Accounting implications of the Russian invasion of Ukraine

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Key points

This In depth considers the impact of the Russian invasion of Ukraine (‘the invasion’) on the financial statements for periods ending on or after 31 March 2022 of entities whose business is affected by the invasion

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1. Background

1.1. General discussion

The Russian invasion of Ukraine, alongside the imposition of international sanctions, have a pervasive economic impact. It is important for reporting entities to recognise the significance of the impacts that the invasion will have on the business environment, liquidity and asset values, not only in the affected region, but also on companies beyond Russia and Ukraine. Global businesses might be severely impacted by supply chain disruption, market volatility, payment risk and increasing commodity costs resulting from the invasion. The impact is compounded by the decision of some global companies to limit or cease operations in Russia.

The potential implications of the recent developments on financial statements include not only the recognition and measurement of assets and liabilities but also presentation, disclosure and, possibly, an entity's ability to continue as a going concern.

In addressing the accounting implications of the invasion, management should consider company-specific information as well as the broader situation and implications. While the situation continues to evolve and new accounting implications will emerge, entities will need to take account of the events that have already occurred (for example, suspending operations, loss of customers or end markets, current inability of customers or debtors to pay, increase in commodity prices, SWIFT ban). As a result, we expect that many companies will reflect impairments, valuation allowances and other write downs in the current period. Global businesses that have taken the decision to exit their operations in Russia would need to consider whether these decisions result in a loss of control or significant influence over the operations and whether these operations, and related assets, represent non-current assets held for sale and discontinued operations.

Further, management should assess the need for transparent disclosure around the impact on current and future financial performance and the related risks and uncertainties, including those around the entity's ability to continue as a going concern.

This In depth addresses the main accounting implications of the current geopolitical situation on financial statements with a reporting period ending on or after 31 March 2022. The current situation, and responses thereto by governments and entities, is fast-moving and subject to change. Although this In depth provides an overview of the current state of affairs, it might not consider all current sanctions or all possible accounting implications. While we will update or add to this document as warranted, entities should consider their individual circumstances and ensure that they have performed a thorough accounting analysis of the implications of the invasion.

2. Sanctions and restrictions

2.1. General discussion

The level and severity of sanctions and restrictions on Russia continues to evolve and could have both direct and indirect accounting impacts on companies. Companies that have interests in Russia or Russian customers and suppliers are likely to be the most severely impacted by sanctions.

The number of sanctions and restrictions being introduced are fast-moving and very fluid. Entities should consult with legal counsel and professional advisors to get an understanding of the sanctions that directly and indirectly impact them. Furthermore, sanctions are continually being updated and so any sanctions list may become outdated quickly. Government websites may be a source for sanctions that are applicable in various jurisdictions.

The following summary sets out examples of broad categories of sanctions that may be applicable. However, this should not be interpreted as a complete list of the types of sanctions an entity may be exposed to.

Sanctions and restrictions imposed generally fall into the following categories:

Financial service sector sanctions: Imposing financial restrictions has been at the heart of the co-ordinated global response to the Russian invasion of Ukraine including investment, borrowing and lending, blocking or restricting cash transfers/bank & investment accounts etc.

Energy sector restrictions: Restrictions could include bans on purchasing outputs of the energy sector (for example, crude oil) and banning imports relevant to the energy sector (for example, oilfield equipment).

Geographic restrictions: Restrictions on doing business with areas of Ukraine occupied by Russia (for example, Crimea and other Ukrainian territory claimed by Russia, the Luhansk and Donetsk regions).

Restrictions on doing business with individuals and entities within Russia: A number of countries have introduced restrictions on certain Russian wealthy or politically connected individuals. This may include restrictions on transactions with the individuals and any entities controlled by such individuals or other entities considered to be in strategic sectors. The level of restrictions and which individuals are restricted can vary by territory.

Export controls: A number of countries have introduced bans/restrictions on a broad range of items that can be imported or exported to and from Russia (for example, advanced technologies in the defence, aviation, and maritime sectors).

Restrictions against Belarus: A number of countries have introduced similar categories of restrictions against individuals or entities in Belarus.

Counter-sanctions imposed by Russia: In response to sanctions against Russia, Russia has imposed counter-sanctions that may fall into similar categories as the sanctions against Russia.

Within this In depth, further guidance is provided on the accounting implications as a result of the direct and indirect consequences of the sanctions and restrictions introduced. Impacted areas include consideration of restricted cash (see section 7.1), impact of foreign currency and exchange rates (see section 13), financial instruments (see section 4), impairment of non-financial assets (see section 3.1) and consideration of non-current assets held for sale (see section 3.7).

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 2.1 – What are the implications following the limited access certain Russian banks have to the SWIFT (Society for Worldwide Interbank Financial Telecommunication) system?

3. Non-financial assets

3.1. Impairment of non-financial assets

Reporting entities will need to assess whether a non-financial asset or cash generating unit (CGU) is impaired as a direct or indirect result of the invasion and other geopolitical tensions. Assets potentially affected include fixed assets, right-of-use assets, goodwill, and intangibles assets. IAS 36 requires goodwill and indefinite-lived intangible assets to be tested for impairment at a minimum every year, and other non-financial assets whenever there is an indicator those assets might be impaired. The following are events that might indicate impairment:

- temporarily ceasing operations;
- breaches of supply/purchase contracts;
- limitation of market for product delivery;
- decisions by multinational companies to leave the Russian market; and
- decline in profitability and physical damage as a result of the invasion.

Plans to dispose of or abandon an operation because of the invasion could trigger an impairment of the underlying assets in the consolidated financial statement.

When assessing impairment, a company should distinguish between assets that are damaged and those whose value is impacted by changes in projected cash flows as a result of the invasion. Assets that are destroyed should be written off. Assets that are damaged may need to be written down, and/or their useful lives may need to be revisited. Assets impacted by changes in the supply and demand for physical items or in the cash flows relating to the assets (for example, production is affected due to reduced or increased demand for goods or limited supply of raw materials, which may also affect pricing and cash flows as a result of sanctions or otherwise) may need to be tested for impairment.

Management should consider whether:

- these events are an indicator of impairment requiring goodwill and indefinite-lived intangible assets to be tested outside the annual cycle or other assets to be tested;
- the invasion and the measures taken by governments and organisations to respond to it are likely to reduce future cash inflows, or increase operating and other costs, for the reasons described above; and
- the assumptions and cash flow forecasts used to test for impairment should be updated to reflect the economic conditions at the balance sheet date, specifically to address increased risk and uncertainty.

An expected cash flow approach (using multiple probability-weighted scenarios) might be a better way to estimate the recoverable amount of the asset /CGU than a single predicted outcome, to capture the increased risk and uncertainty in the cash flows. The potential impact of measures taken to deal with the effects of the invasion could be included as additional scenarios in an expected cash flow approach. There might be a range of potential outcomes considering different scenarios.

Irrespective of how the recoverable amount is determined, the factors used to determine the discount rate should be revised to reflect the impact of the sanctions and the invasion and the measures taken to respond to it (for example, the risk-free rate, country risk and asset risk). The discount rate used in a single predicted outcome approach should be adjusted to incorporate the risk associated with the invasion. Management should ensure that appropriate risk is reflected in either the cash flows or the discount rate.

