

Technical Line

Accounting and reporting considerations for the war in Ukraine

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What you need to know

- ▶ Companies need to consider the accounting and financial reporting implications of the war in Ukraine, the sanctions on Russia and the ripple effects.
- ▶ While many companies have limited direct exposure to the Russian and Ukrainian economies, they may be indirectly affected by supply chain disruptions, rising prices for oil and other commodities, volatility in capital markets and foreign currency exchange rates, rising interest rates, or heightened cybersecurity risks. The potential effect on an entity's accounting and disclosures will depend on its facts and circumstances.
- ▶ Management should determine whether the entity's controls are sufficient to identify and assess the impact, given the uncertainty about how widespread the economic effects will be.
- ▶ Affected SEC registrants may need to make additional disclosures.

Overview

Companies need to consider how their accounting and financial reporting are affected by the war in Ukraine, the sanctions on Russia and the ripple effects of the war.

The ramifications are far reaching and affect global trade and capital markets, in addition to companies' operations and risk management activities. The war and its ripple effects are also impacting people and operations not only in Ukraine and Russia but in many other countries. Most companies likely have limited direct exposure to the Russian and Ukrainian economies, but the indirect effects could have a meaningful impact on accounting and reporting matters.

These effects include the increases in oil and gas prices and supply disruptions for certain raw materials and component parts, which are fueling inflation and may accelerate interest rate hikes by central bankers. The impact will vary by company, and management will need to consider the company's facts and circumstances.

The potential financial statement reporting effects may be account specific or may be more widely associated with broad transactions (e.g., disposal of operations in Ukraine or Russia). Companies should review all accounts and related disclosures for potential impacts. Timely engagement and discussion across the organization are critical to the evaluation.

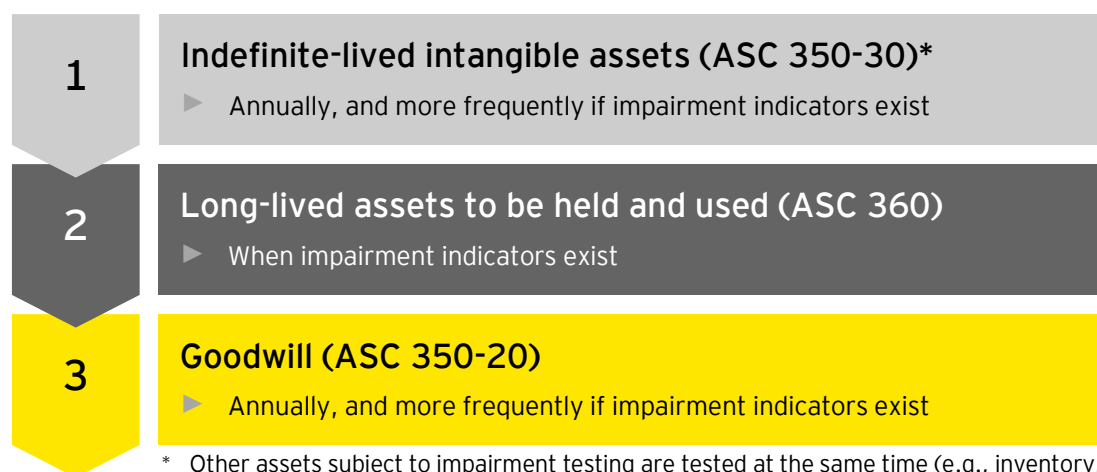
Below we discuss some accounting, disclosure and Securities and Exchange Commission (SEC) reporting considerations that may be relevant in the current environment. For more information about the topics discussed throughout this Technical Line, refer to the list of our publications in the Appendix.

Accounting considerations

Asset impairments

Indicators of impairment likely exist for entities with long-lived assets (asset groups), goodwill, equity method investments or certain financial assets measured at amortized cost in Ukraine or Russia, or for those assets that are supported by cash flows that are dependent on activity in those countries. These entities will need to consider whether the war alters their projections of future cash flows (either discounted or undiscounted) and other significant assumptions (e.g., discount rates) used in testing for impairment or determining fair value. In certain cases, companies may conclude that the assets previously classified as held and used may now be classified as held for sale or abandoned.

If a company identifies impairment indicators that require it to perform impairment tests, the company needs to make sure it performs those tests in the appropriate order. When assets are classified as held and used, indefinite-lived intangible assets are tested first for impairment in accordance with Accounting Standards Codification (ASC) 350, *Intangibles – Goodwill and Other*. Groups of long-lived assets are then tested for impairment in accordance with ASC 360, *Property, Plant, and Equipment*. Goodwill is tested for impairment last, and those tests are performed at the reporting unit level. These steps are summarized in the graphic below.



* Other assets subject to impairment testing are tested at the same time (e.g., inventory, equity method investments).

However, when a disposal group is held for sale, the order of impairment testing differs from what is shown in the graphic shown above; more information about disposal groups that are held for sale can be found in our Financial reporting developments (FRD) publication, [*Impairment or disposal of long-lived assets*](#).

Affected companies will need to consider whether indicators of impairment exist for a variety of assets.

Goodwill and other indefinite-lived intangible assets

Goodwill and indefinite-lived intangible assets are tested for impairment at least annually and more frequently if events or changes in circumstances indicate that it is more likely than not that the asset is impaired. ASC 350 provides examples of events and circumstances that should be considered in evaluating whether an interim impairment test is required for both goodwill and indefinite-lived intangible assets. To determine whether an interim impairment test is required, companies will need to consider the potential effects of the war, sanctions and other current economic conditions on the fair value measurement of their reporting units and indefinite-lived intangible assets. The current economic environment, including capital market volatility, effects of inflation, rising interest rates and disruption in operations, should be considered in determining whether an interim impairment test is required.

Refer to our FRD, [*Intangibles – Goodwill and other*](#), for more information.

Long-lived assets

Long-lived assets to be held and used

Long-lived assets to be held and used (including right-of-use assets under ASC 842, *Leases*) are tested for impairment when factors are present that indicate that the recorded value of a long-lived asset or asset group may not be recoverable. Estimated undiscounted cash flows for a long-lived asset or asset group being evaluated for recoverability are compared with the carrying amount of that asset or asset group. An entity that determines that the carrying amount is not recoverable (i.e., the carrying amount of the long-lived asset or asset group exceeds the estimated undiscounted cash flows) is required to determine the fair value of the long-lived asset or asset group and recognize an impairment loss if the carrying amount of the long-lived asset or asset group exceeds its fair value.

Long-lived assets to be disposed of by other than sale (e.g., abandoned)

A long-lived asset or asset group to be abandoned is classified as held and used until disposal (abandonment). While an asset or asset group is classified as held and used, companies should determine whether their depreciation estimates must be revised (in accordance with the change in estimate guidance in ASC 250, *Accounting Changes and Error Corrections*) to reflect a useful life that is shorter than initially expected and a salvage value, if any, consistent with the intention to abandon. Because a decision to abandon a long-lived asset or asset group is akin to a decision to dispose of a long-lived asset or asset group before the initially intended date, it generally would be viewed as an indicator of impairment for a held and used long-lived asset.

Some companies have temporarily halted operations in Russia and Ukraine. A long-lived asset or asset group that has been temporarily idled should not be accounted for as if abandoned. However, similar to the decision to abandon a long-lived asset or asset group, temporarily halting operations that are unplanned would be viewed as an indicator of impairment for a held and used long-lived asset.

The complete destruction of a long-lived asset results in the write-off of that asset rather than an impairment. That is because the complete destruction of an asset is effectively a disposal of the asset.

