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In this issue:

Accounting and financial reporting implications of the military conflict in Ukraine

We highlight some of the accounting and financial reporting implications of the military conflict in Ukraine for the consideration of audit committees (ACs).

On 24 February 2022, the military conflict between Russia and Ukraine started. As a result, a number of countries, including Singapore, have imposed new sanctions against Russian government entities, state-owned enterprises and certain specified entities and individuals linked to Russia anywhere in the world. Sanctions have also been imposed on Belarus. These events have far-reaching effects on trade, capital markets and company operations, and companies need to take into account the accounting and financial reporting implications of the military conflict and its ripple effects.

ACs play an important oversight role in ensuring that these implications are adequately considered and appropriately disclosed in the financial statements where relevant.

In this issue, we highlight some implications for ACs' consideration.

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Accounting and financial reporting implications of the military conflict in Ukraine

On 24 February 2022, the military conflict between Russia and Ukraine started. As a result, a number of countries, including Singapore,[1] have imposed new sanctions against Russian government entities, state-owned enterprises and certain specified entities and individuals linked to Russia anywhere in the world. Sanctions have also been imposed on Belarus.

This situation – together with potential fluctuations in commodity prices, foreign exchange rates, restrictions to imports and exports, availability of local materials and services, and access to local resources – has far-reaching effects on trade, capital markets and company operations, and companies need to take into account the accounting and financial reporting implications of the military conflict and its ripple effects.

AC members overseeing the company's financial reporting and audit processes play a key role in managing the risk of material misstatement to the company's financial statements due to the omission and/or inappropriate consideration and disclosure of these financial reporting implications. In this issue, we highlight some accounting and financial reporting implications for ACs' consideration in respect of year-end and interim reporting that may be affected.

1 In February and March 2022, a number of countries (including Australia, EU, Japan, Singapore*, UK, US and others) imposed new sanctions against Russian government entities, state-owned enterprises or sanctioned entities and individuals linked to Russia anywhere in the world and announcements of potential additional sanctions followed military operations in Ukraine initiated on 24 February 2022. Subsequently, new sanctions have been imposed. Sanctions have also been imposed on Belarus. "Sanctions and Restrictions Against Russia in Response to its Invasion of Ukraine," Ministry of Foreign Affairs, Singapore, 5 March 2022.

- While most companies would likely have limited direct exposure to the Russian, Belarus and Ukrainian economies, the indirect effects of the military conflict and the impact of sanctions and other actions on Russian and Belarusian entities and their affiliates are likely to have an impact on companies' year-end and interim accounting and reporting matters. In some cases, this impact may be material. The indirect effects may include fluctuations in energy, oil and gas and other commodities prices, foreign exchange rates, supply disruptions for certain raw materials and component parts due to trade restrictions, and funding flow and transactions restrictions with certain counterparties due to sanctions. There is also a heightened risk of a protracted economic downturn as a result of the situation. These direct impacts and indirect effects would be considered adjusting events that represent conditions that exist on year-end or interim reporting dates on or after 24 February 2022 that need to be taken into consideration in the recognition, measurement and disclosure of the company's assets, liabilities, income, expenses and cash flows. As the situation continues to evolve, there may be additional events and impacts, and judgment would be required to determine if they are adjusting or non-adjusting events for the relevant reporting date.

  There could be implications to the company's going concern assessment and related disclosure made up to the date when the year-end or interim financial statements are issued. Companies would need to critically evaluate whether the direct impacts and indirect effects of the military conflict in Ukraine and resulting sanctions could adversely affect the company's sources of operating, investing or financing cash flows or threaten the viability of certain continuing operations that impede the company's ability to continue as a going concern. Even when the use of the going concern assumption remains appropriate, the ongoing events and their effects on the company may give rise to a related material uncertainty that warrants disclosure in the financial statements.

- Fair values and related disclosures of investment securities that have direct exposure to the Ukraine, Russia or Belarus markets and related sanctions are expected to be significantly impacted. Indicators of impairment or doubts on recovery also likely exist for entities that have property, plant and equipment, goodwill, other intangible assets, equity method investments, financial assets and receivables measured at amortized cost, inventories and deferred tax assets in Ukraine, Russia or Belarus or have activities in these countries or cash flows that are dependent on activity in these countries. These companies will need to consider how the military conflict, or changes in their business strategy in Russia and Belarus, changes their projections of future cash flows and other significant assumptions (e.g., discount rates) used in testing for impairment or recoverability, estimating expected credit losses, determining if certain costs can be capitalized, or determining fair value. In certain cases, companies may conclude that the assets previously held for ongoing use may now be classified as held for sale or abandoned, and the restructuring of operations and related provisions may be needed. There could also be potential loss of control, joint control or significant influence of certain group components due to sanctions or lack of access to management of the group components that lead to significant accounting implications.

