Accounting for electricity procurement agreements: Applying the own-use exemption

The IASB issued amendments to IFRS 7 and IFRS 9 for contracts that reference nature-dependent electricity. This article provides a brief overview of the issues that resulted in the amendments and the main elements of the amendments.

Arrangements for electricity procurement vary in how they match electricity production from natural sources with usage. The IASB identified that applying the own-use exemption in IFRS 9 to such arrangements posed certain challenges. This prompted narrow-scope amendments to be published in December 2024. This article briefly considers these amendments.

The own-use exemption

IFRS 9 *Financial Instruments* must be applied to contracts to buy or sell non-financial items (commodities) that can be settled on a net basis as if they were financial instruments. An exception to this rule exists for contracts entered into and held for purposes of taking receipt or delivery of the commodity for the entity's expected purchase, sale or usage requirements (i.e. own-use).

Some commercial arrangements to procure electricity generated in a manner that is nature-dependent, for example, solar or wind-generated electricity, have elements of own-use and net settlement, in particular, relating to electricity that the purchaser does not use in its operations. This would be the case if, for example, an entity procures to purchase all or part of the production of an electricity-generating source but does not use all the electricity purchased because it cannot store it. The unused electricity is then sold. This raised questions about how an entity should assess whether this contract is for own-use or not.

Arrangements structured as contracts for difference between the spot and agreed fixed prices (virtual power procurement arrangements) raised similar economic questions.

Amendments for nature-dependent electricity procurement contracts

The IASB published amendments to IFRS 7 and IFRS 9 titled *'Contracts Referencing Nature-dependent Electricity'* in December 2024. Entities must apply the amendments for financial years beginning on or after 1 January 2026.

The amendments only apply to contracts referencing nature-dependent electricity. These contracts are defined as:

> "contracts that expose an entity to variability in the underlying amount of electricity because the source of electricity generation depends on uncontrollable natural conditions (for example, the weather)."

Financial instruments referencing such electricity are also considered such contracts.

The main aspects of the amendments are:

- It introduces detailed application guidance to assess whether contracts referencing nature-dependent electricity are entered into for own use. This involves considering whether an entity has been and expects to be a net purchaser of electricity for the contract period.
- It relaxes the hedge accounting requirements to allow entities to designate a variable nominal amount of forecast electricity transactions as the hedged item if a contract referencing nature-dependent electricity is designated as the hedging instrument.
- It introduces additional disclosure about contracts affected by the above amendments.

The first step in considering the practical effect of the amendments is to assess existing electricity procurement arrangements critically.

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