# Update on the IFRS Interpretations Committee's activities

## Objective

1 The objective of this paper is to provide, for information purposes, a summary of the main open issues discussed by the IFRS Interpretations Committee (the 'IFRS IC' or the 'Committee').

2 The paper focuses on the issues that are still 'open' at the date of the summary, that is, matters that have not yet led to a final decision by the IFRS IC.

3 The purpose of the presentation is to raise EFRAG FR TEG's and EFRAG CFSS's awareness on the issues being discussed at the IFRS IC and possible interactions with EFRAG's commenting activities and future standard setting. The session is not intended, however, to respond to the IFRS IC tentative decisions. Therefore, the paper does not contain the EFRAG Secretariat's initial views on the issues and does not seek EFRAG FR TEG's nor EFRAG CFSS's technical assessment on the matters.

4 If EFRAG FR TEG or EFRAG CFSS express the wish to further discuss any of the presented issues, a session could be organised at a future meeting. EFRAG TEG-CFSS members can also express the need to participate in IASB´s outreach on the topics listed.

## Overview of IFRS IC's current activity

5 Below is an overview of the IFRS IC's current activities.

| **Project/Topic** (including hyperlinks to the IASB project pages for each item) | **Related Standards** | **Current status** | **Next milestone** | **Next milestone expected date** |
|---|---|---|---|---|
| **Initial consideration** | | | | |
| Climate-related Commitments | IAS 37 | Nov 2023 IFRS IC meeting | Tentative Agenda Decision feedback | Not specified |

| **Project/Topic** (including hyperlinks to the IASB project pages for each item) | **Related Standards** | **Current status** | **Next milestone** | **Next milestone expected date** |
|---|---|---|---|---|
| Disclosure of Revenues and Expenses for Reportable Segments | IFRS 8 | Nov 2023 IFRS IC meeting | Tentative Agenda Decision feedback | Not specified |
| **Finalisation of agenda decision** | | | | |
| Merger between a Parent and Its Subsidiary in Separate Financial Statements | IAS 27 | Nov 2023 IFRS IC meeting | IASB meeting | Not specified |
| **Input to IASB** | | | | |
| Climate-related and Other Uncertainties in the Financial Statements | IAS 36 | Nov 2023 IFRS IC meeting (also, consulting stakeholders) | IASB meeting | Not specified |
| Provisions—Targeted Improvements | IAS 37 | Nov 2023 IFRS IC meeting (also, consulting stakeholders) | IASB meeting | Not specified |
| Power Purchase Agreements | IFRS 9 | Nov 2023 IFRS IC meeting (also, consulting stakeholders) | IASB meeting | Dec 2023 |
| **End of consultation period** | | | | |
| Payments Contingent on Continued Employment during Handover Periods | IFRS 3 | Consultation deadline of 20 Nov 2023 | Tentative Agenda Decision feedback | Q1 2024 |

## Initial consideration

*Climate-related Commitments*

*Issue and background*

6 The IFRS IC received a submission seeking clarification on how to apply IAS 37 Provisions, Contingent Liabilities and Contingent Assets to climate-related risks and related commitments (e.g., “Net Zero transition commitments”).

7 In particular, the submitter discussed a plurality of examples[1] of "Net zero transition commitments", defined as statements in which an entity indicates that it has accepted a responsibility to reduce its carbon emission, and asked three questions:

(a) Question 1 - does the public statement of a net zero transition commitment create a constructive obligation as defined in IAS 37?

(b) Question 2 - does a constructive obligation created by a net zero transition commitment meet the criteria in IAS 37 for recognising a provision?

(c) Question 3 - if a provision is recognised, is the expenditure required to settle it recognised as an asset or as an expense when the provision is recognised?

8 Based on the IASB's tentative decision at the September 2023 meeting the IASB Staff concluded that the matters described in the submission have widespread and material effect on affected entities.

9 The IASB Staff created a specific fact pattern that reflects two common features of the aforementioned Net Zero transition commitments and that can be summarised as follows:

(a) Entity is a manufacturer;

(b) In December 20X0 it publicly states the following commitments:

(c) to reduce greenhouse gas emissions by 60% by 20X9; and

(d) to offset the remaining greenhouse gas emissions in 20X9 and thereafter by buying carbon credits.