Long-lived assets to be disposed of by sale

Some companies have announced their intention or plans to sell their operations in Russia as a result of the war and related sanctions. A long-lived asset or disposal group classified as held for sale is initially measured at the lower of its carrying amount or fair value less cost to sell. A long-lived asset or disposal group to be disposed of by sale (including an asset group considered a component of an entity) is considered held for sale when certain criteria for a qualifying plan of

sale are met. However, given the uncertainty associated with the current economic environment, it may be difficult for entities to meet all of the held-for-sale criteria (e.g., active program to locate a buyer, the ability to sell within one year).

Refer to our FRD, *[Impairment or disposal of long-lived assets](#)*, for more guidance.

If the disposal of a component of an entity, including components that are abandoned or classified as held for sale, represents a strategic shift that has or will have a major effect on a company's operations and financial results, the company should consider the discontinued operations guidance in ASC 205-20, *Presentation of Financial Statements – Discontinued Operations*.

Refer to our FRD, *[Discontinued operations – ASC 205-20](#)*, for more guidance.

Inventory

Net realizability

If there is a decline in the net realizable value or utility of inventory, ASC 330, *Inventory*, requires the decline to be recognized as a charge in the period in which it occurs. A loss may result from complete destruction, abandonment, damage, contamination, physical deterioration, obsolescence, changes in price levels or other causes.

Companies whose supply chains have been disrupted or whose sales have fallen because of the current trade sanctions and other market conditions should evaluate whether they need to adjust the carrying value of their inventory. Given the uncertainty of the current economic environment, determining the market price of some inventory may be challenging.

Entities also should consider the requirements in ASC 270, *Interim Reporting*, to determine whether to write down inventory as of an interim date. Any loss should not be deferred beyond the interim period in which the decline occurs unless the decline can reasonably be expected to be restored within the same fiscal year. While temporary declines in the market or value of inventory that can reasonably be expected to be restored by the end of the fiscal year need not be recognized at the interim date, this may be a difficult judgment to make, given the uncertainty associated with the current economic environment. If inventory is written down, any subsequent recovery of recognized losses in the same fiscal year should be reflected as a gain, but any gain should not exceed the previously recognized losses.

Firm purchase commitments for inventory

Companies must consider whether firm, noncancelable and unhedged purchase commitments for a future purchase of inventory are impaired. Any net loss should be measured in the same manner as inventory.

Changes in manufacturing levels and excess capacity

Unplanned work stoppages, labor or material shortages, or production bottlenecks could cause production levels to drop below normal capacity levels. If this happens, a company will need to consider the effects on its inventory costing. The amount of fixed overhead allocated to each unit of production is not increased when production is abnormally low, and the costs associated with underutilized capacity (known as excess capacity costs) are expensed in the period they are incurred without adjusting overhead absorption rates.

Companies will need to use judgment to determine when production is lower than normal capacity. The range of normal capacity can vary based on business and industry-specific factors. Examples of factors that might cause an abnormally low production level include unplanned facility or equipment downtime.

Entities should evaluate whether certain costs, including those resulting from supply chain disruptions (e.g., excessive spoilage, double freight, rehandling costs) meet the criteria to be capitalized under ASC 330-10-30 or whether they should be expensed as incurred.

Equity method investments

Equity method investments (including investments in joint ventures) are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the investment might not be recoverable in accordance with ASC 323, *Investments – Equity Method and Joint Ventures*. Evidence that could indicate the carrying amount of the investment might not be recoverable includes:

- ▶ The investor does not have the ability to recover the carrying amount of the investment.
- ▶ The investee cannot sustain earnings.
- ▶ The current fair value of the investment is less than the carrying amount.
- ▶ Other investors have ceased providing support or reduced their financial commitment to the investee.

Entities should consider whether current conditions and the current economic environment represent changes in circumstances that require an impairment assessment for equity method investments.

If there has been a significant decline in the value of an investee, an investor would need to exercise judgment to determine whether the decline is other than temporary. This aspect of the test differs from other impairment tests, such as those for goodwill and indefinite-lived intangible assets under ASC 350, that don't require consideration of whether an impairment is temporary. When an investor has the intent and ability to recover the carrying amount of the investment over a long period (e.g., from cash flows from the investee), the investor still must evaluate whether that recovery will occur in the near term. If the fair value of the investment is less than its carrying amount and the investment will not recover in the near term, an other-than-temporary impairment may exist. There is no "bright line" or "safe harbor" in either the duration or severity of an impairment to indicate whether it is other than temporary.

An impairment loss is recognized for a decrease in value of an investment that is other than a temporary decline. The investment is recorded at its fair value (i.e., the impairment is measured as the difference between its carrying amount and fair value). ASC 820, *Fair Value Measurement*, provides guidance for measuring fair value. See the *Fair value measurement* section below for more guidance on determining fair value and the required disclosures.

If there is a change in how decisions about the significant operating and financial policies of an investee are made, an investor should evaluate the facts and circumstances to determine whether it continues to have significant influence over the equity method investee.

Refer to our FRD, [***Equity method investments and joint ventures***](#), for more guidance.

Equity securities measured using the measurement alternative

For equity securities measured using the measurement alternative in ASC 321, *Investments – Equity Securities*, entities are required to perform a qualitative impairment assessment. Impairment indicators that an entity needs to consider include a significant deterioration in earnings, a significant adverse change in the economic environment of the investee, or a significant adverse change in the general market condition of the geographical area or industry in which the investee operates. If a qualitative assessment indicates that the investment is impaired, and if the investment's fair value is less than its amortized cost basis, the excess of the amortized cost basis over fair value is recognized as an impairment loss.

Refer to our FRD, [*Certain investments in debt and equity securities*](#), for additional information.

Investments in debt securities

Entities that hold debt securities that are not measured at fair value with changes in the fair value of the securities recognized in net income are required to assess at each reporting date whether to recognize an impairment loss.

The new credit impairment guidance (ASC 326, *Financial Instruments – Credit Losses*) provides separate credit loss models for held-to-maturity (HTM) and available-for-sale (AFS) debt securities in ASC 326-20 and ASC 326-30, respectively. For HTM debt securities and certain other financial assets, entities are required to estimate expected credit losses. For AFS debt securities, entities are required to recognize an allowance for credit losses instead of an other-than-temporary impairment that reduces the cost basis of the investment. These models are discussed in more detail below.

This guidance is currently effective for public business entities that are SEC filers that are not smaller reporting companies. For all other entities, the guidance is effective for fiscal years beginning after 15 December 2022, including interim periods within those fiscal years.

Accounting for impairment of AFS and HTM debt securities (after the adoption of ASC 326)

An AFS debt security is considered impaired if its fair value is less than its amortized cost basis. If an entity intends to sell an impaired AFS debt security or more likely than not will be required to sell the security before recovering its amortized cost basis, the entire impairment amount is recognized in earnings with a corresponding adjustment to the security's amortized cost basis.

An entity that does not intend to sell an impaired AFS debt security and is not more likely than not to be required to sell the security prior to recovery of its amortized cost basis must determine whether any impairment is attributable to credit-related factors. Management may not use the length of time an AFS debt security has been in an unrealized loss position as a factor, either by itself or in combination with other factors, to conclude that a credit loss does not exist. If any impairment is attributable to credit-related factors, an entity must measure the credit loss and recognize an allowance for credit losses along with the related charge to earnings. The amount of the allowance is limited to the difference between the security's amortized cost basis and its fair value. Further, any improvements in estimated credit losses on AFS debt securities are recognized immediately in earnings to the extent of the amount of any allowance and then prospectively as a yield adjustment.