Whichever approach management chooses to reflect the expectations about possible variations in the expected future cash flows, the outcome should reflect the expected present value of the future cash flows. Where fair value is used to determine the recoverable amount, the assumptions made should reflect market participant assumptions.

An absence of market-based pricing puts significant focus on the determination of the appropriate market participants with whom the company would transact. As a result of the invasion, the historically applied perspectives may no longer be valid and certain counterparties may not be available. As such, management

will have to assess if historical assumptions are still sustainable or who presently would be a relevant market participant and how that may affect the price or other aspects of determining fair value. When there is no market available to the company, it may have to determine the characteristics of a market participant to which it would hypothetically sell the asset if it were seeking to do so. Once the market participant characteristics have been determined, the company would identify the assumptions that those market participants would consider when pricing the asset. The company should construct a hypothetical or "most likely" market for the asset based on its own assumptions about what market participants would consider in negotiating a sale of the asset or transfer of the liability.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.1.1 – Is the Russian invasion of Ukraine an impairment indicator?

FAQ 3.1.2 – Should the business plan prepared by management be revised to incorporate the impacts of the Russian invasion of Ukraine?

FAQ 3.1.3 – How can impairment tests that incorporate cash flow forecasts be more reliably performed in periods of uncertainty?

FAQ 3.1.4 – What are the consequences of the Russian invasion of Ukraine on the discount rate?

FAQ 3.1.5 – Impact of country and currency risk on discount rate

FAQ 3.1.6 – Rates vary to reflect specific risk factor

FAQ 3.1.7 – Level at which impairment testing is performed

FAQ 3.1.8 – Is an entity permitted to change the timing of its annual impairment test of goodwill, in the light of the Russian invasion of Ukraine if the test was not historically performed at year end?

FAQ 3.1.9 – How are future cash flows determined if the entity intends to abandon it's activity?

FAQ 3.1.10 – Determining a hypothetical market participant

3.2. Impairment disclosures

The disclosure requirements in IAS 36 are extensive. Management should consider specifically the requirements to disclose assumptions and sensitivities in the context of testing goodwill and indefinite-lived intangible assets.

Management should also consider the requirements in IAS 1, *Presentation of financial statements*, to disclose the major sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the financial statements in a subsequent period.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.2.1 – Which impairment disclosures will be of particular interest to users of financial statements this year?

3.3. Associates and joint ventures

Interests in joint ventures and associates accounted for under the equity method are tested for impairment in accordance with IAS 28 *'Investments in Associates and Joint Ventures'*. Management should consider whether the impact of the invasion is an indicator that an associate or joint venture is impaired.

Interests in joint ventures and associates that are within the scope of IFRS 9, 'Financial instruments', are subject to that standard's impairment guidance.

The international sanctions against Russia and local legislation could impact whether an investor continues to exercise significant influence or joint control over a Russian investee. For example, local legislation and/or sanctions might result in an investor needing to remove its directors from the board and the investor might

legally be unable to appoint any directors in the foreseeable future. It is likely in this case that the investor has lost significant influence. However, in limited cases an entity might still have significant influence over its associate or joint control over its joint venture under these circumstances when considering the other indicators of significant influence in paragraph 6 of IAS 28.

Decisions by global entities to voluntarily abandon businesses and withdraw representatives from operations in Russia and/or Ukraine, such as directors from the board of directors, could also impact the significant influence or joint control assessment.

Equity accounting ceases when significant influence or joint control is lost. An investor might lose significant influence or joint control but retain an investment in the entity.

For further consideration on how to account for a loss of significant influence or joint control in an associate or a joint venture, please refer to paragraph 31.72 and 31.73 in the Manual of Accounting

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.3.1 – Is the Russian invasion of Ukraine a significant event for associates with different period ends from the entity?

FAQ 3.3.2 - What are the implications in the significant influence assessment of an entity that decides to remove directors from the board in the context of the Russian invasion of Ukraine?

FAQ 3.3.3 - What are the implications in the significant influence assessment of an entity that is required to remove directors from the board in the context of the Russian invasion of Ukraine?

3.4. Inventories

It will be necessary to consider the net realisable value of inventory and in some cases write-down inventory on hand at balance sheet date. These write-downs could be due to reduced movement in inventory, an inability to source or an increase in the cost of raw materials and component parts to complete production due to disruptions in international supply chains, an inability to pass increased costs on to existing customers or inventory obsolescence due to lower than expected sales.

Determining net realisable value at the balance sheet date requires consideration of all available data, including changes in product prices experienced or anticipated subsequent to the balance sheet date. However, when a specific event results in the loss of value of the inventory, such as discrete governmental actions (such as sanctions) or the disappearance of a market due to the invasion that was not reasonably predicted as of the balance sheet date, the inventory would be impaired in the same period that the specific event occurred.

In addition, IAS 2 Inventories requires fixed production overheads to be included in the cost of inventory based on normal production capacity. Reduced production might affect the extent to which overheads can be included in the cost of inventory.

Entities should assess the significance of any write-downs and whether they require disclosure in accordance with IAS 2.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.4.1 – What factors should be considered in determining the normal capacity and abnormal costs for inventory capitalisation as a result of the Russian invasion of Ukraine?

FAQ 3.4.2 – How is overhead cost allocated to inventory where the number of units produced is reduced due to the Russian invasion of Ukraine?

3.5. Property, plant and equipment

The Russian invasion of Ukraine, subsequent sanctions and economic crises might mean property, plant and equipment are under-utilised or not utilised for a period, or that capital projects are suspended. Assets that are damaged may need to be written down or their useful lives may need to be revisited. IAS 16, *'Property, plant*

and equipment', requires depreciation to continue to be charged in the income statement while an asset is temporarily idle. IAS 23, *'Borrowing costs'*, requires the capitalisation of interest to be suspended when development of an asset is suspended.

A long-lived asset is not abandoned if it is only temporarily idled. For example, if a company temporarily shutters a manufacturing facility with a long remaining useful life, but intends to resume operations after military activities in the area abate, the facility has not been abandoned. Although temporarily idling a long-lived asset (including ROU assets) may trigger an impairment of that asset (or asset group to which it belongs), a company does not stop depreciating the asset while it is idle.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.5.1 – Can an entity stop depreciating an asset if it is idle?

3.6. Fair value measurement of non-financial assets and liabilities

Fair values are likely to change significantly as a result of the Russian invasion of Ukraine.

Valuation best practices support the use of multiple valuation techniques when estimating the fair values. Changing methodologies (for example, from a market multiple approach to a discounted cash flow approach) or changing the weighting where multiple valuation techniques are used, would be appropriate if the change results in a measurement that is equally or more representative of fair value in the circumstances. This change would be considered a change in accounting estimate.

The discount rate used in a discounted cash flow technique includes a number of market inputs, including a risk-free rate and a cost of debt. In jurisdictions impacted by the invasion, the cost of debt has likely increased due to the numerous sanctions imposed on Russia and the pervasive impact of the invasion on the territories' economies and financial markets. This could result, for some entities, in a higher weighted average cost of capital, and thus a higher discount rate, which would reduce the fair values. However, entities should remember that the discount rate needs to be calibrated to the risks in the cash flow forecast, including the long-term growth rate.