(e) Entity publishes a detailed plan setting out how it will gradually modify its manufacturing methods between 20X1 and 20X9 and management is confident that it can make all the proposed modifications.

10 In addition to the questions above, the IASB staff discussed other accounting consequences of such a commitment (i.e., potential impacts to be reflected in accordance with other IFRS Accounting Standards).

[1] Examples of "Net zero transition commitments" discussed in the submission include: end state commitments (i.e., responsibility to reduce carbon emission by a specified future date), interim commitments (i.e., responsibility to reduce carbon emission by a specified interim date before the end date), commitments to actions that have a secondary effect of reducing carbon emissions and transition plans of entities in the oil and gas sector (e.g., to replace fossil fuel production with renewable energy production).

### *IASB Staff analysis and recommendations*

Question 1 - does the public statement of a net zero transition commitment create a constructive obligation as defined in IAS 37?

11 Based on the requirements in IAS 37.10 and 20[2], the IASB staff concluded that:

(a) Other parts are involved as specifically required by IAS 37.20. Indeed, the entity's obligation would be owed to all people adversely affected by entity's emissions (i.e., the public at large); but

(b) A net zero transition commitment does not necessarily create a constructive obligation; indeed, entity's management would need to judge whether such a commitment has created a valid expectation in the public at large as required by IAS 37.20. In doing so, factors affecting management's conclusion might include:

(i) The language used in the statements, which could strengthen or soften the likelihood an entity will fulfil its commitment;

(ii) The specificity and status plans supporting the statement – if it is supported by formally-approved and detailed plans (e.g., detailing the nature and timing of expected actions, the milestones to be achieved and how management will measure entity's progress)

(iii) The timing of the actions required to fulfil the commitment – short and medium-term plans are less likely to be changed that those for longer term actions;

(iv) Publicly available evidence of progress to date – evidence that an entity has achieved communicated milestones may enhance expectations in achieving also longer-term goals.

Question 2 - does a constructive obligation created by a net zero transition commitment meet the criteria in IAS 37 for recognising a provision?

12 The IASB staff analysed whether the submitted fact pattern met all the following three criteria for recognising a provision in accordance with IAS 37.14:

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[2] **IAS 37.10** defines a constructive obligation as: "An obligation that derives from an entity's actions where:

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities."

**IAS 37.20** states that: "[…] Because an obligation always involves a commitment to another party, it follows that a management or board decision does not give rise to a constructive obligation at the end of the reporting period unless the decision has been communicated before the end of the reporting period to those affected by it in a sufficiently specific manner to raise a valid expectation in them that the entity will discharge its responsibilities."

(a) The present obligation criteria – the entity has a present obligation as a result of a past event, which has to exist independently of entity's future actions (IAS 37.18-19);

   (i) In the submitted fact pattern, the IASB staff concluded that the entity has not a present obligation for the following reasons:

      - all the costs of modifying its manufacturing methods and of purchasing carbon credits need to be incurred to operate in the future and, therefore, when an entity publishes it net zero transition commitment in 20X0 they do not exist independently of the entity's future actions;
      - The entity will at some point incur a present obligation to pay for resources it purchases to modifying its manufacturing methods (e.g., new plant or equipment) but only when it receives those resources; and
      - The entity will have a present obligation to purchase carbon credits only if and when it emits greenhouse gases in 20X9 and later year.

(b) The probable outflows criteria – it is probable that an outflow of resources will be required to settle the obligation;

   (i) In the submitted fact pattern, the IASB staff concluded that satisfying the probable outflow assessment depends on the nature of the actions required to settle the constructive obligation. In particular:

      - Commitment to reduce greenhouse gas emissions does not satisfy this recognition criteria because for any cost an entity will incur in to modify its manufacturing methods it will receive resources (e.g., a new plant) in exchange for this expenditure.
      - Conversely, the commitment to offset remaining gas emission from 20X9 does satisfy such a criterion as the entity will not receive any resources in exchange for its purchase of carbon credits.

