Staff Paper

Project	**Emissions Trading Schemes**
Topic	**Cover memo**

Purpose

1. The staff have prepared the following 3 papers for the joint meeting to analyse the initial and subsequent measurement of allowances and liabilities in a cap and trade scheme.
   - IASB AP 5A/FASB AP 7A: **Initial and subsequent measurement of allowances (assets) and the liability for the allocation (cap and trade scheme)**
   - IASB AP 5B/FASB AP 7B: **Interaction of emissions with the liability for the allocation and recognition and measurement of a liability for excess emissions**
   - IASB AP 5C/FASB AP 7C: **Quantitative examples**

Issues to be discussed at future board meetings

2. The staff plan to discuss the following issues[1] at future joint board meetings:

Date	Topic
November 2010	i) Presenting the assets and liabilities net (netting[2])

[1] These issues were described in the September 2010 IASB Agenda Paper 10C/FASB Agenda Paper 6C.

	ii) Right to receive a future allocation iii) Baseline and credit schemes
December 2010	iv) Presentation and disclosure issues (excluding netting)
January 2011	v) Other issues

Terminology

3. A number of terms used throughout the papers are specific to emission trading schemes. The September 2010 IASB Agenda Paper 10/FASB Agenda Paper 6, included the staff's working definition of terms. For ease of reference, these terms are reproduced as Appendix A to this paper. A few terms have been added (the 'liability for the allocation' and the 'liability for excess emissions') that are relevant for the papers listed above. As explained in September 2010 IASB AP 10/FASB AP 6, Appendix A is not meant to provide the specific drafting for those definitions, nor is it meant to provide a comprehensive list of definitions that may be required.

[2] We have used this term to distinguish this concept from the mechanics of emissions trading schemes. This concept is the same as described as offsetting in paragraph 42 of IAS 32 *Financial Instruments: Presentation* and Topic 210-20 *Offsetting*.

Appendix A
Terms used throughout the agenda papers

A1. A number of terms used throughout the agenda papers are specific to emission trading schemes. Commonly used terms and staff's working definitions of these terms are as follows:

(a)	allocate	the granting or providing of allowances to entities (who are scheme participants) from the scheme administrator. These allowances are provided to entities for no monetary consideration.
(b)	allowances	a certificate used in a cap and trade scheme to offset a unit of emissions. Allowances are freely tradable in markets that are generally well established. Allowances can be allocated to the entity by the scheme administrator (for no monetary consideration) or can be purchased (in the market or through auction).
(c)	baseline	an individual upper limit of total units of emissions assigned to an emitting source as part of a baseline and credit scheme.
(d)	baseline and credit scheme	a type of emissions trading scheme that establishes an overall limit on total units of emissions. The overall limit is implemented by assigning individual limits on emissions to specific sources of emissions (eg a factory) in the form of baselines. At the end of the compliance period, the source is issued credits for the difference between actual emissions and its baseline (if it emits below the baseline). (One credit is issued for each unit of emissions.) For every unit of emissions above its baseline, the source must provide the scheme administrator with credits.
(e)	cap and trade scheme	a type of emissions trading scheme that establishes an overall cap (ie a limit) on total units of emissions for particular pollutants for all entities combined. The overall cap therefore establishes the total number of allowances in circulation. The allowances create a trading mechanism that is used to carve up the overall limit between entities. Entities must return an allowance to the scheme administrator for every unit of emissions.

(f)	clawback	a rule in a cap and trade scheme that requires an entity to return previously allocated allowances upon closure of the facilities for which the allocation was provided.
(g)	credit	a certificate used in a baseline and credit scheme to offset units of emissions (similar to an allowance). Credits are issued to emitting sources for the differential between a baseline and actual emissions when the source emits below the assigned baseline. The issued credits are freely tradable in markets.
(h)	commitment period	an administrative period over which the scheme administrator will apply the defined total cap or limit on units of emissions. For administrative purposes, the commitment period will often comprise a number of compliance periods. The commitment period is defined differently by each scheme, but may be tied to a specific period defined, for example, by the Kyoto Protocol.
(i)	compliance period	a defined time period (often an annual period) for reporting emissions. At the end of a compliance period, entities are required to report their total units of emissions and 'settle' any obligations under the scheme by surrendering allowances or credits to the scheme administrator.
(j)	liability for the allocation	an obligation to return the allowances if the entity does not reduce emissions below the level of the allocated allowances. This liability is incurred when an entity is allocated allowances from a scheme administrator for no monetary consideration.
(k)	liability for excess emissions	a liability to provide allowances to the scheme administrator for emissions in excess of the liability for the allocation.
(l)	statutory scheme	an emissions trading scheme imposed by the law. Participation in the scheme is mandatory if an entity wishes to conduct the business to which the scheme applies.

(m)	voluntary scheme	an emissions trading scheme that is not a statutory scheme. An entity agrees to the terms of the scheme upon entering the scheme. Once an entity has joined a scheme, the entity`s participation is generally governed by contract and may no longer be `voluntary`.