kindly ask the IASB reconsider and potentially clarify or amend the wording of the criterion in lit. (b).

Question 2 – Own use requirements

Paragraph 6.10.3 … includes the factors an entity would be required to consider when applying IFRS 9.2.4 to contracts to buy and take delivery of renewable electricity that have 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?

The proposals appear to be very case-based amendments. We acknowledge again that the proposals do intend to address specific circumstances, thus providing clarity to those specific issues accompanied by carefully ringfencing the scope. However, the criteria as regards how to apply the OuE – as set out in para. 6.10.3 – might be too narrow or too specific, thereby excluding other types of contracts that are, or may become, similarly prevalent. In this respect, we refer to our additional comments in Appendix B.

As regards **para. 6.10.3(a)**, we agree with the proposals. On these, we have not identified unclear or inappropriate wording.

As regards **para. 6.10.3(b)**, we generally support the idea of addressing (i) the reason for sales and (ii) whether timing and pricing is at the discretion of the entity. Yet, we do not agree with some of the respective wording. Moreover, we deem (iii) considering whether sales imply expected (re-)purchases that interrelate with those sales being inappropriate and redundant.

In respect of the condition in **lit. (b)(i)**, we basically agree that the volume risk and the resulting timing mismatch should be the reason for any sale. However, we refer to our answer on Q1, expressing reservations as regards the imprecise description of "volume risk" (and potential different variations of what the volume risk is). These reservations similarly affect lit. (b)(i).

In respect of the condition in **lit. (b)(ii)**, we understand and support the intention, but are not convinced that the wording is broadly helpful. As per the current wording of an "entity not having the practical ability to determine timing or price", we consider some contracts to be unintendedly excluded. Sometimes, entities sell excess quantities prior to delivery, as soon as the excess becomes obvious or vey probable. Such action is commonly referred to as "balancing" on a so-called "day ahead market". Balancing could be considered as a practical ability to determine the timing and/or price of sales, thus failing the condition in (b)(ii). Even further, some entities make use of an automatic mechanism (so-called "auto trader") for excess sales, thereby reducing (or excluding) the degree of influencing timing or price of any sales. Current wording in the ED might suggest that only an auto-trader mechanism would fulfil the condition in (b)(ii), which would narrow-down the practical use of the intended relief.

Summing up our findings on lit. (b)(i) and (b)(ii), we suggest that proposed wording be re-deliberated and potentially amended, aiming at a more general wording that captures sales without the intention of short-term selling and profit-taking (see IFRS 9.2.6).

Our main, and more severe, reservations relate to the condition in **lit. (b)(iii)**.

Firstly, the **“repurchase” criterion** does not appear appropriate because repurchases may not (or not in the same quantity) come along with earlier partial sales, or because partial/excess sales and repurchases are not always causally linked. In addition, excess sales and repurchases may also take place in reverse. Furthermore, sometimes excess sales and repurchases cannot be allocated to the same contract, but rather to different contracts within an energy contract portfolio, or simply to the entire portfolio. In addition, sales and repurchases sometimes occur because of cross border transactions, due to the market design. Under these circumstances, and obviously due to market structure, entities sell and repurchase quantities in different grids/markets. This effectively is like a virtual transportation of electricity. Finally, we acknowledge that excess sales and repurchases can also take place in different group entities.

We are not entirely clear, but derive from general understanding throughout the IFRSs literature, that this would still be in line as far as both entities are part of the same reporting unit (”the entity”). Hence, we would appreciate were the IASB clarifying this.

Secondly, the **example of “one month”** for an appropriate repurchase period is not suitable in practice, as production cycles (of the purchaser) and seasonal demand patterns cover significantly longer periods. A possible repurchase period further depends on the specific source of electricity, as the production patterns of different technologies/sources of “renewable electricity” have different degrees of predictability (e.g. the overall pattern, maybe not the quantity, for solar power is more “season-depending” than for wind power). We suggest that another, more general wording – like “usual operating cycle”, which would be one year, or even without example for a specific period – should be found for expressing the ”reasonable period”.

Summing up our findings on lit. (b)(iii), we feel that the repurchase requirement deserves a fundamental reconsideration.