(c) The reliable measurement recognition criteria – a reliable estimate can be made of the amount of the obligation.

   (i) In the submitted fact pattern, the IASB staff concluded that if the other two criteria are satisfied, it is likely that also the reliable measurement recognition one will be met. Indeed, in 20X9 and thereafter and only for a constructive obligation to purchase carbon credits to offset remaining greenhouse gas emitted to date, the entity will be able to make a reliable estimate of the required amounts (also within a range of possible outcome).

(ii) Based on the above, the IASB staff conclude that if the statement creates a constructive obligation (refer to question 1):

- The entity does not recognise a provision when it makes the statement. At that time, the constructive obligation is not a present obligation as a result of a past event.
- As the entity emits greenhouse gases in 20X9 and thereafter, it will incur a present obligation for the expenditure required to offset its past emissions. If it has not already bought the carbon credits needed to offset its past emissions, and assuming that a reliable estimate can be made of the amount of the obligation, the entity recognises a provision for the cost of buying and retiring those carbon credits.

Question 3 - if a provision is recognised, is the expenditure required to settle it recognised as an asset or as an expense when the provision is recognised?

13 The IASB staff's view was that when an entity recognises a provision, it recognises the expenditure required to settle that provision as an asset, rather than as an expense, only if that expenditure gives rise to—or forms part of the cost of—an item that qualifies for recognition as an asset in accordance with an IFRS Accounting Standard (e.g., the expenditure required to fulfil an asset decommissioning provision could be capitalise in accordance with IAS 16 if all the recognition criteria are satisfied).

14 Based on the above the IASB staff concluded that the principles and requirements in IAS 37 provide an adequate basis for an entity to determine how to apply that Standard to climate-related commitments. Consequently, the IASB staff recommended that the Committee not add a standard-setting project to the work plan and publish a tentative agenda decision that outlines how an entity applies IAS 37 to climate-related commitments.

15 Furthermore, beyond the scope of this submission, the IASB staff analysed the accounting consequences to the amounts at which other assets and liabilities are measure and arising from the actions the entity plans to take to fulfil its commitment (e.g., reassessing the carrying amount of an asset in accordance with IAS 36, reassess the useful life of an asset in accordance with IAS 16, reassess whether an existing contract becomes an onerous contract, provide additional disclosure about major estimates and uncertainties under IAS 1, IAS 36 and IAS 37).

### *Disclosure of Revenues and Expenses for Reportable Segments*

#### *Issue and background*

16 The IFRIC received a request about how an entity applies the requirements in paragraph 23 of IFRS 8 Operating Segments to disclose for each reportable segment specified amounts related to segment profit or loss.

17 The request asked the IFRIC:

(a) is an entity required to disclose the specified amounts 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)?

(b) is an entity required to disclose the specified amounts in paragraph 23(f) of IFRS 8 for each reportable segment if the entity presents or discloses those specified amounts applying a requirement in IFRS Accounting Standards other than paragraph 97 of IAS 1 Presentation of Financial Statements?

(c) How does an entity determine 'material items' in paragraph 23(f) of IFRS 8? In particular:

(i) are 'material items' only those that are material on a qualitative basis?

(ii) do 'material items' include amounts that are an aggregation of individually quantitatively immaterial items?

(iii) is the materiality assessment performed at an income statement level (from an overall reporting entity perspective) or at a segment level?

18 The submitter did not provide fact patterns on which the questions are based. The submission asked about the principles underlying the requirements, rather than their application in a particular situation.

19 The submitter noted that there is diversity in their jurisdiction as to what the words in the IFRS Standards mean and their application thereof.

#### *IASB Staff analysis and recommendations*

20 To help address the issue of diversity the IASB staff developed the following fact patterns:

(a) **Fact pattern 1**: An entity does not disclose the specified amounts in paragraph 23(a)–(i) of IFRS 8 for each reportable segment. Those specified amounts are included in the measure of segment profit or loss reviewed by the CODM but are not considered by the entity to be reviewed separately by management (or by the CODM).

(b) **Fact pattern 2**: An entity does not disclose the specified amounts in paragraph 23(f) of IFRS 8 for each reportable segment because the entity presents or discloses those specified amounts in its financial statements applying a requirement in IFRS Accounting Standards other than paragraph 97 of IAS 1.