In addition, after adopting ASC 326, entities account for impairment of HTM debt securities consistently with how impairment is recognized for loans and other financing receivables. See the discussion in the *Financing receivables and contract assets* section below for further discussion of this guidance.

Refer to our FRD, [*Credit impairment under ASC 326*](#), for additional information.

Accounting for impairment of AFS and HTM debt securities (before the adoption of ASC 326)

Entities that have not yet adopted ASC 326 recognize an impairment loss on an AFS or HTM security when the security is considered other than temporarily impaired (OTTI).

An AFS or HTM debt security is considered OTTI if its fair value is less than its amortized cost basis and (1) the entity has the intent to sell the security, (2) it is more likely than not that the entity will be required to sell the security or (3) the entity does not expect to recover the entire amortized cost of the security (i.e., a credit loss exists). ASC 320, *Investments – Debt and Equity Securities*, lists factors that an investor should consider to determine whether a credit

Volatility in global markets may affect the fair value of debt and equity securities.

loss exists and the period over which the security is expected to recover. These factors include the length of time and the extent to which the fair value has been less than the amortized cost basis and adverse conditions related to the security (e.g., any changes to the rating of the security by a rating agency), the issuer's industry or the geographic area where the issuer operates.

There is no "bright line" or "safe harbor" in either the duration or severity of an impairment to indicate whether it is other than temporary. As declines in fair value become more severe, an entity must do more analysis and collect more objective evidence to support an assertion that an OTTI does not exist. If an entity plans to sell an impaired debt security or it is more likely than not it will be required to sell prior to recovery of its amortized cost basis, the amortized cost basis of the security is written down to fair value and the loss is recognized in earnings. If an entity does not intend to sell an impaired debt security and it is not more likely than not that it will be required to sell the security prior to recovery of the amortized cost basis, the OTTI amount representing the credit loss is recognized in net income, and the amount related to all other factors is recognized in other comprehensive income.

OTTI write-downs of a debt security cannot be immediately reversed. Any improvement in cash flows expected to be collected is recognized over the remaining life of the security as an adjustment to yield.

Financing receivables and contract assets

Entities with financing receivables (e.g., loans, trade accounts receivable) and contract assets should consider the guidance in ASC 326 (or ASC 310, *Receivables*, if they haven't yet adopted ASC 326) to evaluate whether and to what extent the war in Ukraine, sanctions on Russia and their ripple effects affect the collectibility of their financing receivables and contract assets.

Companies applying ASC 326 are required to consider reasonable and supportable forecasts of future economic conditions in the estimate of expected credit losses. Affected companies that apply ASC 326 will need to consider the degree to which the economic impact of these events changes their forecast of future economic conditions.

ASC 326 requires companies to pool financial assets but allows them to choose which risk characteristics to use. Affected companies need to assess whether assets in pools continue to display similar risk characteristics or determine whether they need to revise their pools or perform an individual assessment of expected credit losses.

There are significant uncertainties about what the effects of the war in Ukraine and the sanctions on Russia will ultimately be. Entities should consider highlighting these risks in their qualitative and quantitative disclosures about credit risk and the allowance for credit losses. They should also consider the disclosures related to the basis of inputs and assumptions and estimation techniques used, and how forward-looking information has been incorporated.

If an entity believes it is appropriate to incorporate in its expected credit loss model an input, assumption or forward-looking adjustment associated with the war in Ukraine and the sanctions on Russia, and if the effect of these is significant or it is otherwise useful to understand the uncertainty of future cash flows, the entity should disclose such an input, assumption or forward-looking adjustment.

Creditors of entities that are adversely affected by the war in Ukraine, sanctions on Russia or their ripple effects may modify the terms of financing arrangements. Creditors need to consider the guidance in ASC 310-40, *Receivables – Troubled Debt Restructurings by Creditors*, to determine whether such a modification is a troubled debt restructuring (TDR) if they have not yet adopted Accounting Standards Update (ASU) 2022-02, *Financial Instruments – Credit*

Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures, which eliminated the TDR guidance for creditors. Creditors that have adopted ASU 2022-02 should apply the guidance in ASC 310-20, *Receivables – Nonrefundable Fees and Other Costs*, to determine whether modifications should be accounted for as new lending arrangements or the continuation of the original arrangements and to determine the appropriate accounting for both unamortized origination fees and costs and any origination fees and costs for new loans.

Refer to our FRDs, [*Credit impairment under ASC 326*](#) and [*Credit impairment for short-term receivables under ASC 326*](#), for more information on measuring credit impairment after the adoption of ASC 326. Refer to our To the Point publication, [*FASB eliminates TDR guidance for creditors and requires enhanced vintage disclosures*](#), for more information on ASU 2022-02.

How we see it

When an affected company concludes that it has an impairment loss, the company should disclose the facts and circumstances leading to impairment. When other circumstances also contributed to an impairment loss, companies should be transparent about all material circumstances contributing to the impairment or loss.

Further, in response to sanctions placed on Russia by the US, the European Union and other countries, the Russian government has said it may nationalize assets of foreign investors that leave the country. Companies with operations in Russia should carefully monitor developments and any actions taken by the Russian government that could affect the recoverability or impairment of their assets.

Leases

Entities that have contracts to lease assets (e.g., aircraft, real estate, shipping vessels, telecommunication equipment) should monitor events that may indicate that a lease has been terminated or modified and the lease-related assets (e.g., the underlying asset for lessors of operating leases, a right-of-use asset for lessees) may be impaired. Lessees should also consider whether there have been events within their control that would result in a reassessment of an existing lease contract (e.g., a lessee may decide to exit certain properties and change its conclusion on whether it will exercise future lease renewal options). Further, entities should monitor any laws or regulations governing their contracts to determine whether there are impacts to their contracts (e.g., new governmental sanctions prohibiting or curtailing certain lease transactions may result in changes that impact the accounting for lease contracts).

While lessors follow the guidance on credit losses (i.e., ASC 310 or ASC 326, as applicable) to consider possible impairments of net investments in sales-type leases and direct financing leases, they need to follow the guidance in ASC 842 (if they have adopted this standard) to evaluate the collectibility of lease payments (and any residual value guarantee) for operating leases.

Under the guidance in ASC 842, if a lessor determines that it is no longer probable that it will collect operating lease payments and any residual value guarantee from an affected lessee, the lessor's lease income is limited to the lesser of (1) the income that would have been recognized if collection were probable, including income from variable lease payments, and (2) the lease payments, including variable lease payments, that have been collected from the lessee. Lease income is reversed if the lease payments, including variable lease payments, that have been collected from the lessee are less than the lease income recognized to date.

Refer to our FRDs, [*Lease accounting \(ASC 842\)*](#) or [*Lease accounting \(ASC 840\)*](#) (before the adoption of ASC 842), for more information.

Exit or disposal activities

A company may decide to sell or abandon certain assets or execute a restructuring plan as a result of the war in Ukraine, sanctions on Russia or the ripple effects. ASC 420, *Exit or Disposal Cost Obligations*, addresses the accounting and reporting for costs associated with exit or disposal activities. Exit activities may include:

- ▶ The sale or termination of a line of business
- ▶ The closure of a business location in the Ukraine, Russia or other affected country or the relocation of business activities from one country, region or facility to another
- ▶ Changes in management structure
- ▶ A fundamental reorganization that has a material effect on the nature and focus of a company's operations

An event doesn't need to have a material effect on an entity's business or the manner in which that business is conducted to be considered an exit activity. For example, a decision to move from one facility to another would be considered an exit activity.

