



FASB issues ASU

Environmental credits and credit obligations

May 20, 2026



FASB issues guidance on accounting for environmental credits and obligations.

Source and applicability

- ASU 2026-02, [Environmental Credits and Environmental Credit Obligations](#)
- All entities

Fast facts, impacts, actions

ASU 2026-02 introduces Topic 818, which sets out accounting rules for environmental credits and environmental credit obligations (ECOs). The ASU aims to address diversity in practice and explains how to recognize, measure, present and disclose these items in financial statements.

- **Scope:** Topic 818 applies only to environmental credits and ECOs that meet the Topic 818 definitions described below.
- **Environmental credits:** Environmental credits are recognized as assets if the entity intends to use them to settle ECOs or transfer them in an exchange transaction or a nonreciprocal transfer. Environmental credits used for compliance (i.e. to settle an ECO) are recorded at cost and not remeasured. Noncompliance environmental credits are also recognized at cost but assessed for impairment at each reporting date. Costs for environmental credits that do not meet the asset recognition criteria (e.g. credits to be used on a voluntary basis), including nonrefundable deposits for those credits, are expensed as incurred.
- **ECO liabilities:** ECO liabilities reflect the number of credits needed to settle the obligation if the reporting date were the end of the compliance period. The ECO liability is measured as the sum of the carrying amount of available compliance credits (the funded portion) and the fair value of any additional credits required to fulfill the obligation (the unfunded portion).

Effective date and transition

Public business entities must adopt this guidance for annual periods beginning after December 15, 2027; other entities must adopt it for annual periods beginning after December 15, 2028. Early adoption is permitted. In the period of adoption, the entity adjusts its balance sheet to comply with the new requirements and records a cumulative-effect adjustment to beginning retained earnings. Prior periods are not recast.

Background

Emissions trading arrangements are not new, but for entities making net-zero or other emissions commitments, offsets and credits are often a key driver of their strategy. These arrangements were historically established to help entities comply with government or regulatory emissions mandates. Now, a growing number of global programs incentivize entities to produce cleaner products and invest in renewable energy projects.

Entities generally obtain or generate environmental credits through regulators or designees by producing environmentally friendly products or meeting and exceeding emissions standards in their production processes. For instance, automobile manufacturers can earn credits by producing electric vehicles, which they can use to fulfill compliance obligations or trade with other manufacturers. Entities across all sectors can invest in renewable energy projects that generate Renewable Energy Certificates (RECs), which they can sell or use to offset their own emissions.

In the US, federal and state mandatory compliance programs include cap-and-trade type programs such as those created by California’s Low Carbon Fuel Standard (LCFS), and trading programs related to the Clean Water Act (CWA) and Clean Air Act (CAA). These programs often establish markets in which entities can purchase environmental credits to meet their compliance obligations and sell excess credits. However, the expansion of these programs in the US introduces accounting complexity as they become more sophisticated to meet stakeholders’ growing environmental and financial expectations.

Before ASU 2026-02, US GAAP did not explicitly address the accounting for carbon offsets, allowances or credits, resulting in diversity in practice. In practice, some entities analogized to guidance on inventory, intangible assets or even marketing costs to account for environmental credits. Further, there was inconsistency in how ECOs were recognized and measured. The ASU aims to address this diversity by establishing new Topic 818.

Scope of Topic 818

Topic 818 applies to both environmental credits and ECOs. Specifically, its scope applies to credits and obligations that meet the following definitions.

Environmental credit	<p>An enforceable right that is acquired, internally generated, granted by a regulatory agency or designee(s), or received in a nonreciprocal transfer that is not a grant from a regulator, and that meets the following criteria:</p> <ul style="list-style-type: none"> • lacks physical substance and is not a financial asset; • is represented to prevent, control, reduce or remove emissions or other pollution; • is, or previously was, separately transferable in an exchange transaction or is no longer separately transferable but can be used to satisfy an ECO; and • is not an income tax credit.
ECO liability	<p>A regulatory compliance obligation arising from existing or enacted laws, statutes or ordinances represented to prevent, control, reduce or remove emissions or other pollution that may be settled with environmental credits. Obligations in the scope of Subtopic 410-30 are not ECOs.</p>

The ASU also clarifies that environmental credits and ECO liabilities accounted for under Topic 818 are not in the scope of Topic 815 on derivatives and hedging. However, contracts to acquire environmental credits (e.g. forward contracts) do not have an explicit scope exception and would need to be evaluated to determine if they should be accounted for as a derivative.