Please also refer to fair value measurements of financial instruments under IFRS 13 (section 4.7).

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.6.1 – Uncertainties in cash flows and change in valuation technique for level 3 fair value measurement

FAQ 3.6.2 – Determining fair value where an entity might be forced to liquidate assets

3.7. Assets held for sale and discontinued operations

A growing number of international companies are dialling back operations in Russia as a result of the invasion. As businesses around the world assess their response to the invasion and related sanctions, some have announced plans to discontinue operations in Russia while others are likely considering similar actions. Some entities outside of Russia may be owned or otherwise controlled by entities or individuals who are subject to sanctions and may be considering transactions to change ownership (see further section 3.8).

Subsidiaries, businesses and non-current assets might be disposed of in a number of different ways. The method by which the asset or business is disposed of will determine whether the disposal will fall within the scope of IFRS 5.

Some scenarios that may likely arise in the current situation are:

1. Outright sale of a business

In an outright sale/disposal, the entity sells a business, resulting in the loss of control, in exchange for consideration. Consideration should be given to all of the factors to determine the date on which the parent loses control of the investee.

An outright sale will fall within the scope of IFRS 5 once the held for sale criteria are met. An outright sale includes sales for nil consideration and paying to dispose of an investment.

When an entity is committed to a sale plan involving loss of control of a subsidiary, it should classify all the assets and liabilities of that subsidiary as held for sale when the relevant criteria are met. This is regardless of whether it will retain a non-controlling interest in the former subsidiary after the sale, such as for instance an interest in an associate or a joint venture.

The plan to dispose of a non-current asset or disposal group in the current environment is an impairment indicator, and therefore the non-current asset or disposal group should be tested for impairment under IAS 36 before being classified as held for sale. In addition, on classification as held for sale, the requirement to measure a non-current asset or disposal group held for sale at the lower of carrying amount and fair value less costs to sell may give rise to a further write down in value (impairment loss) and possibly its subsequent reversal.

2. Piecemeal sale, in which assets are sold individually or as a disposal group (that is, a group of assets disposed of together that might include associated liabilities)

In a piecemeal disposal, assets are sold individually or as a disposal group. The assets and liabilities should be de-recognised in accordance with the relevant standard. For example, IAS 16 or IAS 38 is relevant to non-financial assets. The gain or loss on the sale of individual assets is measured as the difference between the net disposal proceeds and the carrying amount of the asset at the date of disposal. The principle applies to each sale. IFRS 9 (IAS 39) is relevant to financial assets and liabilities. Any profits or losses on sale or settlement are recognised on derecognition.

In a piecemeal disposal, the disposal plan needs to be analysed to determine if the piecemeal disposals should be considered as a single plan of disposal, where all of the assets and liabilities meet the 'held for sale' criteria at the same point. If the IFRS 5 criteria are met, the individual assets or groups of assets and liabilities will need to be classified as non-current assets or disposal groups held for sale prior to the date of disposal. Prior to classification as held for sale, the assets should be measured in accordance with their applicable standards; the planned change in use of the asset (that is, plan to dispose) in the current environment would be an impairment indicator requiring the assets to be tested for impairment under IAS 36.

3. Abandonment (for example, closure of the business)

If companies are unable to sell a business or specific assets due to sanctions restrictions on foreign currency movement or as a result of a depressed economy resulting from the invasion, companies may decide to abandon the businesses or scrap the assets. For businesses over which the company previously exercised control, management will need to first establish whether the decision to abandon the business results in a loss of control (refer to section 3.8).

Typically, transfer of control cannot be clearly evidenced when a business is disposed of by terminating it through closure. Individual assets might be sold off and liabilities might be settled, and these are subject to the same de-recognition principles as above for piecemeal disposals. Other assets might be scrapped.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.7.1 – Abandonment and discontinued operations

FAQ 3.7.2 – Treatment of lease penalty for costs to sell

FAQ 3.7.3 – How should the impairment loss be allocated?

3.8. Loss of control and disposal of investments in subsidiaries

Restrictions have been imposed by governments on Russia and by the Russian government. Furthermore, many global companies have decided to withdraw from operations in Russia and/or Ukraine. As a result of these decisions, entities might consider whether they have lost control over their subsidiaries in the affected regions. Concluding on whether these restrictions result in an entity losing control might be an area of significant judgement.

An investor loses control of an investee (its subsidiary) when it no longer has the power to direct the investee's relevant activities or when it no longer has exposure to variable returns. Multinational companies should only

de-consolidate Russian subsidiaries if they no longer meet one of the three criteria for control under IFRS 10, 'Consolidated financial statements'. These are:

1. power over the investee;
2. exposure, or rights, to variable returns from its involvement with the investee; and
3. the ability to use its power over the investee to affect the amount of the investor's returns.

[IFRS 10 para 7(a)–(c)].

If one or more of the elements of control changes, an entity should reassess control.

An investor will lose control of its subsidiary when it no longer has the power to direct its relevant activities, and hence loses the ability to vary its returns. This is a high hurdle. Where an entity has power, it must demonstrate (in order to determine that it does not have control) that it has no exposure to variable returns. Difficulties in repatriating earnings, and uncertainty about the exchange rate, are typically not sufficient to conclude that an entity no longer has exposure to variable returns.

Although the restrictions imposed by government sanctions may be temporary and result in a temporary loss of control, a parent will be required to deconsolidate the investee from the date when it loses control. A subsidiary's income and expenses should be included in the consolidated financial statements until the parent ceases to control the subsidiary. When an entity ceases to be a subsidiary, its former parent might retain an ownership interest and the entity might still be an associate or a joint venture or merely an investment. The loss of control of a subsidiary results in recognising a gain or loss on deconsolidation of the interest and on the revaluation of any retained non-controlling investment in the consolidated financial statements. A loss of control is an economic event, similar to that of gaining control, and so it is a remeasurement event.

A parent is required to continually assess whether it has control over its investees.

A parent needs to consider whether there is significant doubt about the existence of control. An entity should also consider what should be disclosed to explain the significant judgements and assumptions made in its control assessment. [IFRS 12 para 7]. An entity is also required to disclose significant restrictions on its ability to access or use the assets and settle the liabilities of the group. [IFRS 12 para 13].

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 3.8.1 – Does an entity lose control over its subsidiaries as a consequence of the foreign exchange and trade restrictions imposed by governments in the context of the Russian invasion of Ukraine?

FAQ 3.8.2 – What are the implications in the control assessment of an entity that decides to remove directors from the board in the context of the Russian invasion of Ukraine?

4. Financial instruments

When accounting for an existing financial instrument within the scope of IFRS 9, there are a wide range of possible impacts that could arise from the invasion and related responses such as sanctions and other governmental actions, depending on individual facts and circumstances.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.1 – What are factors to consider when reflecting impacts of the Russian invasion of Ukraine in the accounting of an existing financial instrument within the scope of IFRS 9?