(c) **Fact pattern 3**: An entity applies 'material items' in paragraph 23(f) of IFRS 8 as:

(i) only those items that are material on a qualitative basis, such as unusual items (fact pattern 3(a)).

(ii) not including items or amounts that are an aggregation of individually quantitatively immaterial items (fact pattern 3(b)).

(iii) only those items that are material at a segment level (fact pattern 3(c))

21 The IASB sent an information request to IFASS members, securities regulators and large accounting firms. They received 16 responses - seven from large accounting firms, seven from national standard-setters, and two from organisations representing groups of securities regulators.

22 The IASB staff analysed the responses in two sections:

(a) Disclosure requirements under paragraph 23 of IFRS 8 for each reportable segment; and

(b) Meaning of material items of income and expense applying paragraph 23(f) of IFRS 8.

Disclosure requirements under paragraph 23 of IFRS 8

23 Paragraph 23 of IFRS 8 requires an entity to report a measure of profit or loss for each reportable segment and to disclose specified amounts for each reportable segment. Paragraph 23 sets out specified amounts that an entity is required to disclose for each reportable segment if those specified amounts are:

(a) included in the measure of segment profit or loss reviewed by the CODM; or

(b) otherwise regularly provided to the CODM, even if not included in that measure of segment profit or loss.

24 Many respondents, particularly national standard-setters and accounting firms, provided their view of how entities should apply paragraph 23. These respondents say that, in their view, if the specified amounts in paragraph 23(a)–(i) of IFRS 8 are included in a measure of segment profit or loss reviewed by the CODM or are otherwise 'regularly provided' to the CODM, even if not included in that measure of segment profit or loss, those specified

amounts are required to be disclosed for each reportable segment. Some of these respondents say, therefore, paragraph 23 of IFRS 8 requires disclosure of specified amounts included in a measure of segment profit or loss even if those amounts are not 'reviewed separately' by entity management or the CODM.

IASB staff conclusion and recommendations

25 Based on the responses received, and the general lack of diversity, the IASB staff concluded that, in applying paragraph 23 of IFRS 8, an entity discloses specified amounts for each reportable segment if those specified amounts are either

(a) included in the measure of segment profit or loss reviewed by the CODM, or

(b) otherwise regularly provided to the CODM.

26 In either of those circumstances, an entity discloses specified amounts for each reportable segment even if those specified amounts are not 'separately reviewed' by the CODM. Therefore, the staff recommended that there was no need for further guidance on this issue.

Material items

27 Fact pattern 1 -. Many respondents said that 'material' in the context of paragraph 23(f) of IFRS 8 is assessed based on both qualitative and quantitative factors.

28 Fact pattern 2 - Most respondents say either that fact pattern 2 is not common or they could not determine whether it is common. One accounting firm says fact pattern 2 is common and has a material effect and they observe diversity. A few other respondents, particularly securities regulators, say they observe diversity related to fact pattern 2.

29 Fact pattern 3 - Most respondents say either that fact pattern 3(a) is not common or they could not determine whether it is common. Most respondents say either that fact patterns 3(b) and 3(c) are not common or they could not determine whether those fact patterns are common.

30 Most respondents did not share observations about whether 'material items' in paragraph 23(f) of IFRS 8 include amounts that are an aggregation of individually quantitatively immaterial items. A few respondents to the information request refer to US GAAP requirements for segment reporting and say that those requirements affect their interpretation of paragraph 23(f) of IFRS 8.

IASB staff conclusion and recommendation

31 In view of the IASB staff, determining whether an item represents material information requires judgement, and the IFRIC would be unable to determine whether any particular item is material.

32 The IASB staff noted that paragraph 7 of IAS 1 states that 'materiality depends on the nature or magnitude of information, or both'. In our view, therefore, whether an 'item of income and expense' represents material information is assessed based on both qualitative and quantitative factors.

33 The IASB staff therefore conclude that, in applying paragraph 23(f) of IFRS 8, an entity **considers both qualitative and quantitative factors**, representing the nature or magnitude of information, or both, in assessing the materiality of an item of income and expense.