The costs often incurred as part of an exit or disposal activity include employee termination benefits under a one-time termination plan, contract termination costs and costs to consolidate or close a facility and relocate employees. A liability for costs associated with an exit or disposal activity is recognized at fair value in the period the liability is incurred. For example, a liability to terminate a contract before the end of its term is recognized when the entity terminates the contract. A liability for costs associated with closing a facility and relocating employees is recorded when the associated costs are incurred, which is generally when the goods or services (e.g., security services incurred during the closing of the facility) associated with those activities are received.

The costs associated with temporarily vacating a facility would not be subject to ASC 420 but would continue to follow other relevant guidance related to the nature of those costs. An evaluation of whether an entity has ceased using a facility permanently or temporarily is based on the facts and circumstances.

Refer to our FRD, [*Exit or disposal cost obligations*](#), for additional information.

Asset retirement obligations

Damage to long-lived assets in Ukraine may trigger the initial recognition of an asset retirement obligation under ASC 410-20, *Asset Retirement and Environmental Obligations – Asset Retirement Obligations*, (e.g., reclamation of the ground from contamination of an underground storage tank). Additionally, entities may need to make changes to the amount or timing of the expected cash flows required to settle asset retirement obligations that already have been recognized. While the uncertainty in Ukraine may create an expectation that an obligation won't be enforced, if a legal obligation exists, then an asset retirement obligation must be recognized in accordance with ASC 410-20.

Refer to our FRD, [*Asset retirement obligations*](#), for additional information.

Fair value measurement

ASC 820 defines the term fair value and provides a principles-based framework for measuring fair value when US GAAP requires or permits a fair value measurement. For example, fair value measurements may be required when measuring impairment of long-lived assets, goodwill, indefinite-lived intangible assets and equity securities.

The objective of a fair value measurement is to determine the price at which an orderly transaction would take place between market participants under the market conditions that existed at the measurement date. While recent events could result in market volatility (e.g., a significant decrease in the volume or level of activity in certain markets), companies should not disregard market prices at the measurement date unless those prices are from transactions that are not orderly.

The concept of an orderly transaction is intended to distinguish a fair value measurement from the price in a distressed sale or forced liquidation. The intent is to convey the current value of the asset or liability at the measurement date, not its potential value at a future date. The objective of a fair value measurement does not change when markets have been volatile or inactive during a period of dislocation.

The determination of whether a transaction is distressed or forced is made at the individual transaction level and requires the use of judgment based on the facts and circumstances. While market factors, such as an imbalance in supply and demand, can affect the prices at which transactions occur in a given market, such an imbalance does not automatically indicate that the parties to a transaction were not knowledgeable and willing market participants or that a transaction was not orderly. Determining whether an observed transaction is orderly should be based on the available evidence from all relevant factors.

In addition, while a fair value measurement incorporates the assumptions that sellers, as well as buyers, would consider in pricing the asset or liability, a reporting entity's conclusion that it would not sell its own asset (or transfer its own liability) at prices currently observed in the market does not mean these transactions should be presumed to be distressed. ASC 820 makes clear that fair value is a market-based measurement, not an entity-specific measurement, and notes that the reporting entity's intention to hold an asset or liability is not relevant.

A significant decrease in the volume or level of activity in a market can influence which valuation technique(s) are used to measure fair value and how those techniques are applied. Determining fair value of an asset or liability when market activity has significantly declined requires the use of judgment and careful consideration of the specific facts and circumstances. However, the core concepts of the fair value framework continue to apply.

Regardless of the valuation techniques used, ASC 820 requires that the techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs. For example, it would not be appropriate for an entity to determine fair value using solely a model's value based on unobservable inputs (i.e., a level 3 measurement), when there are relevant prices or inputs observed from orderly transactions (i.e., a level 2 measurement).

When the level of activity in a market has declined from recent (or historical) levels of activity, transactions for an asset or liability in a particular market may still occur with sufficient frequency and volume to provide pricing information on an ongoing basis. That is, a significant decrease in the volume or frequency of transactions does not automatically imply that a market is no longer active.

If a decrease in market activity has affected an entity's valuation technique(s) used or how the techniques are applied, it should consider the disclosure requirements in ASC 820. For example, an entity should provide a description of the valuation technique(s) applied and the inputs used for level 2 or level 3 fair value measurements. Entities are also required to disclose a change in the valuation approach or a valuation technique and the reasons for that change.

Refer to our FRD, [Fair value measurement](#), for more information on fair value measurements and related disclosures.

Derivatives and hedge accounting

Business transactions may be postponed or canceled, or they may occur in significantly lower volumes than initially forecasted. If a company has designated a transaction, such as the purchase or sale of goods, in a cash flow hedge accounted for under ASC 815, *Derivatives and Hedging*, the company will need to consider whether the transaction is still “probable of occurring,” whether the volume or amounts involved will be lower than forecasted or whether it is now probable that the forecasted transaction will not occur.

That is, if current events and circumstances affect the probability of hedged forecasted transactions occurring during the time period and in the amounts designated at the inception of a hedge, a company will need to determine whether it can still apply hedge accounting. In addition, if a company determines that it is probable that a forecasted transaction will not occur within the specified time period (or within an additional two-month period thereafter as stated in ASC 815-30-40-4), it has to immediately reclassify to earnings the balances from past changes in the fair value of derivative contracts that have been recorded in accumulated other comprehensive income (AOCI).

However, the guidance in ASC 815 includes an exception to this requirement when extenuating circumstances that are related to the nature of the forecasted transaction and are outside the control or influence of the reporting entity cause the forecasted transaction to be probable of occurring on a date that is beyond the additional two-month time period. If the exception applies, an entity should continue to retain amounts previously recorded in AOCI until the forecasted transaction affects earnings. If not, amounts previously recorded in AOCI would have to be reclassified into earnings immediately and disclosed in the entity’s interim and annual financial statements. Making this determination will require the use of professional judgment, based on the facts and circumstances.

Companies that apply cash flow hedge accounting should also remember that a loss recorded in AOCI must be immediately reclassified into earnings if at any time the continued reporting of this loss in AOCI would lead to the recognition of a net loss when the forecasted transaction affects earnings. For example, an entity would need to reclassify from AOCI into earnings a loss that relates to a hedge of a forecasted purchase of inventory if it expects to recognize a net loss when the inventory is sold (i.e., if the cost basis of the inventory plus the related loss on the hedging instrument reported in AOCI exceeds the amount expected to be recovered through the future sale of the inventory).

Companies also need to consider whether the current market conditions could affect their assessment of whether hedging relationships continue to be highly effective, given the price volatility in certain commodities. This is particularly relevant when there are differences between the hedging instrument and the hedged item (e.g., hedging variable rate debt that contains an embedded floor with an interest rate swap that does not contain a floor, hedging forecasted purchases of jet fuel with crude oil derivatives). Current market conditions may also represent a change in facts and circumstances that requires an entity to switch from a qualitative to quantitative method of assessing hedge effectiveness.

Changes in a derivative counterparty’s credit risk or an entity’s own nonperformance risk also could affect fair value estimates of derivatives and hedge effectiveness. A fundamental requirement is that a hedging relationship, both at inception and on an ongoing basis, is expected to be highly effective in offsetting changes in fair value or cash flows attributable to the hedged risk during the period that the hedge is designated.

Companies need to consider whether the war, sanctions and their ripple effects could affect their assessment of whether hedging relationships continue to be highly effective.