4.1. Classification and measurement of financial assets under IFRS 9

Under IFRS 9, the classification of financial assets that are debt instruments depends on both (a) the entity's business model for managing the financial assets, and (b) whether the contractual cash flows of the financial asset are solely payments of principal and interest.

Management should consider the impact of the invasion on the classification of these assets, in particular whether the entity's business model for managing financial assets might have changed, both for existing financial assets and/or new financial assets.

Additionally, the impact of any changes to the terms of a loan agreement, such as a result of sanctions, or the renegotiation of terms between a borrower and a lender, should be assessed. Specifically, lenders should apply the guidance in IFRS 9 to determine the impact of the change in terms, including those for determining whether the change to the terms results in derecognition and, if not, for recognising a modification gain or loss.

Borrowers should also apply the guidance in IFRS 9 to determine whether a financial liability should be derecognised. A financial liability should be removed from the balance sheet when it is extinguished (that is when the obligation is discharged, cancelled or expires). Similarly, a substantial modification of the terms of an existing financial liability or a part of it should be accounted for as an extinguishment of the original liability and the recognition of a new liability.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

EX 4.1.1 – De-recognition of financial assets

EX 4.1.2 – De-recognition of financial asset due to modification of cash flows

FAQ 4.1.3 – How should an entity account for changes to the cash flows on a debt instrument measured at amortised cost or fair value through other comprehensive income (FVOCI)?

FAQ 4.1.4 – How are the criteria for reclassification of financial assets and the timing of reclassification assessed?

Relevant guidance for the borrowers:

FAQ 4.1.5 – What qualitative and/or quantitative tests are required to determine whether terms are 'substantially different'?

4.2. Impairment under IFRS 9

Where an entity has any financial instruments that are within the scope of IFRS 9's expected credit loss (ECL) model, management should consider the impact of the invasion on the ECL. Instruments to be considered include;

- loans, trade and other receivables;
- debt instruments not measured at fair value through profit or loss;

- contract assets;
- lease receivables;
- financial guarantees; and
- loan commitments.

Management should consider the impact of the invasion on the following:

- whether the ECL is measured at a 12-month or lifetime ECL. If the credit risk (risk of default) has increased significantly since initial recognition, the ECL is measured at the lifetime ECL rather than the 12-month ECL (except for assets subject to the simplified approach, such as short-term receivables and contract assets, which are always measured using lifetime ECL);
- whether the financial instrument is credit impaired. This might be evidenced by significant financial difficulty of the borrower, a breach of contract such as a default, or it becoming probable the borrower will enter bankruptcy or other financial reorganisation. More broadly, an asset is credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred. That might be the case even when the borrower itself is credit worthy, for example where the borrower is prevented from making contractual payments due to sanctions or other governmental restrictions; and
- the estimate of ECL itself. This will include all of:
  - the credit risk (risk of default); for example, this might increase if the debtor's business is adversely impacted by the invasion;
  - the amount at risk if the debtor defaults (exposure at default); for example, debtors affected by the invasion might draw down on existing unused borrowing facilities, or cease making discretionary over-payments, or take longer than normal to pay, resulting in a greater amount at risk; and
  - the estimated loss as a result of default (loss given default); for example, this might increase if the invasion results in a decrease in the fair value of a non-financial asset pledged as collateral and the enforceability of integral guarantees would also need to be considered.

Where contractual payment dates are extended or amounts are expected to be received later than when contractually due, this may give rise to an ECL, unless either additional compensation is received for the lost time value of money, or the EIR is 0%.

IFRS 9 requires forward-looking information (including macro-economic information) to be considered both when assessing whether there has been a significant increase in credit risk and when measuring ECL. This might be achieved by adding one or more additional scenarios to the entity's existing scenarios related to the escalation of the invasion, amending existing scenarios and/or increasing their weighting, or using an 'overlay' if the impact is not included in the entity's main ECL model.

Management should consider the need to disclose the impact of the invasion on the impairment of financial assets. For example, disclosures required by IFRS 7, 'Financial instruments: Disclosures', that might be affected include:

- how the impact of forward-looking information has been incorporated into the ECL estimate;
- details of significant changes in assumptions made in the reporting period; and
- changes in the ECL that result from assets moving from stage 1 to stage 2, and to stage 3.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.2.1 – In the context of the Russian invasion of Ukraine and ECL, what information is 'reasonable and supportable'?

FAQ 4.2.2 – To what extent should additional information related to the Russian invasion of Ukraine that becomes available after the reporting date be included in the ECL estimate?

4.3. Hedge accounting under IFRS 9

Management should consider the impact of the invasion on its existing hedges, in particular whether the hedges continue to meet the criteria for hedge accounting. For example, if a hedged forecast transaction is no longer highly probable to occur, hedge accounting is discontinued. For similar reasons, management should also consider the impact of the invasion on its ability to designate new hedges.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.3.1 – What factors should be considered in assessing the 'highly probable' criterion for cash flow hedges of forecast purchases or sales in light of disruptions to the supply chain or sales process as a result of the Russian invasion of Ukraine?

EX 4.3.2 – Recoverability test for hedging reserves

FAQ 4.3.3 – Are government bonds that are denominated in USD or Euro, and issued by the government of Russia and held by foreign investors who are impacted by the sanctions, credit impaired under IFRS 9 as at 31 March 2022?

4.4. Hedge accounting under IAS 39

Management should consider the impact of the invasion on its existing hedges, in particular whether hedges continue to meet the criteria for hedge accounting. For example, if a hedged forecast transaction is no longer highly probable to occur or no longer highly effective, hedge accounting is discontinued. For similar reasons, management should also consider the impact of the invasion on its ability to designate new hedges.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.4.1 – What factors should be considered in assessing the 'highly probable' criterion for cash flow hedges of forecast purchases or sales in light of disruptions to the supply chain or sales process as a result of the Russian invasion of Ukraine?

4.5. 'Own use' under IFRS 9

Under IFRS 9, contracts to buy or sell a non-financial item that can be settled net in cash are within the scope of the standards (with the result that they are typically accounted for as derivatives), unless the contracts were entered into and continue to be held for the purpose of receipt or delivery of non-financial items to meet the entity's expected purchase, sale or usage requirements. The Russian invasion of Ukraine might impact whether some contracts meet these 'own use' requirements. For example, disruption to an entity's supply chain due to the invasion might have the effect that certain commodity contracts will be settled net in cash rather than by physical delivery. Wide-ranging impacts to the supply of commodities (energy, rare earth metals, etc.) and other inputs/materials, transport disruption (flight paths, invasion areas), and export control restrictions may have an impact on the "own use" assertion.

As noted, entities should carefully assess the broader implications of the invasion and associated sanctions as well as the overall market developments in response to the invasion.

4.6. Disclosures under IFRS 7

Additional disclosures might be required to reflect the evolving risks associated with the invasion. IFRS 7 requires, amongst other things, disclosure of defaults and breaches of loans payable, of gains and losses arising from derecognition or modification, and of any reclassification from the cash flow hedge reserve that results from hedged future cash flows no longer being expected to occur.

