Summary to Exposure Draft – Guidance Note on Accounting for Self-generated Certified Emission Reductions (CERs)

INTRODUCTION

- CERs is just another move to prevent the country from global warming. United Nations Framework Convention on Climate Change (UNFCCC) let Kyoto protocol to came into force to prevent Green House Gases (GHG) Emissions.
- One unit of CER is equal to one metric tonne of carbon dioxide emission saved.
- 41 developed countries (i.e. Annexure – 1 countries) are bound to reduce their GHG emission as specified in protocol.
- Developing or least-developed countries are not bound by any limit on GHG emissions.
- CDM project must provide reductions in emissions that are additional to that would occur in the absence of the project.
- These 41 countries can take help of three mechanisms to meet there CERs targets.
  - **Joint implementation –** An entity in a DEVELOPED country can set up a project in another DEVELOPED country where cost of setup is relatively less.
  - **Clean Development Mechanism –** The DEVELOPED country can take the GHG reduction project in DEVELOPING country to save cost and the CERs generated by that developing country would be given to DEVELOPED country.
  - **International Emission Trading** - Carbon credits can be brought and sold in the international market, called Carbon Trading.

OBJECTIVE & SCOPE

- Recognition, measurement and disclosures of CERs generated under Clean Development Mechanism (CDM).

REGISTRATION AND SUBSEQUENT VERFICATION OF CDM PROJECT

Registration with CDM executive board of UNFCCC and also from National CDM Authority.

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Validation by Designation Operational Entity (DOE) by hosting it on the UNFCCC website and reviewing the public comment received.

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Registration of the project by CDM executive board.

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Other DOE undertakes the subsequent verification of the CDM

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After verification, written assurance is given by UNFCCC abount the CERs achived which can be sold.

ACCOUNTING TREATMENT AS PER GUIDANCE NOTE:

- CER meets the definition of asset (as stated in 'Framework for Preparation and Presentation of Financial Statements' issued by ICAI) when communication of credit of CERs is received by the generating entity.

- After generation but before receipt of communication it can be treated as Contingent Asset as is meets the definition stated in AS – 29 *Provisions, Contingent Liabilities and Contingent Assets*.

- CER regarded as inventory:
  - As it partially meets the criteria for Intangible Assets in AS – 29 and those intangible assets which are specifically dealt with in another AS should be accounted under that AS, hence AS – 2, *Valuation of Inventories* applies.

- Recognition of an asset in Financial Statements is done when there is:
  - Probable future economic benefits :- as the market of CER is relatively new future economic benefits may not always be assured.
  - Cost or value can be measured reliably. :- Because of set criteria of recognition the cost can be easily measured

- CERs are measured at cost or NRV whichever is less i.e. as per AS – 2.

- Cost to be taken as defined in Para 6 of AS – 2, Examples :
  - Cost for certification of CERs.
  - Payment for administration charges of UNFCCC.
  - Fees to consultant for services rendered.

- There are some costs which cannot be considered as the costs of bringing the CERs into existence and therefore that should not be included in the cost of CER, they are to be treated as per AS – 26, *Intangible Assets* as they give rise to some Intangible Asset, Examples:
  - Research costs arising from exploring alternative ways to reduce emissions.
  - Costs incurred in developing the selected alternative as a process/device to reduce emissions.

- Net Realisable Value is calculated as per Para 22 of AS – 2 which states that NRV should be based on most reliable evidence available at the time of estimate.

- The entity may use some of the Tangible Assets for production of CERs, these should be accounted for as per AS – 10 (Revised) *Property Plant and Equipment*, which states that even if tangible assets are acquired for some reasons which are not directly increasing the future economic benefits (FEB) of the entity but will help in deriving FEB in excess of what could be derived had those items not been acquired.

- The depreciation on these Tangible Assets cannot be added in valuation of the principal products and also cannot be included in the value of CERs as the depreciation is incurred before the CERs come into existence. But should be expensed in the statement of profit and loss.

- The last date for comments is June 15, 2009.

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