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7 August 2024

Dear Sir

Exposure Draft ED/2024/3: Contracts for Renewable Electricity

We are pleased to comment on the above Exposure Draft (the ED). Following consultation with the BDO network[1], this letter summarises views of member firms that provided comments on the ED.

We support the objective of the IASB to clarify how the own use requirements are applied to contracts for renewable electricity, as well as the expansion of the hedge accounting requirements in IFRS 9 *Financial Instruments* to include certain contracts with variable notional amounts. However, we believe the proposals should be clarified in a number of areas:

- IFRS 9.6.10.3(b)(iii): clarification of the basis under which an entity should assess whether the 'reasonable time' criterion is met. For example, it would be helpful to include a period of time that would be considered unreasonable in a specific set of circumstances.
- IFRS 9.6.10.3(b)(iii): clarification of how the 'equivalent volume of electricity' criterion and how the 'net-purchaser' concept noted in BC20(c) is assessed.
- We believe the hedge accounting requirements should be clarified in a number of areas:
    - IFRS 9.6.4.10(b): over which period of time should the 'do not exceed' criterion be assessed.
    - As a hedge accounting relationship with a variable notional hedged amount is not eligible under the current criteria in IFRS 9, an illustrative example would be beneficial in understanding how the mechanics of hedge accounting would be applied.
- IFRS 9.7.2.52: clarification of how a change in the designation of a hedge accounting relationship on transition is accounted for.

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We also have concerns about the volume of additional required disclosures that are proposed in IFRS 7.

Finally, we suggest that the effective date of the amendments be for annual reporting periods beginning on or after 1 January 2026 with earlier adoption being permitted. This would assist those jurisdictions which have an endorsement or similar process for the adoption of new requirements in IFRS Accounting Standards.

Our detailed responses to the questions in the ED, along with the reasons for our concerns, are set out in the attached Appendix. The Appendix only includes responses to questions where we have concerns or suggestions.

We hope that you will find our comments and observations helpful. If you would like to discuss any of them, please contact me at +44 (0)7875 311782 or by email at abuchanan@bdoifra.com.

Yours faithfully

Andrew Buchanan

Global Head of IFRS and Corporate Reporting

Appendix

Question 2 – Proposed 'own-use' requirements

Paragraph 6.10.3 of the proposed amendments to IFRS 9 includes the factors an entity would be required to consider when applying paragraph 2.4 of IFRS 9 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?

We generally agree with the proposals. However, we suggest that IFRS 9.6.10.3(b)(iii) be clarified to address two points:

1. The basis under which an entity should assess the 'reasonable time' criterion; and
2. Clarification of how the 'equivalent volume of electricity' criterion should be assessed

<u>#1 – The basis under which an entity should assess the 'reasonable time' criterion</u>

To assess the own use exception criterion in IFRS 9.2.4, the ED proposes that for contracts that have the characteristics in paragraph 6.10.1, an entity would consider the reasons for past and expected sales of unused renewable electricity within a short period after delivery. Such sales would be in accordance with the entity's usage requirements if three criteria are met, with IFRS 9.6.10.3(b)(iii) being that 'the entity expects to purchase at least an equivalent volume of electricity within a reasonable time (for example, one month) after the sale.'

We understand that the IASB did not specify how a 'reasonable time' should be assessed, and that the example of one month is intended to demonstrate that a 'reasonable time' is typically a short time (BC20(c)). However, we believe it would be beneficial for the IASB to specify the parameters that should be considered when assessing whether the equivalent volume being purchased occurs within a 'reasonable time'. For example, should the reasons for the delay in purchasing an equivalent volume of electricity relate only to operational reasons (e.g. a 'high' and a 'low' season for production) or supply constraints (e.g. the supply of electricity having 'high' and 'low' periods of production due to nature-based factors such as photovoltaic electricity production varying depending on the seasons in certain regions such as the global north), or is the 'reasonable period' assessment meant to be interpreted as an absolute measure of time where an entity is to develop an accounting policy for assessing the meaning and apply it consistently?

We suggest that the IASB clarify the intended meaning of 'reasonable time', or at least include an explanation of the concept in the Basis for Conclusions to IFRS 9. Additionally, it would be useful

if the IASB included an example of a period of time that would not be considered reasonable and the reasons for that period not being reasonable if entity-specific factors should be considered.

#2 – Clarification of how the 'equivalent volume of electricity' criterion should be assessed

The proposed paragraph IFRS 9.6.10.3(b)(iii) would require that 'the entity expects to purchase at least an equivalent volume of electricity within a reasonable time (for example, one month) after the sale.'