Entities will need to disclose any changes in their financial risks (such as credit risk, liquidity risk, currency risk and other price risk) or in their objectives, policies and processes for managing those risks. In particular, additional disclosures about liquidity risk might be needed where the invasion has affected an entity's normal

levels of cash inflows from operations or its ability to access cash in other ways, such as from factoring receivables or supplier finance.

Enhanced concentration risk disclosures may also be necessary to indicate the extent to which various financial risks are concentrated in Russia/Ukraine.

The fair value hierarchy level of investments in shares or financial instruments traded in Russian markets may be impacted where active markets are no longer accessible/observable. See section 4.7 for more information.

Given the volatility in the commodities market, certain derivatives may be in a significant liability position. Therefore, entities need to consider the disclosures relevant to liquidity risk, including the fact that IFRS 7B.11FG requires disclosures of derivative arrangements that could require the posting of collateral (for example, margin calls for derivatives).

Entities also need to consider if there are liabilities that cannot be paid due to sanctions and whether these are considered to be in default. The impact of any cross-default clauses should also be considered. Please see section 11.2 for further guidance on breach of covenants.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.6.1 – What are examples of concentrations of risk?

4.7. Fair value of financial assets and liabilities

The fair value of an asset or liability at the reporting date should be determined in accordance with the applicable IFRS standards. Where fair value is based on an observable market price, the quoted price at the reporting date should be used. The fair value of an asset reflects a hypothetical exit transaction at the reporting date. Changes in market prices after the reporting date are therefore not reflected in asset valuation.

The volatility of prices on various markets may increase as a result of the invasion. This affects the fair value measurement either directly – if fair value is determined based on market prices (for example, in the case of shares or debt securities traded on the Russian market) – or indirectly (for example, if a valuation technique is based on inputs that are derived from volatile markets).

Counterparty credit risk and the credit spread that is used to determine fair value might also increase, particularly as a result of increased sanctions imposed on Russia.

A change in the fair value measurement affects the disclosures required by IFRS 13, 'Fair value measurement', which requires entities to disclose the valuation techniques and the inputs used in the fair value measurement, as well as the sensitivity of the valuation to changes in assumptions. It might also affect the sensitivity analysis required for recurring fair value measurements categorised within level 3 of the fair value hierarchy. The number of instruments classified as level 3 might increase.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.7.1 – Determining whether a market is still active in a period of market disruption

FAQ 4.7.2 – Assessing prices in inactive markets

FAQ 4.7.3 – Determining whether transactions are orderly

FAQ 4.7.4 – Adjustments to the quoted price in an active market

FAQ 4.7.5 – Delays in the availability of information as a result of the Russian invasion of Ukraine

FAQ 4.7.6 – Post market closure events

FAQ 4.7.7 – Uncertainties in cash flow fair value measurement of financial instruments as a result of the Russian invasion of Ukraine

FAQ 4.7.8 – Should possible future modifications be considered when determining the fair value of a debt instrument?

FAQ 4.7.9 – Consideration of fair value where an entity has breached a debt covenant

FAQ 4.7.10 – What are the implications of the Russian invasion of Ukraine on the measurement of Russian bonds that are held at fair value?

4.8. Subsidiaries, associates and joint ventures measured at fair value

The fair values of investments in subsidiaries, associates and joint ventures might be affected by equity market volatility. The starting point for the valuation of a listed company is the market prices at the reporting date.

Entities are required to disclose changes in business or economic circumstances that affect the fair value of investment entities or investments in associates and joint ventures carried at fair value under IFRS 9.

4.9. Classification and measurement of financial assets under IAS 39

Financial assets are classified in one of four categories under IAS 39. Reclassifications between categories could be considered by management as a result of the Russian invasion of Ukraine. The guidance in IAS 39 should be followed to determine whether reclassification is permitted or required.

4.10. Impairment of financial assets under IAS 39

Under IAS 39, a financial asset is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the asset's initial recognition (a 'loss event'). For investments in equity securities, changes in the political or legal environment affecting the issuer's business, or a 'significant' or 'prolonged' decline in the fair value below cost, are examples of objective evidence of impairment.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 4.10.1 – What is a 'significant' or 'prolonged' decline in fair value below cost?

FAQ 4.10.2 – Are government bonds that are denominated in USD or Euro, and issued by the government of Russia and held by foreign investors who are impacted by the sanctions, impaired under IAS 39 as at 31 March 2022?

5. Leases

A lessor and a lessee might renegotiate the terms of a lease as a result of the invasion. In some cases, a lessor may have significant concerns over the recoverability of lease receivables from entities within Russia, particularly given the sanctions imposed on a number of Russian banks. Both lessors and lessees should consider the requirements of IFRS 16, 'Leases', and whether the concession should be accounted for as a lease modification and spread over the remaining period of the lease.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 5.1 – What are the accounting implications of a force majeure clause in a lease contract in the context of the Russian invasion of Ukraine?

FAQ 5.2 – Impairment of lease receivables

FAQ 5.3 – Should a lessor in an operating lease continue to recognise lease income when its collectability is uncertain due to the Russian invasion of Ukraine?

6. Insurance contracts

6.1. Policyholder accounting

Management should consider whether losses arising as a result of the Russian invasion of Ukraine are covered by its insurance contracts. For example, the closure of some businesses in Russia, Ukraine or neighbouring countries may give rise to claims under business continuity insurance. Property damaged or destroyed as a result of the invasion might give rise to claims under property-casualty insurance. An entity that holds insurance contracts (and does not also issue insurance contracts) might have a contingent asset arising from a right to reimbursement under an insurance contract. See section 9.3 for further information.

6.2. Insurer accounting

An entity that issues insurance contracts that provide coverage in the affected areas should consider whether there is a need to revise its estimate of claims. IFRS 4 grandfathers an entity's existing accounting policies for insurance contracts from previous GAAPs, specifying limited requirements for the measurement of insurance contracts. However, it does include minimum measurement requirements, including a liability adequacy test.

Entities should assess whether any costs arising from the Russian invasion of Ukraine should be considered when measuring insurance liabilities under the grandfathered GAAP.

There are no additional requirements to an entity's grandfathered accounting policies provided the liability adequacy test meets minimum requirement. The minimum requirement is that the test considers current estimates of:

- all contractual cash flows;
- of related cash flows such as claims handling costs; and
- cash flows resulting from embedded options and guarantees.

The costs arising from the Russian invasion of Ukraine should therefore be considered in the current estimate of future cash flows used for the liability adequacy test, including current estimates of the expected severity and frequency of expected claims given macro-economic information, and expectations related to the escalation of the invasion.

If the entity's accounting policies do not require a liability adequacy test that meets the minimum requirements, the entity is required to conduct a test that compares the carrying amount of insurance liabilities adjusted for any related deferred acquisition costs and related intangible assets, with the amount that would have been recognised if the insurance liabilities had been in the scope of IAS 37.

Management should consider the need to disclose the impact of the invasion on the risks arising from insurance contracts, and hence the assumptions used to measure insurance contracts. IFRS 4 requires an insurer to disclose information that enables users of its financial statements to evaluate the nature and extent of risks arising from insurance contracts. To comply with these requirements, information disclosed would include:

- the insurer's objectives, policies and processes for managing risks arising from insurance contracts. Such risks include;
  - risks relating to the Russian invasion of Ukraine;
  - information about risk exposures;
  - concentrations of risk;
  - how an entity manages those risks; and
  - the sensitivity analysis showing the effect of changes in risk variables.
- the significant judgements and changes in those judgments as a result of assumptions about risks covered.