Finally, it appears questionable how criterion (b)(iii) relates to (b)(i) and (b)(ii). Considering our reservations as described above, we feel that criteria (b)(i) and (ii) – subject to amended wording – do sufficiently ringfence and clarify which sales under the specific circumstances are considered in line with the requirements in IFRS 9.2.6. Altogether, criterion (b)(iii) appears needlessly complicated and even redundant.

Question 3 – Hedge accounting requirements

Paragraphs 6.10.4–6.10.6 … 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?

We acknowledge, and consider it essential, that the proposals as regards hedge accounting focus on virtual power purchase agreements (PPAs) and on some physical PPAs (those not eligible for the OuE), whereas the OuE clarifications relate exclusively to physical PPAs. Hence, we clearly welcome the IASB's approach to provide a solution not only for applying the OuE but on challenges around hedge accounting, too.

As regards the specific proposals on hedge accounting, we take the view that they represent a relief for producers/suppliers as well as for buyers. Thus, we overall agree with the proposals.

Further, we like to mention that the question has arisen whether the proposals are also applicable in the case of economic portfolio/macro hedging. Since applying cash flow hedge accounting for an economic macro hedge is allowed in general, we take the view that it should also be allowed under these specific circumstances. If so, we believe it could be worth clarifying this explicitly.

Question 4 – Disclosures

Paragraphs 42T–42W … 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?

Generally, we consider the proposed disclosures acceptable in part, but in its entirety to be too far-reaching. This is based on two main reasons:

- First, the proposals would require disclosure of more information for contracts for renewable electricity than for other (long-term) executory contracts (i.e. those not within the scope of these amendments or even not within the scope of IFRS 9). Although the proposals provide an exception from, the current own-use requirements in IFRS 9, we do not comprehend why specific contracts (as are contracts for renewable electricity) deserve specific, more intensive disclosures than those other executory contracts.

- Second, we have been made aware that the entire set of proposed disclosures would cause more efforts and costs than expected (cf. BC49), while at the same time they provide less decision-useful (and less reliable) information than assumed.

In pointing to some proposed details, we like to comment as follows:

- We welcome as a relief that fair value disclosures (for contracts that are not measured at FVtPL, hence are eligible for the OuE) are not required (para. 42T(b)). Also, we consider the permission to aggregate the volumes to time bands (para. 42T(b)(ii)) being a practical solution providing useful information.
- However, as regards the proposal to disclose proportions (renewable electricity vs. total electricity sold or purchased, paras. 42U, 42V) we consider it unfavourable that such information be disclosed in the notes as part of the financial statements, as for other contracts no similar disclosures are required. Further, we deem it more suitable that this information be provided, and integrated, in relevant sections of the non-financial (ie. sustainability) report.
- Further, it appears unclear whether volume and proportion disclosures in accordance with paras. 42U, 42V refer to energy units or value/monetary units.

In summary, we suggest the following compromise: The entire set of disclosure requirements be generally reduced and, in addition, all remaining disclosure requirements be narrowed-down so that they are mandatory only for contracts for renewable electricity that are eligible for the OuE in IFRS 9, but not for those accounted for at FVtPL under IFRS 9, or even under other IFRSs (e.g. IFRS 15 or IFRS 16).

Question 5 – Disclosures for SwoPA (IFRS 19)

Paragraphs 67A–67C … 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?

We acknowledge that the proposed disclosures under IFRS 19 nearly equal those under IFRS 7, except for IFRS 7.42W, for which there is no proposed equivalent in IFRS 19. This said, we do not understand why that requirement in IFRS 7.42W is not identically proposed under IFRS 19. Therefore, we suggest adding an identical paragraph to IFRS 19.

As regards any of the IFRS 19 disclosures proposed in the ED, we acknowledge and like to note – as we did on earlier occasions – that assessment is difficult, since IFRS 19 has not yet been applied and therefore no practical experience is available yet.

However, our comments on Q4 (as regards IFRS 7) equally apply to Q5 (as regards IFRS 19).

Question 6 – Transition

The IASB proposes to require an entity to apply:
(a) the amendments to the own-use requirements using a modified retrospective approach;
(b) the amendments to the hedge accounting requirements prospectively.

Early application … would be permitted from the date the amendments were issued.

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?

We consider the proposed transition requirements to be balanced and appropriate, thus, we fully agree. In particular, we consider not requiring restatement of prior periods to be a very helpful relief.

