Beyond the GAAP

Forvis Mazars' monthly newsletter on financial and sustainability reporting

Contents

3 Editorial

3 IFRS Highlights / International

8 European Highlights

The drafting of the present issue was completed on 4 October 2024.

Editorial

The IASB continues to be very busy with standard-setting work around the topic of financial instruments, with redeliberations ongoing on the proposed amendments to the provisions on PPA and VPPA contracts, and the launch of a research project on amortised cost measurement. It has also begun new projects to clarify or improve some older standards, publishing an exposure draft to address application questions relating to the equity method (IAS 28) and launching another research project on the statement of cash flows (IAS 7).

Things are a little quieter on the sustainability reporting front, although the European Commission has recently published other corrigenda to the Delegated Regulation on ESRS Set 1 in the Official Journal of the European Union (OJEU). They make significant language improvements to some translations into EU official languages like French or German, without changing the substance of the regulation. Furthermore, at the international level, consideration of social issues is gathering force with the creation of a dedicated taskforce bringing together around 20 organisations from the public, private and third sectors, with the aim of contributing to improved sustainability reporting standards.

IFRS Highlights / International

IASB redeliberates proposed amendments to IFRS 9 and IFRS 7 on contracts for renewable electricity

In May 2024, the International Accounting Standards Board (IASB) published an exposure draft of proposed amendments to IFRS 9 – *Financial Instruments* and IFRS 7 – *Financial Instruments: Disclosures* on contracts for renewable electricity, known as ’PPAs’ (power purchase agreements) and ’VPPAs’ (virtual power purchase agreements) (see Beyond the GAAP no. 188, 2024).

After examining a summary of feedback received (available here) in August 2024, the IASB began redeliberating in September 2024, considering the comments received on the scope of the amendments and the own-use classification.

Scope

Feedback on the ’nature-dependent’ aspect of the source of production included:

- the relevance of the concepts of ’renewable’ energy and ’nature-dependent’ energy sources; and
- the impact of the producer’s ability to control the production of energy (e.g. by opening or closing a hydroelectric dam).

Comments on the purchaser’s exposure to volume risk included:

- the relevance of limiting the scope to ’pay-as-produced’ features when other contractual features, such as ’pay-as-contracted’ features, are also commonly used but do not involve limitation of the volume risk for the purchaser;
- the impact of features such as caps or floors, which purchasers sometimes include in contracts; and
- the appropriate unit of account when transactions are carried out through market structures that involve intermediaries (aggregators, suppliers, etc.) or when the contract is accompanied by the delivery of renewable energy certificates.

In this context, the IASB tentatively decided to finalise the amendments, subject to clarifying that contracts falling within the scope of the amendments:

- reference electricity that is i) generated from nature-dependent sources and ii) whose quantity cannot be controlled by human intervention (according to the staff papers, contracts for renewable energy generated by a hydroelectric dam would fall outside the scope of the amendments, as production is regulated by human intervention);

- can be settled net, through payment of the difference between the contractually agreed price and the market price (for VPPAs) or gross, through payment of the contractually agreed price (for physical PPAs); and
- expose an entity to cash-flow variability that depends on the contracted amount of electricity generated from nature-dependent sources.

Some aspects relating to volume risk were addressed in the context of the discussions on 'own-use' classification.

Finally, the term 'nature-dependent electricity' (or NDE) may replace 'renewable electricity' in the final text of the amendments, if the IASB follows the staff recommendation.

Own-use classification

Feedback focused on the following topics:

- how the proposals interact with paragraphs 2.4 and 2.6 of IFRS 9;
- the concept of an 'oversized' contract;
- the concept of a 'reasonable time' and the appropriate referenced market when matching purchases and sales.

The IASB tentatively decided to finalise the amendments on own-use requirements, clarifying how the rules introduced by the amendments interact with the current paragraphs 2.4 to 2.7 of IFRS 9.