34 The IASB staff also concluded that applying paragraph 23(f) of IFRS 8, an entity cannot omit material items on the basis that those items are presented or disclosed applying a requirement other than paragraph 97 of IAS 1. The IASB staff are of the view that paragraph 97 of IAS 1 sets out the overarching principle for when separate disclosure of an 'item of income or expense' is required in the financial statements, and paragraphs 98–105 of IAS 1 include additional information and requirements about how an entity applies paragraph 97.

35 On this basis, and on the basis that there is no significant diversity in practice, the IASB staff recommended that the IFRIC could provide some direction on what is material but not change existing requirements or add further guidance.

*EFRAG Secretariat comment*

36 Following the 2021 agenda consultation, segment reporting is included as a reserve list project for EFRAG's proactive workplan. This stems from the challenges with existing requirements identified by stakeholders including those articulated in EFRAG's response to the 2020 Discussion Paper on Business Combinations, Goodwill and Impairment (i.e., in how the allocation of goodwill to CGUs is done[3]).

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[3] In its comment letter on the IASB's DP/2020/1 Business Combinations - Disclosures, Goodwill and Impairment, EFRAG noted that opportunistic reporting of goodwill impairments losses can be done by means of adopting a certain approach when allocating goodwill to CGUs, either by allocating goodwill to a higher level (where managerial monitoring is possible at a lower level) and/or by reallocating goodwill (for example, by means of changing segment reporting). EFRAG noted that, in some circumstances, operating segments can be defined by entities independent from the structure of cash inflows and as companies have the possibility to claim that they are not "monitoring" goodwill, this could lead to the situation whereby the allocation of goodwill is not connected to the reasons it was recognised as of the acquisition date. In such circumstances, events that trigger impairment may become more difficult to promptly be identified.

## Finalisation of agenda decision

*Merger between a Parent and Its Subsidiary in Separate Financial Statements*

*Issue and background*

37 The IFRS IC received a submission about how an entity that prepares separate financial statements applying paragraphs 9-10 of IAS 27 Separate Financial Statements accounts for a merger with its subsidiary in its separate financial statements.

38 In the submitted fact pattern:

(a) a parent entity prepares separate financial statements applying IAS 27 and recognises an investment in a subsidiary applying paragraph 10 of IAS 27;

(b) the subsidiary contains a business (as defined by IFRS 3 Business Combinations); and

(c) the parent entity merges with the subsidiary resulting in the subsidiary's business becoming part of the parent entity.

39 The submitter asked whether, in the context of the parent entity's separate financial statements, the merger transaction:

(a) constitutes a business combination and consequently, whether an entity should apply the acquisition method (and related requirements) in IFRS 3; or

(b) should not be accounted for as a business combination. Applying this view, the parent entity—in its separate financial statements—recognises the subsidiary's assets and liabilities at their previous carrying amounts (carrying amount method).

*IFRS IC tentative decision (June 2023)*

40 Evidence gathered through the IASB information request and other additional research indicated little, if any, diversity in accounting for the merger transaction. In accounting for the merger transaction, in their separate financial statements, parent entities generally do not apply the acquisition method.

41 Consequently, the Committee concluded that the matter described in the submission does not have widespread effect. Consequently, the Committee tentatively decided not to add a standard-setting project to the work plan and published a tentative agenda decision.

*Comment letter analysis*

42 The IASB staff received 14 comment letters by the comment letter deadline (14 August 2023). In particular:

(a) Seven respondents (some national standard setters, an auditor and one preparer) agreed with the Committee's decision not to add the matter to its standard-setting agenda for the reasons outlined in the tentative agenda decision.

(b) Some respondents said the merger transaction is prevalent but most of these respondents agreed with the Committee's observation about entities not generally applying the acquisition method to account for the merger transaction. However:

(c) Two of these respondents (two national standard setters, of which one outside EU) nonetheless suggest updating the agenda decision to explain how an entity applies IFRS Accounting Standards when considering the matter described in the submission. Otherwise, it may accidently create divergence in practice, because it could lead to believe that both methods may be applied in accordance with IFRS Standards;

(d) One respondent (a non-EU national standard setter) highlighted there is an urgent need of guidance on accounting for such transactions.