IFRS 4 will be replaced by IFRS 17 for annual reporting periods beginning on or after 1 January 2023, with early adoption permitted. We do not expect entities to be early adopting IFRS 17.

7. Cash and cash equivalents

IAS 7 defines cash equivalents as short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. The sanctions that have been imposed against the Russian Central Bank have restricted the access of the Russian state to foreign currency reserves. Accordingly, the Russian Central Bank will have limited options in intervening in the foreign currency market and the liquidity/exchangeability of the Russian Rouble as well as its value may be severely impacted.

Entities may also have limitations on the ability to access deposits in the Russian banking system. Management should consider whether investments previously classified as cash equivalents continue to meet the definition in light of increases in credit risk and/or restrictions on redemption. Investments might need to be re-classified out of cash equivalents and/or cash might need to be presented or disclosed as restricted.

7.1. Restricted cash

The sanctions and restrictions imposed on Russia continue to evolve and could have both direct and indirect accounting impacts on entities. Entities that have interests in Russia or Russian customers and suppliers are likely to be the most severely impacted by sanctions. For more information on Sanctions and restrictions see section 2.

Cash might be held by Russian subsidiaries where sanctions and restrictions are in force, such that the cash is not freely transferable around the group. Where significant amounts of cash and cash equivalent balances are not available for use by the group, disclosure is required of the relevant amounts, along with a commentary on their restriction.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 7.1.1 – How do restrictions on the remittance of cash affect presentation of cash and cash equivalents?

FAQ 7.1.2 – How should the entity classify demand deposits that are subject to restrictions on use in the statement of cash flow and in the statement of financial position?

FAQ 7.1.3 – Should restricted funds that are not cash be classified in the cash flow statement as part of ‘cash and cash equivalents’?

8. Revenue recognition

The Russian invasion of Ukraine and the associated sanctions have impacted some companies' ability to sell or receive goods and services and has significantly impacted the foreign currency market and the liquidity/exchangeability of the Rouble.

An entity's sales and revenue might decline as a result of the reduced economic activity following the sanctions imposed by different governments, supply chain disruptions, and the recent volatility in the financial markets. The decline in sales, and resulting impact on revenue, is accounted for when it happens.

However, there could also be an effect on the assumptions made by management in measuring the revenue from goods or services already delivered and, in particular, on the measurement of variable consideration. For example, reduced demand could lead to additional price concessions, reduced volume discounts, penalties for late delivery or a reduction in the prices that can be obtained by a customer. All of these could affect the measurement of variable consideration. IFRS 15, 'Revenue from contracts with customers', requires variable consideration to be recognised only when it is highly probable that amounts recognised will not be reversed when the uncertainty is resolved.

Management should reconsider both its estimate of variable consideration and whether the recognition threshold is met.

IFRS 15 is applied only to those contracts where management expects a customer to meet its obligations as they fall due. Management might choose to continue to supply a customer even where it is aware that the customer might not be able to pay for some or all of the goods being supplied. Revenue is recognised in these circumstances only where it is probable that the customer will pay the transaction price when it is due, net of any price concession.

IFRS 15 requires an entity to disclose information that allows users to understand the nature, amount, timing and uncertainty of cash flows arising from revenue. This might require, for example, information about how an entity has applied its policies, taking into account the uncertainty that arises from the Russian invasion of Ukraine, the significant judgements applied (for example, whether a customer is able to pay) and the significant estimates made (for example, in connection with variable consideration).

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 8.1 – How could revenue recognition be impacted by a customer's inability to make payments due to the disruption caused by the Russian invasion of Ukraine?

FAQ 8.2 – Negative revenue: revision of a 'highly probable' variable transaction price due to the Russian invasion of Ukraine

FAQ 8.3 – For entities using the cost-to-cost input method for revenue recognition, would additional costs arising due to the Russian invasion of Ukraine be included in the measure of progress?

FAQ 8.4 - What should entities consider when modifying contracts or terminating relationships with customers in Russia?

9. Non-financial obligations

9.1. Provisions

IAS 37, *'Provisions, contingent liabilities and contingent assets'*, requires a provision to be recognised only where:

- an entity has a present obligation;
- it is probable that an outflow of resources is required to settle the obligation; and
- a reliable estimate can be made.

Management's actions in response to the Russian invasion of Ukraine should be accounted for as a provision only to the extent that there is a present obligation for which the outflow of economic benefits is probable and can be reliably estimated. For example, a provision for restructuring should be recognised only where there is a detailed formal plan for the restructuring, and management has raised a valid expectation in those affected that the plan will be implemented.

IAS 37 does not permit provisions for future operating costs or future business recovery costs.

IAS 37 requires an entity to disclose the nature of the obligation and the expected timing of the outflow of economic benefits.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 9.1.1 - Are penalties arising on the termination of a contract in the scope of IAS 37 or IFRS 9?

9.2. Onerous contracts

Onerous contracts are those contracts for which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. Unavoidable costs under a contract are the least net cost of exiting the contract (that is, the lower of the cost to exit or breach the contract and the cost of fulfilling it). Such contracts might include, for example, supply contracts that the entity is able to fulfil only at a loss because of the invasion. Management should consider whether any of its contracts have become onerous.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 9.2.1 – How should payments in relation to termination of contracts be dealt with in the financial statements?

9.3. Contingent assets

One of the steps taken in response to the Russian invasion of Ukraine is that some entities are making decisions to temporarily close their businesses in Russia, Ukraine or neighbouring countries. An entity might have business continuity insurance and be able to recover some or all of the costs of closing. Management should consider whether the losses arising from the closure of businesses are covered by its insurance policies. The benefit of qualifying insurance reimbursement is recognised when the recovery is virtually certain. This is typically when the insurer has accepted that there is a valid claim and management is satisfied that the insurer can meet its obligations. Insurer acceptance of the claim will in many cases be crucial, because many insurance contracts include provisions that do not cover the beneficiary for losses as a result of acts of war.

The benefit of insurance is often recognised later than the costs for which it compensates.

Similarly, any insurance claims for property damaged or destroyed as a result of the invasion would be recognised when the recovery is virtually certain.

9.4. Employee benefits and share-based payments

Management should consider whether any of the assumptions used to measure employee benefits and share-based payments should be revised. For example, the yield on high-quality bonds or the risk-free interest rate in territories affected by the invasion (for example, Russia) might have changed as a result of recent developments, or the probability of an employee meeting the vesting conditions for bonuses or share-based payments might have changed.

Management should consider the impact of any changes made to the terms of, for example, a share-based payment plan, to address the changes in the economic environment and the likelihood that performance conditions will be met. To the extent that such changes are beneficial to the employee, they would be accounted for as a modification and an additional expense would be recognised. Management should be aware that cancelling a share-based payment award, even if the vesting conditions are unlikely to be satisfied, results in immediate recognition of the remaining expense.