The rules introduced by the amendments require an entity to classify a contract as 'own-use' if the following three criteria are met:

- the contractual features expose the entity to the risk of taking delivery of more electricity than it requires in any delivery interval;
- the design and operation of the market requires the entity to immediately resell the oversupply of electricity at the current market price; and
- the entity is a net purchaser, i.e. it expects to buy enough electricity in the same referenced market to at least offset sales of any oversupply, within a reasonable time.

This 'reasonable time' shall be determined by taking account of i) the seasonality of the source of electricity and the entity's business cycle, and ii) all reasonable and supportable information, including forward-looking information, at the date of the assessment. However, it may not exceed twelve months, either prospectively or retrospectively.

At its upcoming meetings, the IASB will examine feedback received on the proposed amendments on hedge accounting, disclosures in the notes, and transition. The aim is to publish the final amendments by the end of 2024 (though they would not be endorsed by the European Union until 2025).

IASB publishes exposure draft on the equity method (IAS 28)

In September 2024, the IASB published an exposure draft (available here) on the equity method set out in IAS 28 – *Investments in Associates and Joint Ventures*.

The amendments proposed by the IASB in the exposure draft are primarily intended to address the application questions presented below, which we will return to in detail in a future issue, including the responses proposed by the IASB.

Initial recognition

- When an investor or joint venturer initially measures the cost of an associate or joint venture:
  - should it include any previously held ownership interest in the cost?
  - should it include any contingent consideration in the amount transferred, and if so, how should it measure that contingent consideration?
- Should the investor or joint venturer include the deferred tax effects related to its share of the fair value of the associate's or joint venture's identifiable assets and liabilities?

Changes in ownership interest

- When an investor or joint venturer buys or sells an ownership interest, while retaining significant influence or joint control, how should it measure:
  - the additional ownership interest?
  - the ownership interest disposed of?

- How should an investor or joint venturer account for other changes in ownership interests (e.g. if an associate issues new shares to a third party and the investor's ownership interest decreases), how should it recognise any resulting gain or loss?

Share of profit or loss and other comprehensive income

- If an investor or joint venturer has reduced the carrying amount of its investment to nil, should it:
  - recognise any unrecognised losses as a 'catch up' adjustment when it purchases an additional ownership interest?
  - recognise separately its share of profit or loss and its share of other comprehensive income?

Transactions with associates or joint ventures

- How should an investor or joint venturer recognise gains or losses resulting from the sale of a subsidiary to its associate or joint venture, in light of the provisions set out in IFRS 10 – *Consolidated Financial Statements* and IAS 28 – *Investments in Associates and Joint Ventures*? While IFRS 10 requires the entity to recognise the gain or loss resulting from the sale in full, IAS 28 requires a share of this gain or loss to be eliminated, to the extent of the entity's interests in the associate or joint venture.

Impairment and impairment indicators

- Should a decline in the fair value of an investment in an associate or joint venture be taken as evidence of impairment?
- Should an investor or joint venturer assess a decline in the fair value of the net investment by comparing the fair value to the initial purchase cost or to the carrying amount at the relevant closing date?

Timetable

The comment period runs until 20 January 2025.

Following the consultation, the IASB will decide on the future direction of the project, depending on the feedback (and if relevant, will decide on the effective date of the proposed amendments).

IASB begins research project on amortised cost measurement of financial instruments (IFRS 9)

In July 2022, the IASB decided to add to its research programme a project on amortised cost measurement of financial instruments, in light of the feedback received in the Post-implementation Review (PiR) of IFRS 9 – *Financial Instruments* Phase I. The project now also includes some points raised as part of the PiR of IFRS 9 Phase II (see Beyond the GAAP no. 190, 2024).

At its September 2024 meeting, the IASB discussed the project direction. The preliminary list of possible topics drawn up by the staff includes topics relating to the effective interest rate (EIR) and to modifications of financial assets and liabilities.

The topics related to the EIR are as follows:

- how to reflect uncertainty resulting from conditions attached to the contractual interest rate (such as indexing to ESG criteria) when determining the effective interest rate on initial recognition;
- accounting for revised estimates and contractual modifications to future cash flows; and
- accounting for unamortised transaction costs or fees received as part of a modification of financial assets and financial liabilities, as well as the meaning of the phrase 'fees and costs incurred' from the perspective of both the lender and the borrower.