(e) One respondent (an accounting professional) disagreed with the Committee's observations and conclusions. The respondent said the merger transaction is prevalent in their jurisdiction (India) and said an entity should apply the relevant requirements in IFRS Accounting Standards (including those in IFRS 3) when accounting for intra-group transactions in separate financial statements.

(f) One respondent (a preparer) suggests amending the agenda decision not to mention prevalent practice because it could be seen as explanatory material that has the potential for confusion;

(g) A number of respondents said there is diversity in how entities apply a carrying amount method. Therefore, some of them suggested clarifying how entities apply (or should apply) a carrying amount method and/or referring the matter to the IASB; others suggested the IASB consider this matter as part of the IASB's Business Combinations under Common Control (BCUCC) project.

*IASB Staff analysis and recommendations*

43 Although the majority of respondents did not disagree with the previous Committee's conclusion and recommendation, the IASB staff analysed the additional feedback received as follows:

(a) <u>Updating the agenda decision to explain how an entity applies IFRS Accounting Standards when considering the matter described in the submission</u> - Feedback on the tentative agenda decision supports the Committee's tentative conclusion that the matter does not have widespread effect (i.e., Such transactions could be common but diversity in accounting for such transactions is limited). Because the matter does not meet the ‘widespread and material’ criterion set out in paragraph 5.16(a) of the Due Process Handbook, **the IASB staff recommended the Committee should not include explanatory material in its agenda decision**.

(b) Diversity in practice in applying the carrying amount method - The submission asked whether an entity applies the acquisition method to the merger transaction and the Committee observed no existing widespread diversity in practice. Therefore, addressing how entities should apply the carrying amount method to the merger transaction would go beyond the question asked; in addition, the staff recommended **updating the wording in the agenda decision to avoid implying that the Committee observed no diversity in how entities apply a carrying amount method.**

(c) Not to mention the prevalent practice – The IASB staff concluded that **this statement would support the Committee’s conclusions about the matter not having widespread effect and it would be useful** because it would allow a reader to understand how the Committee arrived at its decision not to address the matter.

(d) Whether to specify the requirements in IFRS 3 that apply to such transactions – The IASB staff noted that it might not be clear as to whether the statement refers to only the acquisition method (and related requirements) in IFRS 3 or also to other requirements in IFRS 3 (for example, paragraphs in IFRS 3 that set out the scope of IFRS 3). Therefore, the IASB staff suggested **some wording changes to improve the clarity of the agenda decision**.

44 Based on the above, the IASB staff recommends finalising the agenda decision with changes to the wording mainly limited to the “Findings” section of the tentative agenda decision as follows:

“Findings

45 Evidence gathered by the Committee [~~to date~~] indicates little, if any, diversity in ~~accounting~~ determining whether to apply the acquisition method (and related requirements) in IFRS 3 ~~for~~ to the merger transaction described in the request. In accounting for the merger transaction described in the request in their separate financial statements, parent entities generally do not apply the acquisition method (and related requirements) in IFRS 3 ~~that apply to the accounting for a business combination~~.

Conclusion

46 Based on its findings, the Committee concluded that the matter described in the request does not have widespread effect. Consequently, the Committee [decided] not to add a standard-setting project to the work plan."

## Input to IASB

*Climate-related and Other Uncertainties in the Financial Statements*

*Issue and background*

47 At its September 2023 meeting the IASB discussed potential actions it could take to help address concerns about reporting the effects of climate-related risks in financial statements.

48 Among the others, the IASB decided to consult the IFRS IC on how entities apply the requirements in IAS 36 Impairment of Assets in measuring value in use when an asset is subject to highly variable future cash flows over an extended time horizon, which could result from the effects of climate-related risks.

49 In particular, questions could arise about how to apply current requirements in IAS 36 when the high variability of such cash-flows may:

(a) extend beyond the five-year period specified in paragraph 33(b) of IAS 36; and

(b) affect the extrapolation of cash flow projections based on forecast/budget as required by paragraph 36 of IAS 36.