In addition to the hedge accounting considerations noted above, companies that have elected to apply the normal purchases and normal sales (NPNS) scope exception to contracts that would otherwise be accounted for as derivative instruments should determine whether it remains probable that these contracts will result in physical delivery and not net settle. If a company determines that it is no longer probable that a contract will result in physical delivery, the contract would need to subsequently be accounted for as a derivative instrument (i.e., at fair value) as the requirements to apply the NPNS scope exception would no longer be met.

Companies that have ruble-denominated foreign exchange derivatives that require gross settlement (e.g., a forward contract to exchange a fixed amount of US dollars for a fixed amount of Russian rubles) should determine whether these contracts continue to meet the net settlement requirement to be considered a derivative instrument under ASC 815. A foreign exchange forward or swap contract that will be settled through delivery of a large amount of an illiquid currency would not be considered net settleable if that amount can't be readily converted to the functional currency of the reporting entity (i.e., the asset delivered is not readily convertible to cash).

Refer to our FRD, [*Derivatives and hedging \(after the adoption of ASU 2017-12\)*](#), for additional information.

Debt modifications and loan covenants

Affected companies may experience cash flow challenges as a result of disruptions in their operations, higher operating costs or lost revenues. They may need to obtain additional financing, amend the terms of existing debt agreements or obtain waivers if they no longer satisfy debt covenants.

Affected companies may need to consider the debt guidance in ASC 470-50, *Debt – Modifications and Extinguishments*, and ASC 470-60, *Debt – Troubled Debt Restructurings by Debtors*, to determine whether a change to an existing debt arrangement represents a troubled debt restructuring, a debt modification or a debt extinguishment, each of which would have different accounting implications. In addition, the entity needs to consider the guidance in ASC 470-10 on the classification of long-term debt when there has been a covenant violation or other default at the balance sheet date.

Refer to our FRDs, [*Issuer's accounting for debt and equity financings \(before the adoption of ASU 2020-06, Accounting for Convertible Instruments and Contracts in an Entity's Own Equity\)*](#) or [*Issuer's accounting for debt and equity financings \(after the adoption of ASU 2020-06, Accounting for Convertible Instruments and Contracts in an Entity's Own Equity\)*](#), for additional information.

Foreign currency matters

Intercompany transactions of a long-term investment nature

When an intercompany foreign currency transaction is of a "long-term investment" nature, foreign currency transaction gains and losses are reported in other comprehensive income rather than through income when the parties to the transaction are consolidated, combined or accounted for under the equity method in the reporting entity's financial statements. To be considered a long-term investment, an intercompany balance must continually meet the condition that settlement is neither planned nor anticipated in the foreseeable future. Affected companies may need to reassess whether an intercompany balance continues to qualify as a long-term investment.

A company's reassessment of its liquidity needs or a planned restructuring or relocation of foreign operations could be examples of changes in circumstances that could change the nature of an intercompany transaction from a long-term investment to one for which settlement becomes planned or anticipated. If a change in circumstances leads to such a change, foreign currency transaction gains and losses on the transaction should be recorded in earnings prospectively. Foreign currency transaction gains and losses recorded in other comprehensive income during the period for which settlement was not planned or anticipated remain in other comprehensive income and are not immediately reclassified to earnings.

Highly inflationary economies

Though Russia and Ukraine do not presently have highly inflationary economies, companies with operations in these countries should have processes in place to monitor for potential increases in inflation that could trigger highly inflationary economy accounting (i.e., cause a change in those operations' functional currency).

Exchange rates and financial statement translation

There may be a significant impact on the exchange rates used to account for foreign currency transactions and translation of financial statements given the current volatility in the currency markets. Companies that hold Russian or Ukrainian denominated debt securities classified as available for sale should consider whether changing foreign exchange rates, or other factors, trigger an impairment.

Refer to our FRD, [***Foreign currency matters***](#), for more information.

Revenue recognition

The war in Ukraine, the sanctions in Russia and other current economic challenges may affect various aspects of an entity's revenue accounting under ASC 606, *Revenue from Contracts with Customers*.

Refer to our FRD, [***Revenue from contracts with customers \(ASC 606\)***](#), which provides more information about all of the following topics.

Variable consideration

Estimates of variable consideration in new and ongoing customer contracts will need to be evaluated considering current circumstances. Examples of variable consideration estimates that may have changed due to the war in Ukraine and recent global events include expectations about returns of goods, contract volumes and whether an entity will meet contractual conditions for performance bonuses or penalties.

How we see it

In certain circumstances, an entity's estimate of contractual penalties could be limited by force majeure (i.e., unforeseeable circumstances, such as a war, that prevent the fulfillment of a contract) clauses. An entity should carefully consider, potentially with the assistance of legal counsel, the enforceability of any such clauses.

The amount of estimated variable consideration an entity can include in the transaction price at contract inception is constrained to the amount for which it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainties related to the variability are resolved. An entity that makes such an estimate at contract inception is also required to update the estimate, including reassessing the constraint, throughout the term of the contract to depict conditions that exist at each reporting date and reflect its revised expectations about the amount of consideration to which it expects to be entitled.

Changes to the transaction price that relate to a change in estimates of variable consideration (and are not a result of contract modifications, which are discussed below) generally are allocated to the performance obligations on the same basis as their initial allocation. Further, any amounts allocated to satisfied (or partially satisfied) performance obligations should be recognized in revenue in the period in which the transaction price changes (i.e., on a cumulative catch-up basis). This could result in either an increase or decrease in revenue in relation to a satisfied performance obligation or in cumulative revenue recognized for a partially satisfied performance obligation. Entities using the variable consideration allocation exception should also consider whether they can continue to apply this exception.

Contract modifications and terminations

Uncertainties related to recent global events and current market conditions may prompt entities to modify contracts with customers. Customers and entities may also terminate contracts (either fully or partially), which is a form of contract modification under ASC 606, or force majeure clauses may be triggered.

A contract modification occurs when the parties to a contract agree to amend the scope or price (or both) of a contract, and the amendments either create new enforceable rights and obligations of the parties or change their existing rights and obligations. Generally, it is clear when a contract modification has taken place, but in some circumstances that determination requires judgment. Contract modifications can also be implied by customary business practices as long as the changes either create new enforceable rights and obligations in the contract or change existing rights and obligations.

An entity should account for a contract modification under the guidance in ASC 606-10-25-10 through 25-13. Under this guidance, certain modifications are treated as separate, standalone contracts, while others are combined with the original contract and accounted for as one contract. In addition, some modifications are accounted for prospectively, while others are accounted for on a cumulative catch-up basis.

How we see it

When a contract accounted for under ASC 606 is modified, we believe that may indicate that a significant change in facts and circumstances has occurred and that the entity should reassess whether the arrangement still meets the criteria in ASC 606-10-25-1 to be considered a contract, as well as whether the contract's duration (i.e., the period in which parties to the contract have present enforceable rights and obligations) has changed. The accounting for any reassessment is prospective.

Collectibility and extended payment terms

The current global events may impact customers' ability and intent to pay, and entities may be more willing to accept partial payment or extend payment terms. Affected entities will need to determine how to account for these circumstances. Specifically, as discussed below, entities will need to consider the effects on their ASC 606 collectibility assessments, estimates of variable consideration made at contract inception and identification of significant financing components in addition to their credit loss allowance calculations (see *Financing receivables and contract assets* above).