We understand that the underlying principle in this criterion is that the entity should remain a 'net-purchaser' of electricity in order for the contract to be accounted for using the own-use exception. However, we believe it is unclear whether this requirement refers to a purchase of electricity from the spot market or whether the purchase of the delivered electricity from the contract for electricity would also fulfil this requirement.

In performing outreach on the ED, we have identified two alternative interpretations of the criterion in IFRS 9.6.10.3(b)(iii). We have illustrated these alternative interpretations using an illustrative fact pattern.

Assume that Entity A is the purchaser in a power purchase agreement. Any unused electricity in a month is sold back into the grid at the spot price. The actual volume of electricity delivered under a power purchase agreement and Entity A's usage requirements are as follows (expressed in units of electricity):

Month	Actual Delivery	Usage	Excess/(deficiency) of usage vs. actual
1	10	10	0
2	11	5	(6)
3	8	7	(1)
4	5	5	0
5	8	8	0
Totals	42	35	(7)

In month 2, Entity A used 6 units of electricity less than what was delivered and, therefore, those 6 units were sold back into the grid at the spot price. In the following month, Entity A used 7 units of electricity, 1 unit more than what had been sold in the previous month.

Interpretation #1: If, as at the end of month 2, Entity A expected to purchase and use 7 units of electricity in month 3, then the criterion in IFRS 9.6.10.3(b)(iii) would be met because the use of 7 units in month 3 exceeds the sale of unused electricity in month 2 of 6 units. Therefore, over the span of months 2-3, Entity A will remain a 'net-purchaser' of electricity as the total volume of

electricity purchased under the contract and from the spot market exceeds sales into the spot market.

Interpretation #2: Entity A is not a 'net-purchaser' because Entity A sold 7 units of electricity over months 2 and 3 into the spot market. Under this interpretation, to be a 'net-purchaser', an entity would need to repurchase any excess capacity sold into the spot market within a reasonable period of time. In order for Entity A to meet criterion IFRS 9.6.10.3(b)(iii), in month 3 (or some other period of time considered to be 'reasonable'), Entity A would have to purchase at least 6 units of electricity from the spot market in month 3, so 14 units in total (8 units under the contract for electricity and 6 from the spot market).

We recommend that the IASB clarifies the requirement.

Question 3—Proposed hedge accounting requirements

Paragraphs 6.10.4–6.10.6 of the proposed amendments to IFRS 9 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 generally agree with the proposals, although we recommend that the IASB:

- Clarifies the period over which the 'do not exceed' criterion in IFRS 9.6.4.10(b) should be assessed to determine if a hedging relationship is eligible. We assume that this criterion is meant to be interpreted in the context of discrete periods of time (i.e. 'time buckets') over the hedging relationship rather than the entire contractual period in total. However, we consider the wording of IFRS 9.6.4.10(b) to be unclear.
- Adds an illustrative example to IFRS 9, demonstrating how a hedge accounting relationship with a variable notional amount may be accounted for, including the basis under which an entity reclassifies amounts accumulated in other comprehensive income to profit or loss. Hedge accounting has been applied by entities for many years, but a variable notional amount has never been permitted by IFRS Accounting Standards, which we believe may result in diversity in practice. An illustrative example, which demonstrates how the requirements are applied mechanically may reduce diversity and uncertainty about the meaning of the requirements.

Question 4—Proposed disclosure requirements

Paragraphs 42T–42W of the proposed amendments to IFRS 7 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?

In our view, the proposed disclosure requirements in IFRS 7 do not strike an appropriate balance of cost vs. benefits.

The proposed disclosure requirements in IFRS 7.42T would apply to contracts that have the characteristics in IFRS 9.6.10.1. Many of these contracts would be accounted for in accordance with the own-use exception. Other contracts accounted for in accordance with the own-use exception do not require similar information to IFRS 7.42T, and we do not believe that only certain contracts for renewable electricity should have disclosure requirements that significantly exceed those that are required for other executory contracts. For example, an entity that uses significant amounts of copper in production processes may have material contracts accounted for as executory contracts, but the disclosure requirements of IFRS 7.42T would not apply, even if the economic importance of those contracts significantly exceeds contracts for renewable electricity. If the IASB believes that the disclosure requirements for contracts accounted for using the own use exception should be revised, we consider that it would be preferable for this to be undertaken as a holistic project, and not one that imposes disclosure requirements on only certain types of own-use contracts.