50 The IASB staff analysis highlighted concerns about potential:

(a) lack of compliance due to misunderstanding of the requirements— entities may not fully understand some requirements leading to climate-related risks not adequately factorised over extended time horizons into impairment calculations;

(b) limitations of the requirements –reliable and demonstrable cash flow projections in estimating the recoverable amount of an asset (as required in paragraph 35 of IAS 36) could be interpretated by some entities as a prohibition from forecasting future cash flow for a longer period.

(c) insufficiently clear requirements in IFRS Accounting Standards – when measuring the value in use of an asset using the traditional approach, entities may not properly consider that cash flows used should represent management's best estimate of the range of economic conditions that will exist over the remaining useful life rather than a single likely minimum or maximum possible amount.

51 The IASB staff will seek input from the Committee as follows:

(a) how do entities reflect the potential for high variability in future cash flows over an extended time horizon when calculating the value in use of an asset?

(b) is there diversity in how entities understand and apply the requirements in IAS 36 in reflecting such variability in value in use calculations?

*Provisions—Targeted Improvements*

*Issue and background*

52 The IASB has included a project on targeted improvements on its agenda. In this project, the IASB is developing proposals to make three targeted improvements to IAS 37:

(a) to amend the liability definition and the requirements and guidance supporting the present obligation recognition criterion, applying concepts added to the Conceptual Framework for Financial Reporting in 2018;

(b) to specify more precisely the rate an entity uses to discount a long-term provision to its present value; and

(c) to specify which costs an entity includes in measuring an obligation to provide goods or services.

53 The paper for the November 2023 meeting of the IFRS Interpretations Committee deals with the first bullet point. The paper asks for:

(a) Overall reactions to the possible amendments to IAS 37 following from amendments suggested by the IASB staff;

(b) Specific comments on any aspects of the possible amendments;

(c) Whether IAS 37 should specify when an entity has a present obligation for costs that become payable if a measure of its activity exceeds a specified threshold; and

(d) Views on when a present obligation arises.

*Power Purchase Agreements*

*Issue and background*

54 In July 2023, the IASB added a project to its work plan to research whether narrow-scope amendments to IFRS 9 Financial Instruments could be made to better reflect how financial statements are affected by both physical and virtual Power Purchase Agreements (PPAs).

55 The use of PPAs is increasing due to the green energy transition and affects many industries, geographies and entities of different sizes.

56 According to the IASB staff, the primary objective for consumers to enter into PPAs is to secure their supply of renewable power and reduce their greenhouse gas emissions. A secondary factor is to fix the price at which power is purchased. if a producer does not produce sufficient power when needed due to the weather conditions, the consumer need to purchase additional power in the spot market. Conversely, if a consumer receives more power than needed, the consumer needs to sell the excess power in the market. Therefore, there could be a mismatch between the time when power is delivered vs. when it is needed.

57 PPAs are often net settled in cash or considered to be net settled in cash (i.e., they meet the requirements included in paragraph 2.6 of IFRS 9). In addition, due to the mismatch between availability of power and the need of power, PPAs are often considered to fail the own-use exemption, resulting in entities accounting for these contracts in accordance with IFRS 9. Stakeholders consider that the underlying characteristics of this non-financial item (i.e., power) result in PPAs not meeting the own-use exemption but the intentions of entering into PPAs are often to satisfy an entity's need of energy from renewable sources. Hence, in their view, PPAs should often be accounted for as executory contracts.

*Characteristics of the underlying non-financial item*

58 The IASB staff describes the characteristics of the underlying non-financial item that could be used to define the scope of narrow-scope standard-setting:

(a) neither the seller nor the purchaser controls the timing and volumes of power produced;

(b) the entity's usage or sales expectations can be reliably predicted over a period of time that is shorter than contractual period but not at the discrete points when the energy is delivered; and

(c) if electricity is produced and purchaser is unable to use the volume supplied, it is forced to sell unused volumes into market (no control over timing or price of sales, which could be unfavourable).

59 In the IASB Staff's view, the physical or economic feasibility of the storage of renewable energy is not a viable characteristic because of possible future developments. The challenges with storage is, in effect, reflected within paragraph 58(b) above.