If a credit does not meet the criteria to be in scope because it is not transferable, the FASB has indicated it expects the cost of the credit to be expensed as incurred. Further, income tax credits are not in the scope of Topic 818; an entity would have to consider whether Topic 740 or other US GAAP applies.

Accounting model: Environmental credits

The ASU introduces an intent-based asset recognition and measurement model for environmental credits. That is, how an entity expects to use or consume an environmental credit determines the appropriate accounting model. To identify the appropriate accounting model, an entity first assesses whether it is *probable*, collectively, that it will use its environmental credits to either settle an ECO liability or transfer them in an exchange transaction or nonreciprocal transfer.


- If the environmental credits meet the probability threshold, they are recognized as assets and measured at cost. Subsequent measurement will differ based on whether they are classified as compliance or noncompliance credits.
- If the probability threshold is not met, the cost of the credits (referred to as *all other credits*) is expensed as incurred.

An entity reassesses the probability each period and a credit that met the initial recognition threshold could be expensed if it no longer meets the asset recognition criteria. However, once costs are expensed, that expense cannot be reversed even if the expensed credit subsequently meets the asset recognition criteria. For subsequent measurement purposes, an entity will also reassess whether a credit should be reclassified from a compliance credit to a noncompliance credit.

The following table summarizes the recognition and measurement criteria.

Compliance credits	Noncompliance credits	All other credits
Recognition		
Recognized as assets if it is probable that they will be used to settle an ECO liability, be transferred in an exchange transaction or used in a nonreciprocal transfer. For example, an asset would be recorded if it is 50% likely it will be used to settle an ECO and 50% likely it would be transferred in an exchange transaction because the collective likelihood of one of those events occurring is probable.		Expense costs as incurred. This includes the costs of a nonrefundable deposit to obtain environmental credits that are not probable of meeting the asset recognition criteria.
Classification		
Environmental credits that are probable of being used to settle an ECO.	Environmental credits that are recognized as assets but are not compliance credits.	
Initial measurement		
Measured at cost. Capitalizable costs related to granted and internally generated credits are limited to transaction costs incurred (e.g. application fees) and could be zero. The guidance in Subtopic 805-50 on asset acquisitions is used to determine the cost of acquired credits unless other US GAAP applies.		


Compliance credits	Noncompliance credits	All other credits
Subsequent measurement		
<ul style="list-style-type: none"> At cost. Not tested for impairment. 	<ul style="list-style-type: none"> At cost unless fair value measurement is elected (see other considerations below). Tested for impairment at each reporting date. An impairment loss occurs when the carrying value of a noncompliance credit exceeds its fair value. 	
These assets are not amortized.		
Derecognition		
Apply Subtopic 610-20 unless in the scope of other guidance such as Topic 606 on revenue from contracts with customers.		



The ASU specifies that an entity may need to follow other Topics such as the asset acquisition guidance in Subtopic 805-50 for initial measurement and Subtopic 610-20 or Topic 606 for derecognition. However, without specific application guidance an entity will need to evaluate the principles of those Topics to determine the appropriate accounting.

Other considerations

Topic 818 provides flexibility on how to apply the guidance to compliance and noncompliance credits by allowing an entity to choose between the specific identification, FIFO or average cost costing methods to track similar environmental credits. In addition, an entity can elect an accounting policy to remeasure a class (e.g. RECs, RINs) of eligible noncompliance credits to fair value at each reporting period until they are derecognized. Noncompliance credits that are internally generated or granted by a regulator are not eligible for this election.



Because the model for credits can change based on changes in intent, entities may need a robust system to track significant information about environmental credits, processes and controls over the initial evaluation and subsequent re-evaluations.


Accounting model: Environmental credit obligations

At each reporting date an entity determines whether to recognize an ECO liability. To make this determination, the entity calculates the amount of credits it would owe if the balance sheet date was the end of the compliance period. This calculation disregards expected future actions or activities that could reduce the number of environmental credits due at the compliance program’s settlement date.

The measurement of an ECO liability depends on whether the liability is considered funded or unfunded. The ‘funded’ portion of the liability comprises amounts that could be settled with on-hand compliance credits. The ‘unfunded’ portion is the number of credits owed in excess of the funded portion. The following table summarizes the measurement requirements for an ECO liability.