Question 7 – Effective date

Subject to feedback on the proposals in this ED, 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.

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?

If you disagree, what effective date would you suggest instead and why?

We like to confirm that timely first-time application is desirable. Thus, a timely effective date seems useful.

Responding to the suggestion of a first-time application from 1 January 2025, we have not yet sufficient evidence whether, or to what extent, entities would broadly be ready for transition by 1 January 2025. As a compromise, we suggest 1 January 2026 as the effective date, accompanied by an option for voluntary early application. This would provide presumably sufficient room for all entities affected, comprising those wishing to immediately apply the amendments and those wishing to have more time (ie. beyond end of year 2024) for preparation and transition.

Appendix B – Further comments received from outreach

As introduced in our cover letter, we are aware that the proposals do intend to address specific circumstances, thus providing clarity and relief to those specific and urgent issues accompanied by carefully ringfencing the scope.

While agreeing on that narrow-scope approach given the circumstances, not all our constituents agree with it from a holistic perspective. This is because this narrow-scope approach excludes other types of contracts, e.g. PPA that are in part early settled due to energy savings, or PPA commonly referred to as oversized contracts. Both are portrayed in the respective submission to the IFRS IC (see issues 2 and 3). Those types of contracts are similarly prevalent, have been – and still are – under discussion, and they appear to bring about similar accounting issues.

Obviously, the ED's proposals as regards the (narrow) scope lead to those other contracts not being covered by the proposed amendments. It is our additional and more crucial finding, that the criteria as regards how to apply the OuE – as set out in para. 6.10.3 – are too narrow or too specific, thereby excluding those other contracts from the proposed amendments. Therefore, we like to explore on this in more detail.

The ED's proposals do cover contracts that fall short of the company's own needs ("net buyers", from a purchaser's perspective, see 6.10.3(b)). In practice, however, there are also contracts for a quantity more than the company's own needs ("net sellers", from a purchaser's perspective), for which the proposals are not applicable.

For some of those other types of contracts, the volume delivered may or will exceed the company's own needs because of an unexpected surplus of electricity produced – i.e. "unintentional" surplus. For other contracts, the volume delivered will purposely exceed the company's own needs – i.e. "intentional" surplus, or "oversized contracts" in a narrower sense.

Those contracts described are not covered by the ED's proposals, on the ground that such contracts generate permanent mismatches between the volume produced/delivered and the volume needed for own use – in other words, mismatches that do not arise solely due to the volume risk (see BC20). Yet, we struggle with the reasoning why oversized contracts (net sellers) are not in the scope while "undersized contracts" (net buyers) are. The explicit reasoning (as per BC20) for not including oversized contracts is that the "oversize" is not in accordance with the entity's expected usage requirements. Though, any undersized contract would equally, but inversely, generate permanent mismatches between the volume produced and the volume needed for own use, thus is also not in accordance with the entity's expected usage requirements.

Treating those two types of contracts, i.e. "net seller" and "net buyer" contracts, differently is comprehensible only from an accounting perspective, as the excess quantity would require (appropriate) accounting, while a shortfall quantity would not.

However, a different treatment appears inconsistent from a conceptual perspective. The reason is that, in most cases, deviation of the quantity produced/delivered from the (expected) quantity needed for own use (i.e. the "volume risk") is random – because of nature-dependency. More precisely, it is often unpredictable, and sometimes sheer coincidence, whether:

(a) the volume of electricity produced/delivered is exceeding or is falling below a fixed (expected) volume needed for own use – at least in case of minor deviations;
(b) any deviation is temporary and will be "reversed" within a reasonable period (whatever the definition of reasonable period would be) or is permanent, i.e. does not reverse within that reasonable period, or does not even reverse in the far future;
(c) any deviation (shortfall or excess) only results from volume risk or results from intentionally oversizing the contract, or results from both – if so, it would be difficult to differentiate what part of the deviation is incidental/nature-depending and what part is intentional.

In the light of these explanations, several of our constituents felt that it was not imperative that undersized contracts may align with the own use criterion (under certain conditions) while oversized contracts may not at all, as is the established principle and now affirmed by the ED's proposals. Instead, they take the view that the discriminatory treatment of undersized vs oversized contracts deserves thorough reconsideration.