- The indirect effects of the military conflict in Ukraine such as fluctuations in energy and commodities prices, supply chain disruptions and ensuing economic uncertainty could also be indicators of impairment for a company's non-financial assets, drivers of downward fair value adjustments or risk premiums for assets, evidence of significant increase in credit risk, or triggers for recognition of onerous contract provisions, if they are expected to adversely impact future cash flows and financial performance.

Sanctions can directly impact those entities and individuals, and entities under their control. Business counterparties of such sanctioned entities and individuals may also be indirectly impacted, as well as certain industries in the Russian and Belarusian economies.

- There is also likely an impact on the exchange rates used to account for foreign currency transactions and translation of financial statements. Companies that hold Russian or Belarusian Rubles or Ukrainian Hryvnia denominated monetary and non-monetary financial instruments or investments could experience significant impact on the carrying values of these items.
- Companies that have contracts to lease assets such as aircraft, real estate, shipping vessels and telecommunication equipment should monitor events that may indicate that a lease has been terminated or modified and that the lease-related assets may be impaired. Further, companies should monitor any laws or regulations governing their contracts to determine whether there are impacts. These impacts on and modifications to contracts and leases could have significant accounting implications requiring further analysis. The supply chain, commodities markets and revenue arrangement disruptions brought about by the military conflict in Ukraine may also impact hedges entered into by companies and contracts with customers, and give rise to issues surrounding the continuity of hedge accounting, assessment of contractual terms, collectivity and estimates used in revenue recognition.
- Companies are required to make financial statements disclosures about certain risks and uncertainties, including quantitative and/or qualitative disclosures about risks, uncertainties and the range of reasonably possible outcomes that in the near term could significantly affect the amounts reported in the financial statements or the functioning of the reporting entity. Companies whose operations are affected by the current environment may be required to disclose certain significant judgments, estimates, changes in assumptions, and their sensitivity and current vulnerability due to concentrations (e.g., concentration in the volume of business with a particular customer or supplier or in a market or geographic area). Potential supply chain disruptions, viability of business operations and transactions threatened by economic sanctions and any retaliatory actions of Russia or Belarus may also warrant disclosure to help users of financial statements understand the judgments applied in the financial statements.
- In respect of interim reporting, the direct and indirect effects of the military conflict in Ukraine may require companies to provide related disclosures and explanation of the events and transactions if they are significant to an understanding of the changes in the financial position and performance of the entity since the end of the last annual reporting period. Updates to relevant information such as affected fair value and impairment estimates presented in the most recent annual financial report may also be required.

As the current situation evolves and the conditions remain uncertain and unpredictable, at this stage, management is required to exercise significant judgment to assess and determine the accounting implications based on the conditions existing at each year-end and interim reporting dates.

Concluding remarks

- While the year-end and interim accounting and financial reporting implications of the military conflict in Ukraine, resulting sanctions and ripple effects that are briefly shared in this article can help AC members in their engagement with the management and auditors, they are not intended to be exhaustive and comprehensive. There could be additional implications and considerations depending on the unique facts and circumstances of each company, and the further developments that may unfold when this fluid situation evolves. Further details on the accounting considerations for the military conflict in Ukraine can be found in the EY publication, *Applying IFRS - Accounting considerations for the war in Ukraine (updated March 2022)*, which provides a reminder of some of the existing accounting requirements that should be considered when addressing the financial reporting effects of the conflict for the annual or interim periods ending after 24 February 2022.
- Companies must also ensure that they have both robust internal controls over financial reporting and disclosure controls and procedures so that they can identify, in a timely manner, accounting and reporting implications and disclose material information related to the military conflict, the sanctions or the ripple effects.
- In this regard, companies listed on the Singapore Exchange (SGX) should also note that the SGX RegCo has issued a set of guidance notes[2] on what an issuer should do if the issuer, or any person or entity closely associated with the issuer, is exposed to sanctions-related risks. Financial institutions subject to the Monetary Authority of Singapore (MAS) Act 1970 must also comply with the MAS' notice regarding financial measures in relation to Russia issued in March 2022.[3]

2 "Regulator's Column - What SGX expects of issuers in respect of sanctions-related risks, subject or activity," SGX RegCo, 7 March 2022.

3 "Notice to Financial Institutions: Financial measures in relation to Russia," Monetary Authority of Singapore, 14 March 2022.

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