Funded	The funded portion is measured based on the carrying amount of the entity's compliance credits expected to be derecognized on settlement. However, the funded portion excludes credits that were previously expensed or derecognized because they did not meet the asset recognition criteria. The exclusion of the previously expensed credits increases the unfunded portion of the liability. The FASB acknowledged that when an entity uses the previously expensed credits to satisfy the ECO liability, the entity may recognize a gain when that liability is derecognized.
Unfunded	<p>The unfunded portion is measured based on the fair value of the environmental credits an entity needs to acquire to settle the unfunded portion of the liability unless the entity intends to settle (or partially settle) by remitting:</p> <ul style="list-style-type: none"> • Cash. The entity measures the liability based on the cash settlement amount under the compliance program. • Environmental credits that will be received before the settlement of the liability from either (1) an existing unconditional purchase commitment for a fixed quantity of environmental credits at a fixed price, or (2) an unconditional right to receive a fixed quantity of environmental credits as part of a compliance program or contract for which environmental credits will be received as consideration. The entity measures the liability based on the estimated cost basis of the environmental credits to be received.

The entity recognizes the cost of an ECO liability either through earnings or, if appropriate, as part of the carrying amount of another asset accounted for under another Topic (e.g. Topic 330 on inventory). The entity recognizes subsequent changes in the ECO liability in the same manner as the initial cost of the ECO. ECO liabilities are derecognized under existing guidance for extinguishment of liabilities.



An entity first applies the environmental credit guidance to determine the cost of the compliance credits on hand, which is then used to measure the funded portion of its liability. If the compliance credits were internally generated and therefore have little or no cost basis, the funded portion of the liability could be zero or a nominal amount.

Presentation

Environmental credits and ECO liabilities are presented gross on the balance sheet and offsetting is prohibited. The compliance and noncompliance credits that will be transferred, used or remitted within 12 months of the balance sheet date are classified as current and the remainder as noncurrent. The portion of the ECO liability that will be settled within 12 months of the balance sheet date is classified as current and the remainder is classified as noncurrent.

Disclosure

Topic 818 includes quantitative and qualitative annual disclosure requirements about an entity's environmental credits and ECOs. For interim reporting periods, the Board observed that an entity is required to consider whether additional disclosures are required under the interim disclosure guidance in Topic 270. The following table summarizes key annual disclosures.

Environmental credits	
Information about how the entity obtained and intends to use its environmental credits, accounting policies used (e.g. subsequent measurement methodology), and significant estimates and judgments.	
The current and noncurrent portion of compliance and noncompliance credits, if not presented separately on the balance sheet.	
Total impairment expense, including the nature of the impaired environmental credits, the circumstances leading to the impairment, and line item(s) that include the impairment expense.	
Total expense recognized for credits not initially recognized as assets or subsequently derecognized and the line item(s) that include the expense.	
The effect on earnings of changing the use or intended use of the environmental credits and the nature of the change.	
Fair value disclosures in Topic 820 for environmental credits remeasured to fair value.	
Environmental credit obligations	
Information about compliance programs, including events and activities that result in an ECO and the nature and timing of settlement provisions. The accounting policies used to account for the ECO, significant estimates and judgments, and how the unfunded portion of an ECO liability is measured.	
The current and noncurrent funded and unfunded portions of the ECO liability, if not presented separately on the balance sheet.	
Total expense for ECO liabilities recognized, income statement line item, and total costs related to ECO liabilities that were capitalized as part of another asset and a description of that other asset.	
Fair value disclosures in Topic 820 applicable to the unfunded portion of the ECO liability measured at fair value.	

Effective date and transition

Effective date	
Public business entities	Annual and interim reporting periods in fiscal years beginning after December 15, 2027.
All other entities	Annual and interim reporting periods in fiscal years beginning after December 15, 2028.
Early adoption is permitted for all entities in interim and annual periods for which they have not issued or made available to issue their financial statements. If early adoption is elected in an interim period, the entity adopts it as of the beginning of the annual period that includes that interim period.	
Transition	
Transition approach	An entity applies the ASU through a cumulative-effect adjustment to opening retained earnings at the beginning of the annual period of adoption. Prior periods are not recast.

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