When the amount an entity expects to collect changes after contract inception, the entity may need to exercise significant judgment to determine whether that change is due to (1) a change in estimate of the variable consideration identified at contract inception (and, therefore, accounted for as a change in the transaction price) or (2) an identifiable credit event (e.g., a known decline in a customer's operations, governmental restrictions affecting an entity's ability

Companies may need to consider the guidance in ASC 606 on accounting for contract modifications.

to pay) that should be accounted for as bad debt (i.e., outside of revenue). This determination will likely require entities to establish policies to differentiate between price concessions and customer credit events. When the terms of contracts with existing customers change, entities also need to determine whether there is a contract modification (as discussed above).

Entities also will need to exercise judgment to determine whether changes in the facts and circumstances related to a customer's ability and intent to pay the consideration in the contract are significant enough to indicate that a contract no longer exists and revenue should no longer be recognized. This is because ASC 606 requires an entity to reassess whether it is probable that it will collect the consideration to which it will be entitled when significant facts and circumstances change.

Offering extended payment terms to new or existing customers may also indicate that the contract includes a significant financing component. When there is a significant financing component, an entity needs to adjust the transaction price for the effects of the time value of money if the timing of payments agreed to by the parties in the contract provides the customer or the entity with a significant financing benefit.

Other revenue considerations

If an entity changes the pricing of its goods and services (e.g., as a result of higher oil and gas prices), it will need to determine whether the standalone selling prices of its goods and services should be updated for new contracts. As a reminder, standalone selling prices are determined at contract inception and are not updated for existing contracts unless the contract has been modified (and the modification is not treated as part of the existing contract).

Additionally, entities will need to determine any effect on the timing of revenue recognition resulting from customers' requests to hold finished goods at the entity's site. Entities will need to consider the bill-and-hold guidance in ASC 606-10-55-81 through 55-84, which includes criteria that must be met (in addition to the control indicators in ASC 606-10-25-30) for revenue to be recognized for the sale of a good in a bill-and-hold arrangement.

Disclosure

Entities should consider whether uncertainties or changes in business practices due to current global events require their revenue disclosures to be enhanced. For example, if an entity estimates variable consideration (including application of the constraint), it is required to disclose information about the methods, inputs and assumptions used. Entities are also required to disclose certain information about their performance obligations, including when performance obligations are satisfied in a bill-and-hold arrangement and significant payment terms. Entities should also consider the requirements to disclose the judgments and changes in judgments that significantly affect the determination of the amount and timing of revenue.

Insurance recoveries

Entities often maintain insurance to mitigate losses associated with property damage (property and casualty loss) or a business interruption, such as lost revenue during extended periods of suspended operations or stemming from supply chain interruption (i.e., business interruption insurance).

The accounting for insurance claims varies, depending on factors such as the nature of the claim and coverage, the amount of proceeds (or anticipated proceeds), the timing of the loss and insurance recovery, and the ability of an insurer to satisfy a claim.

To account for any potential insurance recovery, companies need to carefully analyze the terms of their insurance policies and the ability of their insurer to satisfy a claim. For example, the policy may contain a “war exclusion” that excludes losses arising directly or indirectly from war. Companies also may need to determine whether their insurance covers losses that are the result of the sanctions on Russia. Some countries, including the US, prohibit insurance payments if the payments would violate sanctions.

If a company determines it has incurred property and casualty losses, any insurance recoveries would be recognized when the company believes it is probable¹ that the insurer will settle the claim. Receipts from insurance up to the amount of the loss recognized are considered recoveries. Insurance recoveries should not be recognized before the related cost is recognized.

Anticipated proceeds in excess of the amount of loss recognized would be considered a gain contingency and would not be recognized until all contingencies related to the insurance claim are resolved.

Future operating losses

While affected companies may account for some of the effects discussed in this publication in the current period, other direct and indirect effects, such as losses or lost revenue, may need to be accounted for in subsequent periods. Companies may anticipate losses that are directly or indirectly related to these events (e.g., increases in the price of oil and gas, supply chain disruptions). Future operating losses do not meet the definition of a liability and, therefore, should not be recognized until the losses are incurred; however, affected registrants may need to consider whether additional disclosures are required.

Short-term employment benefits

Companies may provide employees with short-term benefits due to the war in Ukraine, such as salary continuation to employees on temporary leave. These companies should record an accrual for the expected cost of these benefits when it is probable that the benefits will be paid and the cost of the benefits can be reasonably estimated. To measure the liability for these benefits, companies must estimate the length of time the employee is expected to receive the benefits. This estimate should be updated at each balance sheet date.

Companies should evaluate other benefits they are providing to determine the appropriate accounting for the costs.

Share-based payment awards

Companies that grant share-based payment awards with performance conditions recognize the related compensation cost over the employee’s requisite service period or the nonemployee’s vesting period when it is probable that the performance condition will be satisfied. Probability is assessed at each reporting date, and changes in estimate are accounted for in the period of the change through a cumulative catch-up adjustment. Companies must consider updated forecasts to assess whether performance conditions based on metrics (e.g., sales, earnings per share) that have been affected by current global events will be satisfied. If a performance condition changes from being probable to improbable, the company reverses previously recognized compensation cost in the period in which the assessment changes.

Companies that grant share-based payment awards with conditions related to achieving a specified price of the company’s shares include that market condition in the estimate of the grant-date fair value. The related compensation cost is recognized over the employee’s derived service period or the nonemployee’s vesting period. If the service is rendered or goods are delivered, compensation cost must be recognized even if the market condition is not achieved (i.e., previously recognized expense is not reversed just because stock prices decline).

Companies that expect to be in a cumulative loss position based on revised forecasts that reflect the effects of the war in Ukraine should consider this negative evidence about the realizability of deferred tax assets.

Due to the significant uncertainty in the current environment, companies may amend the terms or conditions of share-based payment awards to keep grantees incentivized. If amendments to the terms and conditions of an award change the fair value, vesting conditions or classification of an award, the company must apply modification accounting. To determine the compensation cost to recognize for a modification a company generally must determine on the date of the modification whether, based on *current* circumstances, it is probable that the awards would vest under either the original vesting conditions, the new vesting conditions or both.

Companies that have grantees in Russia or Ukraine also need to consider whether their method of settlement of share-based payment arrangements has changed. For example, because of the sanctions, a company may conclude it can no longer settle certain arrangements in shares and, therefore, would be required to settle them in cash. Alternatively, a company may choose to modify awards that were previously classified as equity to be settled in cash. When an award changes classification from an equity instrument to a liability, a company is required to measure the fair value of the liability on the date of the modification and generally includes in its measurement of compensation cost any increase in the fair value of the award between the grant date and the modification date.

Modifying share-based payments can have tax consequences. Accordingly, companies should consult with their tax advisors before modifying share-based payments.

Refer to our FRD, [Share-based payment](#), for more information.

Income taxes

The war in Ukraine, sanctions on Russia and their ripple effects could affect a company's income tax accounting in several ways, including with respect to the indefinite reinvestment assertion, judgments made about the realizability of deferred tax assets and carryforwards, and interim-period accounting considerations.

Please also refer to our FRD, [Income taxes](#), for additional information on the topics discussed below.

Indefinite reinvestment assertion

Companies that assert their intent and ability to indefinitely reinvest foreign earnings should challenge whether they can continue to do so in Ukraine, Russia or other countries in which their operations have been affected by current events.

The assertion that earnings from foreign operations will be indefinitely reinvested should be supported by projected working capital and long-term capital needs in the locations in which those earnings are generated (or other foreign locations) and an analysis of why those funds are not needed upstream.

