

Issue

Recognition of Intangible Asset resulting from Climate-related expenditure (IAS 38)

The request asks whether during its 2024 annual reporting period the entity's investments in carbon credits and expenditures for research activities and development activities, resulting in intellectual capital from innovation programs as described in the fact pattern, meet the requirements in IAS 38 to be recognised as intangible assets.

Comments

Companies around the world are acting in a concerted manner to reduce their carbon emissions.

A. Carbon Credit

A carbon credit represents one tonne of carbon dioxide (or equivalent greenhouse gases) reduced, avoided or removed from the atmosphere. An entity can obtain carbon credits and “retire” them to claim the underlying emissions reduction against its own emissions. Carbon Credits are the certificates awarded to the countries taking active participation in reducing the emissions that cause global warming. Even though the terminology can vary, but these carbon credits typically represent a reduction in or removal of emissions (e.g. CO₂ or greenhouse gas)

B. CDM

Clean Development Mechanism also offers an effective source of economic as well as technological development for developing countries with environmental sustenance

C. The IASB Roadmap

The IASB has already introduced IFRS S1 and S2 to address the need for Sustainability & Climate related Disclosures in Financial statements by reporting entities.

D. IFRS S2 Climate-related Disclosures

The objective of IFRS S2 is to require an entity to disclose information about its climate-related risks and opportunities that is useful to users of general purpose financial reports in making decisions relating to providing resources to the entity.

IFRS S2 requires an entity to disclose information about climate-related risks and opportunities that could reasonably be expected to affect the entity's cash flows, its access to finance or cost of capital over the short, medium or long term (collectively referred to as 'climate-related risks and opportunities that could reasonably be expected

to affect the entity's prospects'). IFRS S2 sets out the requirements for disclosing information about an entity's climate-related risks and opportunities.

E. Analysis of IAS 38

IAS 38 sets out the criteria for recognising and measuring intangible assets and requires disclosures about them. An intangible asset is an identifiable non-monetary asset without physical substance. Such an asset is identifiable when it is separable, or when it arises from contractual or other legal rights. Separable assets can be sold, transferred, licensed, etc

Expenditure for an intangible item is recognised as an expense, unless the item meets the definition of an intangible asset, and:

- it is probable that there will be future economic benefits from the asset; and
- the cost of the asset can be reliably measured.

F. Will Carbon credits & Climate-related expenditure meet the definition of an asset?

An asset is defined as a present economic resource controlled by the entity as a result of past events. It is an economic resource and is a right that has the potential to produce economic benefits

G. Carbon accounting

For Carbon Emission Reduction (CER) to be an asset, it should be controlled by the generating entity. Since CER arise as a result of past events, and from which future economic benefits are expected to flow to the generating entity

Carbon Emission Reduction (CER) is an 'INTANGIBLE ASSET'. It is a non-monetary asset without a physical form and expected to generate future economic benefits. For reducing emissions, an entity may carry out some research and development which may result in the creation of an intangible asset and thus should apply IAS 38. Such items qualify for recognition as assets because they enable an enterprise to derive future economic benefits

When assessing whether a carbon credit held for use is an asset, a company should consider the nature of the economic benefits and when they are consumed. The company's ability to use the carbon credit to offset its own emissions generally represents economic benefits flowing to the company from the credit. If economic benefits arise from the ability to offset, then the company may have an intangible asset.

This is because it has the power or the right to obtain the future economic benefits and restrict others' access to those benefits.

Determining when the economic benefits from the carbon credits are consumed may require management to exercise judgement. Management needs to consider its assessment of the economic benefits flowing from the credit.

Opinion

Hence the querist may consider accounting for Research & carbon credit related expenditure as an intangible asset under IAS 38