The topics related to modifications of financial assets and liabilities are as follows:

- the definition of a modification, i.e. whether it refers only to contractual terms, or more broadly to cash flows, in line with the amendments to IFRS 9 relating to interest rate benchmark reform;
- the quantitative and/or qualitative criteria used to determine whether modifications to assets lead to derecognition of those assets, depending on whether the modification is related to forbearance or on-market renegotiations;
- the distinction between partial derecognition and modification of an asset, and the interaction between these requirements and those relating

to expected credit losses, including the order in which these requirements should be applied;

- how gains and losses resulting from modification of an asset should be presented in profit or loss;
- the criteria used to determine when a financial asset should be written off, and how to present a loss arising from a write-off or a gain arising from a recovery of these amounts in profit or loss; and
- how to account for financial concessions (partial forgiveness of debts, payment holidays, etc.) as modifications of assets, write-offs or impairment, depending on whether these concessions are related to forbearance or required by law.

The IASB will continue discussions on this project by organising targeted meetings with its advisory bodies.

IASB begins research project on the statement of cash flows (IAS 7)

In September 2024, the IASB announced the launch of a research project to review and improve the requirements for the statement of cash flows and related matters under IFRS Accounting Standards. The launch of this project follows feedback received in the IASB's Third Agenda Consultation, which identified this project as a high priority.

Stakeholders, particularly investors, suggested that the current requirements of IAS 7 – *Statement of Cash Flows* should be improved in order to provide more useful information to users of financial statements.

The IASB will now carry out initial research, including meetings with stakeholders and a review of existing literature, to gather evidence of the nature and extent of perceived omissions in current reporting and the likely advantages of drawing up new financial reporting requirements.

The IASB is planning to discuss the initial findings of its research and to identify next steps in the first quarter of 2025.

IFRS 15 PiR: IASB work reaches a conclusion

As we announced in our previous issue (see Beyond the GAAP no. 190, 2024), the IASB completed its Post-implementation Review of IFRS 15 – *Revenue from Contracts with Customers* in September 2024, deciding not to take any standard-setting action in the immediate future.

A project summary and feedback statement are available on the IASB's website here.

IFRS Foundation Trustees create strategic insights group

The IFRS Foundation Trustees have announced the creation of the IFRS Foundation Group of Fellows, a strategic insights group, chaired by Professor Lucrezia Reichlin.

The group will provide the Trustees with evidence to improve their understanding of the impact of IFRS Accounting Standards on the global economy, and other strategic issues that are relevant to the future of the IFRS Foundation.

The members of the group are as follows:

- Lucrezia Reichlin (chair), Professor of Economics at the London Business School and former IFRS Foundation Trustee;
- Professor Patrick Bolton of Imperial College London;
- Dr Ma Jun, President of the Institute of Finance and Sustainability in Beijing;
- Professor Christian Leuz, University of Chicago Booth School of Business; and
- Luiz Awazu Pereira da Silva, former Deputy General Manager of the Bank of International Settlements and former Deputy Governor of the Central Bank of Brazil.

The members of this strategic insights group have been appointed for an initial three-year term. They will meet periodically and report to the Trustees to support their decisions.

International taskforce created to improve reporting on social matters

September 2024 saw the launch of the 'Taskforce on Inequality and Social-related Financial Disclosures' (TISFD), whose goal is to develop a global framework that will help companies and financial institutions to communicate more effectively on their impacts, dependencies, risks and opportunities relating to social matters, including inequality.

The framework will be developed by integrating international standards on business conduct with reporting standards, to ensure market usability.

The taskforce is the result of a collaboration between around 20 organisations from the public, private and third sectors, and will be led by four co-chairs:

- Peter Bakker, president of the World Business Council for Sustainable Development (WBCSD);
- Sharan Burrow, former general secretary of the International Trade Union Confederation (ITUC);
- Arunma Oteh, former treasurer and vice-president of the World Bank; and
- Gabriela Ramos, Assistant Director-General for Social and Human Sciences at UNESCO.