Companies that determine they have a change in their indefinite reinvestment assertion during an interim period also should consider the interim reporting guidance in ASC 740-270 on whether to include the effects of the change in assertion in the estimated annual effective tax rate or to recognize the effects as a discrete item in the interim period.

Realizability of deferred tax assets and carryforwards

Companies may need to reevaluate and change their conclusions about the realizability of their deferred tax assets. Future realization of deferred tax assets ultimately depends on the existence of sufficient taxable income of the appropriate character in either the carryback (if permitted under the tax law) or carryforward period under the tax law. Determining whether a valuation allowance for deferred tax assets is necessary often requires an extensive analysis of positive and negative evidence regarding the realization of the deferred tax assets, including

an assessment of the likelihood of sufficient future taxable income. Companies that have a change in a valuation allowance during an interim period should consider ASC 740-270 for guidance on whether to include the effects of the change in the estimated annual effective tax rate or to recognize the effects as a discrete item in the interim period.

Projections of future taxable income to support the realizability of deferred tax assets should be consistent with projections used for other purposes by the company (e.g., long-lived asset impairment tests, interim goodwill impairment tests) and should reflect the direct and indirect effects of the war.

Accounting for income taxes in an interim period

A company is required at the end of each interim reporting period to make its best estimate of the annual effective tax rate for the full fiscal year and use that rate to provide for income taxes on a current year-to-date basis by applying the rate to ordinary income.

Significant unusual or infrequently occurring items are reported as discrete events (i.e., not included in the annual effective tax rate) if they reflect transactions that are separately reported or reported net of the related tax effects (e.g., discontinued operations). In addition to being unusual or infrequently occurring, a transaction also must be significant to be excluded from ordinary income (and, therefore, excluded from the effective tax rate calculation). Significance generally does not, in and of itself, mean that a transaction should be recognized discretely.

Deciding whether certain items (e.g., impairments resulting from current events) should be considered unusual or infrequently occurring can be challenging and can require careful consideration of the facts and circumstances as well as expectations about the future.

Companies affected by the war in Ukraine, sanctions on Russia or its ripple effects may experience a reduction in demand, temporary or permanent closures of their operations, or supply chain interruptions that may create challenges in preparing reliable estimates. Estimates of the annual effective tax rate are, of necessity, based on evaluations of possible future events and transactions and may be subject to refinement or revision.

ASC 740 addresses the consequences of an entity's inability to reliably estimate some or all the information that is ordinarily required to determine the annual effective tax rate in an interim period financial statement. When an entity is unable to estimate a part of its ordinary income (loss) or the related tax expense (benefit) but is able to make a reliable estimate of its estimated annual effective tax rate, the tax expense (benefit) applicable to the item that cannot be estimated should be reported in the interim period in which the item is reported. In some cases, a company may not be able to make a reliable estimate of its estimated annual effective tax rate. If a reliable estimate of the estimated annual effective tax rate cannot be made, the actual effective tax rate for the year to date may be the best estimate of the annual effective tax rate.

How we see it

We generally expect a company to be able to make a reliable estimate of ordinary income and an estimated annual effective tax rate. However, a company may not have the ability to make a reliable estimate of all or part of its ordinary income due to the war in Ukraine, the sanctions on Russia or their ripple effects. We believe that a company's conclusion that it cannot make a reliable estimate of all or parts of its ordinary income or its estimated annual effective tax rate should be consistent with conclusions reached about similar projections used by management in the financial statements and disclosures made to users of the financial statements.

Generally, ASC 740 requires an entity that is subject to tax in multiple jurisdictions to determine one overall estimated annual effective rate to calculate the interim period tax expense (benefit) unless:

- ▶ The company anticipates an ordinary loss for the fiscal year in any jurisdiction or incurs an ordinary loss for the year-to-date period for which a tax benefit cannot be realized.
- ▶ A company is unable to estimate the annual effective tax rate in a foreign jurisdiction in dollars or is otherwise unable to make a reliable estimate of the ordinary income (loss) or the related tax (benefit) in a foreign jurisdiction for the fiscal year.

Companies that may be experiencing losses in certain jurisdictions given current global events should consider the related accounting effects if they meet either exception.

Consolidation

Reporting entities should carefully evaluate any events or actions that could affect their rights associated with governance matters of a legal entity or create additional exposure to risk of loss, in particular for operations in Russia, Ukraine or in other affected jurisdictions.

Reporting entities are required to reevaluate whether a legal entity is a variable interest entity (VIE) when certain significant events occur that change the design of that legal entity or call into question whether (1) the legal entity's equity investment at risk is sufficient or (2) the holders of the legal entity's equity investment at risk, as a group, have the characteristics of a controlling financial interest. In addition, a reporting entity is required to continuously evaluate whether it is the primary beneficiary of a VIE as a result of changes in facts and circumstances. Reporting entities also need to consider whether their actions create new variable interests, including implicit variable interests, or change their previous conclusions.

ASC 810, *Consolidation*, states that control of a foreign entity may not rest with the majority owner under certain circumstances, including when the subsidiary operates under foreign exchange restrictions so severe that they cast significant doubt on the reporting entity's ability to control the entity.

How we see it

While reporting entities should consider the totality of their individual facts and circumstances, we generally do not believe that a lack of exchangeability of a foreign currency, such as the Russian ruble, in and of itself would require the deconsolidation of a foreign subsidiary. Rather, we believe that a reporting entity has a controlling financial interest when it has the ability to direct the activities that significantly affect the legal entity's economic performance. However, affected entities will need to carefully evaluate actions taken by a foreign government that would prevent the parent from making decisions about the activities that significantly affect the legal entity's economic performance.

It is possible that a reporting entity's actions, or changes in facts and circumstances related to a legal entity with which it is involved, could change consolidation conclusions, and judgment needs to be applied carefully.

See our FRD, [*Consolidation*](#), for additional guidance.

Financial statement disclosures

The financial statement disclosures for companies directly or indirectly affected by the war in Ukraine, the sanctions on Russia and the ripple effects will vary depending on the magnitude, duration and nature of the effects on their businesses and the availability of information. Companies will need to closely monitor developments and assess the implications for their businesses.

In some cases, disclosures depend on the nature of the loss (e.g., asset impairments). In other cases, affected companies will be required to make disclosures that generally address loss contingencies, risks and uncertainties, or subsequent events.

Loss contingencies

ASC 450, *Contingencies*, requires disclosure of the nature of a contingency when there is at least a reasonable possibility that a loss has been incurred. For contingencies that meet the threshold for disclosure but no liability has been recognized, companies must disclose an estimate of the possible loss or the range of possible losses or state that such an estimate cannot be made. If a company has recognized a liability, it has to disclose the amount only if not doing so would make the financial statements misleading. If there is at least a reasonable possibility that a loss in excess of the amount recognized exists, the company is required to disclose an estimate of the possible loss or range of losses or state that such an estimate cannot be made.

Risks and uncertainties

ASC 275, *Risks and Uncertainties*, requires disclosures about certain risks and uncertainties, including qualitative disclosures about risks and uncertainties that in the near term (i.e., within one year from the date of the financial statements) 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 under ASC 275 to disclose certain significant estimates and concentrations (e.g., concentration in the volume of business with a particular customer or supplier or in a market or geographic area) that make an entity vulnerable to the risk of a near-term severe impact. These disclosures may be necessary for companies directly or indirectly affected by the current environment (e.g., a company that has material operating costs that are sensitive to fuel prices). Potential supply chain disruptions may also warrant disclosure.