Management should also consider whether it has a legal or constructive obligation to its employees in connection with the invasion (for example, additional leave days granted or additional financial, or other, assistance provided to employees) for which a liability should be recognised in accordance with the guidance in IAS 19 *'Employee benefits'*.

Management might be considering reducing its workforce as a result of the invasion. IAS 19 requires a liability for employee termination to be recognised only when the entity can no longer withdraw the offer of those benefits, or the costs of a related restructuring are recognised in accordance with IAS 37.

IFRS 2, 'Share-based payment', requires entities to explain modifications to share-based payments, the incremental fair value granted, as well as information about how the incremental fair value was determined.

IAS 19 requires extensive disclosure of the assumptions used to estimate employee benefit liabilities, together with sensitivities and changes in those assumptions.

For consideration on the determination of the defined benefit obligation and the fair value of the plan assets and the related expense for interim periods in accordance with IAS 34, please refer to the FAQ 12.3 and FAQ 12.4 in the Interim Financial Statements Section.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 9.4.1 – Is an announcement of a restructuring plan to some of those parties affected by the plan sufficient to recognise a liability for the total expected restructuring provision?

FAQ 9.4.2 - How should change in settlement of equity awards to Russian employees be accounted for?

9.5. income taxes

The Russian invasion of Ukraine could affect future profits as a result of direct and indirect factors (including effects on customers, suppliers and service providers). Asset impairment could also reduce the amount of deferred tax liabilities and/or create additional deductible temporary differences. Entities with deferred tax assets should reassess forecast profits and the recoverability of deferred tax assets in accordance with IAS 12, *'Income taxes'*, taking into account the additional uncertainty arising from the invasion and the steps taken to control it.

Management might also consider whether the impact of the invasion affects its plans, and ability, to distribute profits from subsidiaries and, therefore, whether it needs to reconsider the recognition of any deferred tax liability in connection with undistributed profits. Management's decision to exit certain markets may also need to be taken into account in this regard.

Management should disclose any significant judgements and estimates made in assessing the recoverability of deferred tax assets, in accordance with IAS 1.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 9.5.1 – What should a company consider when assessing the recoverability of its deferred tax assets in the current environment?

FAQ 9.5.2 – What other potential tax accounting implications may companies encounter as a result of the invasion?

10. Going concern and events after the reporting period

10.1. Going concern

Management should consider the potential implications of the Russian invasion of Ukraine and the measures taken in response to it when assessing the entity's ability to continue as a going concern. An entity is no longer a going concern if management intends either to liquidate the entity or to cease trading, or it has no realistic alternative but to do so. Management should consider the impact of measures taken by global organisations, governments and global payment systems in its assessment of going concern as well as the impact of disruptions to supply chains and access to customers and/or goods. Management should also remember that events after the reporting date that indicate that an entity is no longer a going concern are always adjusting events from a going concern perspective.

Material uncertainties that might cast significant doubt on an entity's ability to continue as a going concern should be disclosed in accordance with IAS 1.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 10.1.1 – What timeframe should management consider when assessing going concern?

FAQ 10.1.2 – How does an entity prepare financial statements on a non-going concern basis?

FAQ 10.1.3 – How should the requirements in IAS 1 regarding the going concern assumption be applied?

10.2. Events after the reporting period

The geopolitical situation is evolving rapidly. Management should therefore consider the requirements of IAS 10, *'Events after the reporting period'*, and in particular whether the latest developments provide more information about the circumstances that existed at the reporting date. Events that provide more information about the escalation of the invasion might be adjusting events. Clear disclosure of adjustments made and events that are considered to be non-adjusting is required where this is material to the financial statements.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 10.2.1 – Should the effects of the Russian invasion of Ukraine impact the measurement of assets and liabilities for entities with a reporting date in the first quarter of 2022?

FAQ 10.2.2 – Adjusting events affecting impairment calculations related to non-financial assets with a measurement basis other than fair value

FAQ 10.2.3 – Adjusting events affecting remeasurement/impairment calculations related to assets with a measurement basis of fair value

11. Presentation and disclosure

11.1. Presentation of financial statements

An entity might consider several presentation alternatives within the financial statements to provide useful information in relation to the Russian invasion of Ukraine. Entities should ensure that any presentation alternative complies with IAS 1's requirements. In some cases, it might be more helpful to provide narrative explanations of the impact within the notes.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 11.1.1 – Presentation of the impact of the Russian invasion of Ukraine in the income statement

11.2. Breach of covenants

Companies may experience significant liquidity issues, changes in debt/equity ratios and changes in other financial metrics as a result of the Russian invasion of Ukraine. This might call into question whether the company complies with its debt covenants. The financial impact of the invasion, subsequent sanctions and resulting economic crisis might cause some entities to breach covenants on borrowings, or it might trigger material adverse change clauses. In addition, assets backing collateralised borrowings may have been destroyed or damaged.

This could result in loan repayment terms changing and some loans becoming repayable on demand. Management should consider whether the classification of loans and other financing liabilities between non-current and current is affected and, in extreme situations, whether the entity remains a going concern. Management should consider particularly the impact of any cross-default clauses. Management should also consider the effect of any changes in the terms of borrowings as a result of the circumstances described above.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 11.2.1 – How should loans with material adverse change and subjective acceleration clauses be classified?

FAQ 11.2.2 – What should a company consider if it expects a debt covenant violation after the balance sheet date?

11.3. General disclosures

Management should consider the specific requirements in IAS 1 to disclose:

- significant accounting policies;
- the most significant judgements made in applying those accounting policies; and
- the estimates that are most likely to result in an adjustment to profits in future periods.

All these disclosures might be different as a result of the impact of the invasion. The extent of disclosures regarding estimation uncertainty might need to be increased. For example, the carrying amount of more items might be subject to a material change within the next year.

There might be individually significant financial effects of the invasion – for example, individually material expenses such as an impairment or a modification adjustment. In addition to the disclosure requirements of individual standards, IAS 1 requires an entity to disclose separately on the face of the income statement, or in the notes to the financial statements, material items of income or expense. An entity might also disclose additional line items or sub-totals on the face of the income statement where this is necessary for an understanding of performance. Management should consider the specific requirements of IAS 1 if it discloses

additional subtotals (refer to FAQ 11.1.1). There is also a requirement in IAS 1 to disclose information relevant to an understanding of the financial statements that is not otherwise disclosed.

11.4. Disclosure outside the financial statements

An entity's stakeholders will be interested in the impact of the Russian invasion of Ukraine and the subsequent sanctions. Some of these stakeholders' needs might be met more appropriately or timely by communication outside the financial statements. For example, management might consider updating its analysis of the principal risks and uncertainties. Management should also consider any specific local disclosure requirements, such as those issued by a local securities regulator.

Regardless of the reason for providing additional information outside of the financial statements, entities should ensure that information provided within and outside of the financial statements is consistent and complementary.

12. Interim financial statements

Many entities might first report the impact of the Russian invasion of Ukraine in interim financial statements. The recognition and measurement guidance described above applies equally to interim financial statements. There are typically no recognition or measurement exceptions for interim reporting, although management might have to consider whether the impact of the Russian invasion of Ukraine is a discrete event for the purposes of calculating the expected effective tax rate. IAS 34, *'Interim financial statements'*, states that there might be greater use of estimates in interim financial statements, but it requires the information to be reliable and all relevant information to be disclosed.