An overview of the project is presented in the document People in Scope.

Subsequently, EFRAG announced that it had signed a cooperation agreement with the TISFD to advance social-related financial disclosures.

Adoption of sustainability reporting standards in emerging markets and developing economies

The World Bank Group and the IFRS Foundation announced their commitment to build on their existing partnership around IFRS Accounting Standards to support the adoption of sustainability standards in emerging markets and developing economies (EMDEs).

As part of this, the World Bank has established a roadmap to align its climate and sustainability-related financial disclosures with the International Sustainability Standards Board (ISSB) standards.

Voluntary adoption of ISSB standards – guidance for preparers

The IFRS Foundation has published Voluntarily applying ISSB Standards—A guide for preparers in response to calls from investors for voluntary application of the standards to enable consistent reporting. While adoption of the ISSB standards is progressing around the world, this guidance supports companies in providing voluntary reports where there are no regulatory requirements to do so.

Updates on jurisdictional adoption of sustainability reporting

The latest developments in adoption of the IFRS Sustainability Disclosure Standards (SDS) around the world include:

- Hong Kong – The Hong Kong Institute of Certified Public Accountants (HKICPA) has issued an invitation to comment on Exposure Drafts of HKFRS S1 (General Requirements) and HKFRS S2 Climate-related Disclosures. The proposed standards are fully aligned with the IFRS SDS. The consultation is open until 27 October 2024.
- Malaysia – The Malaysian Stock Market (Bursa Malaysia) has issued consultation on proposed amendments to the listing rules in relation to sustainability reporting. These listing rules changes will require reporting by listed entities, commencing in 2025, under the recently adopted National Sustainability Reporting Framework (NSRF) issued by the securities commission. The NSRF is aligned with the IFRS SDS.

ISSB update – September 2024 meeting

The ISSB September update and podcast are available, summarising the September 2024 meeting and other recent activities of the ISSB. Although the ISSB discussed its research projects and the SASB (Sustainability Accounting Standards Board) standards identified as priorities for improvement, no decisions were made at the September 2024 meeting. In the September 2024 podcast, the ISSB Chair and Vice-Chair summarise recent activities including key messages from a webinar on industry-based disclosures and external engagement activities, as well as providing an update on adoption of the standards.

European Highlights

European Commission publishes new corrigenda to ESRS Set 1

During the summer, the European Commission (EC) published in the Official Journal of the European Union (OJEU) several corrigenda to the Delegated Regulation on the first set of European Sustainability Reporting Standards (ESRS), which was endorsed by the EC on 31 July 2023 and published in the OJEU on 22 December 2023 (see Beyond the GAAP no. 183, 2023-2024).

These new corrigenda make significant language improvements with respect to the translation into several official EU languages (e.g. French, German), without changing the substance of the regulation.

As a reminder, an initial corrigendum was already published in April 2024 (see Beyond the GAAP no. 187, 2024), primarily to amend incorrect paragraph references.

Contact us

Dingeman Manschot
Partner, Forvis Mazars, the Netherlands
dingeman.manschot@forvismazars.com

Inge van Sloun
Director, Forvis Mazars, the Netherlands
inge.vansloun@forvismazars.com

Renick van Oosterbosch
Director, Forvis Mazars, the Netherlands
renick.vanoosterbosch@forvismazars.com

Edouard Fossat
Partner, Forvis Mazars, France
edouard.fossat@forvismazars.com

Carole Masson
Partner, Forvis Mazars, France
carole.masson@forvismazars.com

Contributors to this issue:

Vincent Gilles, Marie-Anastasia Harmand, Clémence Lordez, Laura Niewiadomskyj, Pierre Savu, Arnaud Verchère and Paul Winrow

Forvis Mazars Group SC is an independent member of Forvis Mazars Global, a leading global professional services network. An internationally integrated partnership operating in over 100 countries and territories. Forvis Mazars Group specialises in audit, tax and advisory services. The integrated partnership draws on the expertise and cultural diversity of its teams - more than 35,000 professionals worldwide - to assist clients of all sizes at every stage in their development.
Go to forvismazars.com to find out more.