*Approaches to address the issue suggested by the IASB staff*

60 The IASB staff proposes three approaches to address the issue if standard-setting was required:

(a) Amend the 'own use' requirements in IFRS 9. Include guidance on how to assess 'own-use' requirements in paragraph 2.4 of IFRS 9 for non-financial items with the characteristics described above;

(b) Amend hedge accounting requirements in IFRS 9. Include guidance on how to assesses the requirement for a forecast transaction to be 'highly probable' for non-financial items with the characteristics described above that will enable virtual PPA to be designated as hedging instrument; and

(c) Exception for PPAs. An exception for PPAs could be created to exclude them from either the definition of derivatives and/or the scope of IFRS 9 entirely.

61 The IASB staff will seek input from the IFRS Interpretations Committee on:

(a) whether the characteristics set out above are appropriate and adequate to restrict the scope of a potential standard-setting project and/or whether other characteristics should be considered; and

(b) which of the approaches indicated above would achieve the most appropriate outcome while limiting the risk of unintended consequences and if there are other approaches that should be considered.

## End of consultation period

*Payments Contingent on Continued Employment during Handover Periods*

*Issue and background*

62 The IFRS IC received a submission about how an entity accounts for payments to the sellers of an acquired business when those payments are contingent on the sellers' continued employment during a post-acquisition handover period. These arrangements are automatically forfeited if employment terminates.

63 In most cases, by applying the requirements of paragraph B55(a) of IFRS 3 Business Combinations on the basis of the IFRIC January 2013 Agenda Decision, these arrangements are accounted as compensation for post-combination services rather than additional consideration for an acquisition. The submission describes that the application of the requirements has a material effect on the entity's financial statements (e.g., operating income).

64 The submission includes the main reasons on why the accounting outcome does not reflect the economic substance of the transaction:

(a) The sellers' duty is only related to providing hand-over services;

(b) The sellers are compensated at a level that is comparable to other management executives;

(c) There are two components of the contingent payment: the earnout payment and the post-acquisition compensation.

65 The IASB Staff has sent a request for information to IFASS members, securities regulators and large accounting firms. 19 responses were received:

(a) Most respondents said that fact patterns, as described in the submission are common and can be material for affected entities.

(b) All respondents said that entities (generally) apply the accounting described in the January 2013 Agenda Decision.

(c) Some respondents disagreed with the accounting outcome of the January 2013 Agenda Decision, since in their view it does not always reflect the economic substance of the arrangement.

*IASB Staff analysis*

66 Based on the results from the outreach, and the submitter's statement on current practice, the IASB Staff considered that there is no significant diversity in how entities account for the fact pattern included in the submission. Therefore, they do not consider that the matter satisfies the criteria for adding a standard-setting project to the workplan.

*IASB Staff recommendations*

67 The IASB Staff recommended the IFRS IC not to add a standard-setting project to the workplan but instead publish a tentative agenda decision explaining the reasons for not adding a standard-setting project.

*IFRS IC tentative decision (September 2023)*

68 Evidence gathered by the IFRS IC [to date] does not indicate significant diversity in the accounting for payments contingent upon continued employment in fact patterns such as that described in the request. In these fact patterns, entities apply the accounting described in the agenda decision Contingent payments to shareholders and continuing employment (published in January 2013) and account for the payments as compensation for post-combination services rather than as additional consideration for the acquisition, unless the service condition is not substantive.

69 Based on its findings, the IFRS IC concluded that the matter described in the request does not have widespread effect. Consequently, the IFRS IC [decided] not to add a standard-setting project to the work plan.

70 The consultation period ended on 20 November 2023.

**Questions for EFRAG FR TEG-CFSS**

71 Does EFRAG FR TEG-CFSS have any comments on the topics presented? Does EFRAG FR TEG-CFSS agree with the IASB Staff outreach result, analysis and recommendations/ IFRS IC's tentative decisions related to the topics presented?

72 Does EFRAG FR TEG-CFSS wish to further discuss any of the presented issues at a future meeting?

## Next steps

73 The EFRAG Secretariat will continue to monitor the IFRS IC's discussions.