We do not agree with the proposed disclosure requirements in IFRS 7.42V. We primarily disagree for a similar reason to our view on proposed paragraph IFRS 7.42T; that these disclosures do not apply to other own-use contracts. We see no conceptual basis for requiring these disclosures for contracts for renewable electricity, while other own use contracts are exempted from similar disclosures.

We also believe that some of these disclosures may be better suited for sustainability reporting rather than financial reporting, as they appear to focus on providing users with information about the proportion of total electricity that is consumed by an entity that is renewable or 'green'.

Question 6—Transition requirements

The IASB proposes to require an entity to apply:

- *(a) the amendments to the own-use requirements in IFRS 9 using a modified retrospective approach; and*
- *(b) the amendments to the hedge accounting requirements prospectively.*

Early application of the proposed amendments 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 generally agree with the proposals, though we believe that proposed paragraphs IFRS 9.7.2.51 and 9.7.2.52 should be clarified.

<u>IFRS 9.7.2.51</u>

If an entity applies the amendments in a reporting period that includes the date the amendments are issued, then we believe the IASB's intention is for the amendments to be applied such that the effect reverses the previous accounting treatment applied by the entity, however, we do not believe the drafting of IFRS 9.7.2.51 accomplishes this.

For example, assume that prior to the amendments being adopted, Entity D had measured a power purchase agreement at fair value through profit or loss because it concluded that it failed the own use exception in IFRS 9. As at 31 December 2023, the contract was measured as a liability at CU100. The amendments to IFRS 9 are issued on 1 October 2024, when the fair value of liability has increased to CU140, meaning an additional CU40 loss was recorded in profit or loss during fiscal 2024. Applying the amendments, Entity D concludes that the contract now meets the own use exception.

We believe the intention of the amendments would be for Entity D to reverse the CU100 liability recorded as at 1 January 2024 (DR liability 100, CR opening retained earnings 100), with the additional CU40 recorded as a loss in fiscal 2024 being reversed (DR liability 40, CR profit or loss 40). The combined effect of these entries would be such that the power purchase effect is not accounted for 'on balance sheet' in 2024 and any previous effects are reversed.

However, applying IFRS 9.7.2.51 literally, it appears that Entity D would be required to record the following as at the date the amendments are issued (1 October 2024 in this example):

DR liability	140	
CR opening retained earnings		140**

**CU140 represents the 'difference between the previous carrying amount [140 – the carrying amount immediately before the amendment is adopted] and the carrying amount at the date

when the amendments are issued [0 – assuming that the application of the amendments results in the derivative being derecognised]'

This adjustment of CU140 to retained earnings exceeds the effect recorded in opening retained earnings, which is CU100. We do not believe this is the intention of the amendments, therefore, we suggest that the IASB clarify the requirements.

IFRS 9.7.2.52

It is unclear how an entity would account for a previous designation of a hedged item in a cash flow hedging relationship that was designated before the date the amendments are first applied when the volume of the hedged item increases or decreases, as a result of the application of the amendments. We assume that when the volume of the hedged item increases, which we believe would be the case in most instances, that the effect of hedge accounting would be reflected prospectively (i.e. on a go forward basis only). However, while it would appear less likely to arise in practice, if a designation decreases upon transition, it is unclear to us how such a reduction in the hedged item would be reflected on transition, including the effect on the cash flow hedge reserve. We recommend that the IASB clarify this in the final amendments.

Question 7—Effective date

Subject to feedback on the proposals in this Exposure Draft, 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 suggest that the IASB set the effective date of the amendments to be for annual reporting periods beginning on or after 1 January 2026, rather than 2025, with earlier application permitted.

If final amendments are published in Q4 2024, this would leave a very limited amount of time for entities with quarterly filing options to assess the effect of the amendments for Q1 2025 reporting, including any effect on previously designated hedging relationships.

We also understand that the amendments, even if published in Q4 2024, are not expected to be endorsed by the European Union until well into 2025, meaning that a 1 January 2025 effective date could lead to a 'staggered' implementation date in multiple jurisdictions depending on whether an entity applies IFRS Accounting Standards as endorsed by a national standard setter/other body or IFRS Accounting Standards as issued by the IASB. This outcome would be particularly problematic for groups with multiple levels of reporting, where certain entities may be

required to adopt on 1 January 2025 with others at a later date if they are based in the European Union, which could be costly.

We note that our suggested effective date would align the effective date with the amendments to IFRS 9 and IFRS 7 *Classification and Measurement of Financial Instruments.* While those amendments are not directly related to this exposure draft, requiring a larger suite of financial instrument amendments to be effective all at the same time would be less costly to implement than adding certain amendments in 2025 and others in 2026.