Interim financial information usually updates the information in the annual financial statements. However, IAS 34 requires an entity to include in its interim financial report an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the entity since the end of the last annual reporting period. This implies that additional disclosure should be given to reflect the financial impact of the Russian invasion of Ukraine. This disclosure should be entity-specific and should reflect each entity's circumstances.

Where significant, the disclosures required by paragraph 15B of IAS 34 should be included, together with:

- the impact of the Russian invasion of Ukraine on the entity's results, balance sheet and cash flows;
- significant judgements that were not required previously (for example, in connection with expected credit losses);
- updates to the disclosures of significant estimates; and
- events since the end of the interim period.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 12.1 – What is the impact on impairment testing of providing financial information (such as a Q1 trading update) during the year but not in accordance with IAS 34?

FAQ 12.2 – How should an entity estimate the weighted average annual effective income tax rate?

FAQ 12.3 – What are the implications of the Russian invasion of Ukraine for the net defined benefit liability when reporting under IAS 34?

FAQ 12.4 – What are the implications of the Russian invasion of Ukraine for the pension expense when reporting under IAS 34?

13. The effects of changes in foreign exchange rates

Entities may conduct business with Russia in two main ways. First, entities might enter into transactions in foreign currencies (such as buying goods and services from Russian suppliers and selling to overseas customers). Secondly, they might conduct business through Russian subsidiaries, branches and joint arrangements. In addition, an entity might present its financial statements in a foreign currency. IAS 21 sets out requirements for each of the above.

Companies that have interests in Russia or Russian customers and suppliers are likely to be the most severely impacted by sanctions, which could in turn impact the accounting under IAS 21. A variety of sanctions have been introduced, and entities should consider the implications of each sanction and restriction on their financial and operational performance.

13.1. Foreign currency transactions

The introduction of sanctions and restrictions on Russia has resulted in significant volatility in the exchange rates for the Rouble. In particular, the restrictions against the Russian Central Bank are likely to limit the ability of Russia to stabilise the exchange rate of the Rouble and may impact the ability to exchange Roubles for other currencies.

Exchange rate volatility has an impact on the exchange rates used to translate income statement amounts. An average rate that approximates the actual rate at the date of transaction can be used for practical reasons. However, the use of an average rate may no longer be appropriate if exchange rates fluctuate significantly.

Closing exchange rates must be spot rates at the balance sheet date, and any post balance sheet movements in these rates are considered non-adjusting events.

IAS 21 requires the use of closing rates. In determining whether a rate is a closing rate, an entity should consider whether currency is obtainable at an official quoted rate and whether the quoted rate is available for immediate delivery. In practice, a normal administrative delay in obtaining funds would be acceptable.

Entities will need to consider whether quoted rates are available. For example, as of 1 March 2022, the European Central Bank (ECB), has suspended the publication on its Euro - Rouble exchange rate.

Where exchangeability between two currencies is temporarily unavailable at a transaction date or a subsequent balance sheet date, paragraph 26 of IAS 21 requires entities to use the rate on the first subsequent date at which exchanges could be made. The IFRS IC also previously considered the lack of exchangeability of currencies in Venezuela and also observed that any significant restrictions on the ability to access or use assets and settle liabilities of operations should be disclosed in accordance with paragraphs 20 and 22 of IFRS 12.

In addition, following the volatility of the exchange rate for the Rouble, entities may need to consider any potential impairment of the translation of non-monetary items. For value-in-use calculations, future cash flows are estimated in the currency in which they will be generated and then discounted using a discount rate appropriate for that currency. An entity then translates the present value using the spot exchange rate at the date of the value in use calculation [IAS 36 para 54].

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 13.1.1 – What are the factors to consider in light of sanctions on the Russian Central Bank when determining the spot rate for the Rouble under IAS 21 as at 31 March 2022?

13.2. Foreign operations and consolidated financial statements

Where foreign activities are undertaken through foreign operations, the financial statements of those foreign operations are translated so that they can be included in the reporting entity's financial statements by consolidation or the equity method. The process of translation addresses the appropriate exchange rates to use for translating the income statement and the balance sheet of the foreign operation. It also addresses how the financial effects of changes in exchange rates are recognised in the reporting entity's financial statements.

Parent companies typically use the dividend remittance rate to translate the net assets of a foreign operation, because this is usually the rate that would apply if funds from the foreign operation were remitted to the parent at the reporting date. However, the ability to exchange in Roubles may impact which exchange rate is used.

Any significant accounting policies and judgements made in determining the rate should be disclosed in accordance with the requirements in paragraphs 117 to 124 of IAS 1 *'Presentation of financial statements'*.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 13.2.1 – When would it be inappropriate to use an average exchange rate to translate a foreign subsidiary?

FAQ 13.2.2 – What are the relevant considerations when translating foreign operations with a Rouble functional currency as at 31 March 2022 into another currency for consolidation purposes?

13.3. Impairment and disposals of foreign operations, assets and liabilities

The invasion could result in de-consolidation, disposal or the abandonment of Russian operations, which may in turn result in the recognition of possible discontinued foreign operations, or foreign assets held for sale (refer to section 3.7 and section 3.8). The disposal or abandonment of a foreign operation could trigger an impairment of underlying assets and liabilities in the consolidated financial statement (refer to section 3.1).

A disposal of a foreign operation would result in the reclassification of the cumulative translation adjustment (CTA) that has been recorded in equity attributable to that subsidiary. Disposals might occur either through sale, liquidation, repayment of share capital or a quasi-equity loan, or abandonment of all (or a part) of the entity. A partial disposal is a reduction in an entity's 'ownership interest' in a foreign operation, other than loss of control, significant influence or joint control.

However, an impairment of the carrying amount of a foreign operation, which might arise as a result of a liquidation or abandonment, does not constitute a partial disposal. CTA is not reclassified to profit or loss at the time of the impairment.

As the implications of the sanctions and the impact on exchange rates continue to evolve, entities should carefully monitor the situation and how it impacts foreign currency translation/exchanges.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

EX 13.3.1 – Summary of disposals, partial disposals and effect on cumulative translation adjustment

FAQ 13.3.2 – Will an impairment loss arise in an entity's functional currency if there is an impairment loss on a foreign currency asset when measured in the foreign currency?

EX 13.3.3 – Translation of an impaired foreign asset

13.4. Disclosures in the financial statements

In accordance with IFRS 7, entities should disclose their sensitivity to market risks which will include foreign exchange rates. The sensitivity analysis should show the effect of changes over the period until the entity next presents these disclosures, which is usually its next annual report. This disclosure is based on reasonably possible changes and not on a 'worst case scenario' or 'stress test'.

In addition, entities should disclose the methods and assumptions used in preparing the sensitivity analysis, and changes from the previous period in the methods and assumptions used and the reasons for such changes.

Relevant guidance: (available on Viewpoint.pwc.com free - registration required)

FAQ 13.4.1 – Should prior year sensitivity disclosures under IFRS 7 be restated if the magnitude of reasonably possible change is different?

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