Subsequent events

Companies should evaluate whether the war in Ukraine, the sanctions on Russia and their ripple effects provide additional evidence about conditions that existed at the balance sheet date, including the estimates used to prepare the financial statements. All information that becomes available before the financial statements are issued or available to be issued should be considered in the evaluation of the conditions on which financial statement estimates are based, because these events may represent the culmination of conditions that existed over a relatively long period and, most importantly, existed before the balance sheet date. The financial statements should be adjusted for any changes in estimates resulting from such recognized subsequent events.

For non-recognized subsequent events, affected companies should consider disclosing the nature of the event and an estimate of its effect on the financial statements or a statement that such an estimate cannot be made. Additionally, companies that may be indirectly affected by the events, such as a company with a concentration of revenue from customers in the affected area, should consider whether subsequent event disclosures are necessary to keep the financial statements from being misleading.

Companies need to make disclosures about the nature of a contingency if there is at least a reasonable possibility that they have incurred a loss.

SEC reporting and disclosures

Domestic and foreign companies that file with the SEC need to consider a number of SEC reporting and disclosure requirements. They also need to make sure their disclosure controls and procedures are operating effectively so they can produce the necessary robust disclosures in a timely manner.

MD&A

Companies should disclose any unusual or infrequent events, transactions or significant economic changes that materially affected income from continuing operations (such as lost revenue or costs attributable to the war) in management's discussion and analysis (MD&A). They are also required to disclose known trends or uncertainties that have had, or are reasonably expected to have, a material effect on their revenue or income from continuing operations, liquidity or capital resources.² Known trends or uncertainties may include supply chain disruptions that affect the relationship of costs to revenues, for example.

Companies may need to consider effects on their capital resources and liquidity, including situations in which the sources and uses of cash could be materially affected and potentially lead to uncertainty about a company's ability to continue to meet covenants of credit agreements. A company that is having liquidity issues should evaluate the adequacy of its disclosures related to potential capital needs and alternative sources of capital to fund those needs. If a material liquidity deficiency has been identified, disclosures may need to include the course of action the company has taken or proposed to take to remedy the deficiency.

It may also be appropriate for companies to include disclosures in MD&A related to any heightened uncertainty or changes in key assumptions underlying critical accounting estimates.

Form 8-K

Affected companies should have robust disclosure controls and procedures in place so they can timely disclose material information related to the events and identify any triggering events that may warrant the filing of a Form 8-K. For example, a company will need to consider whether any physical damage, curtailment of operations in Ukraine or Russia or a decline in economic activity triggers a material impairment charge, which generally would require reporting within four business days under Item 2.06 of Form 8-K, unless the conclusion is made in connection with the preparation, review or audit of financial statements required to be included in a timely filing and such disclosure is included in the timely filed report. Companies should also consider whether any costs related to ceasing operations should be reported under Item 2.05 of Form 8-K and whether any liquidity issues trigger the violation of debt covenants or the acceleration of obligations that would have to be reported under Item 2.04 of Form 8-K.

Risk factor disclosures

Since companies are required to disclose in each quarterly report on Form 10-Q any material new risks or changes in risk factors previously disclosed in its annual report on Form 10-K, companies should consider the need to update their risk factor disclosures to reflect the direct and indirect effects of the war. Accordingly, risk factors that were added or revised in the first quarter would need to be disclosed and updated as appropriate in each subsequent quarterly report if they are still applicable.

Non-GAAP financial measures

Companies should be mindful of the SEC's rules, regulations and guidance when non-GAAP financial measures adjust for any items related to the conflict.

We believe that registrants that want to explain any discrete effects should limit adjustments in their non-GAAP measures to charges incurred or gains recognized that clearly relate to the discrete event (e.g., effects of the war) and are incremental to, and separable from, normal operations. Evaluating whether adjustments meet these criteria may require significant judgment.

As always, registrants should explain why such measures are useful to investors and consider whether they are consistent with measures used by management and communicated to the board. It would generally be inappropriate to disclose a non-GAAP measure of operating performance that normalizes operations or eliminates normal recurring cash operating expenses.

Other disclosure considerations

Companies may need to consider adjusting disclosures in other areas of their annual reports and registration statements to reflect the direct and indirect impacts of the war, including the description of their business, properties and human capital under Items 101 and 102 of Regulation S-K.

How we see it

In 10-Ks and 10-Qs filed recently with the SEC, companies in various industries have disclosed specific effects of the war in Ukraine, such as ceasing to sell, serve or support products in Russia and certain regions of Ukraine, and discontinuing operations in Russia.

Cybersecurity considerations

Companies should consider the heightened risk of cybersecurity incidents due to the war and disclose information associated with cybersecurity and cybersecurity incidents that are material to investors.

Cybersecurity incidents may have significant accounting and financial reporting implications. For example, cybersecurity incidents may result in:

- ▶ Expenses related to investigation, breach notification, remediation and litigation, including the costs of legal and other professional services
- ▶ Loss of revenue (e.g., due to an interruption in service, customers switching to a different vendor)
- ▶ Claims related to warranties, breaches of contracts, product recalls/replacements, indemnification of counterparties and insurance premium increases
- ▶ Diminished future cash flows (e.g., as a result of reputational damage), impairment of intangible assets (e.g., trademarks, customer relationships, software) or increased financing costs

When evaluating the information to disclose about cybersecurity risks and material incidents, registrants should consider the relevant accounting guidance (e.g., ASC 275, ASC 450, ASC 606, ASC 350) and the SEC's interpretive guidance on cybersecurity that was issued in 2018 (the 2018 Interpretive Release³). The SEC recently proposed rules on cybersecurity incidents that would codify many of the concepts in the 2018 Interpretive Release and go beyond the guidance by requiring disclosures about cybersecurity risk governance and the board's expertise in that topic.

The SEC also expects that a company's financial reporting and internal control systems would be designed to provide reasonable assurance that information about the range and magnitude of the financial impacts of a cybersecurity incident would be incorporated into its financial statements on a timely basis as the information becomes available.

See our To the Point publication, [*SEC proposes requiring more cybersecurity disclosures*](#), and our SEC Reporting Update publication, [*SEC issues guidance on cybersecurity*](#), for more guidance.

ICFR considerations

Companies will also need to consider how the war in Ukraine or the sanctions on Russia may be affecting their internal control over financial reporting (ICFR). Disruptions to a company's operations, processes, workforce, customers and suppliers should be considered when evaluating whether legacy controls continue to be designed and operating at an appropriate level to mitigate risks of material misstatement to the financial statements. A company needs to evaluate necessary changes in the design of controls to address the original risks of material misstatement as well as any new or modified risks, including whether new or existing controls are appropriately designed to address relevant accounting and reporting implications associated with the war in Ukraine.

SEC registrants also need to consider whether they have made any changes to the design of their ICFR that has materially affected, or is reasonably likely to materially affect, their ICFR and, therefore, would need to be disclosed in Form 10-Q or Form 10-K. Determining what constitutes a material or reasonably likely material change in a control during the current period will require careful consideration.

In addition, companies should hold timely discussions with their audit committees and auditors to make sure their financial reporting and review processes are robust and practical, considering the circumstances.

Endnotes:

¹ Probable is defined in the ASC Master Glossary as "the future event or events are likely to occur."

² Item 303 of Regulation S-K.

³ [Commission Statement and Guidance on Public Company Cybersecurity Disclosures](#), 26 February 2018.

Appendix

This appendix provides links to FRDs referenced throughout this Technical Line and other relevant publications. See below for the breakout by section.

Asset impairments

- ▶ Financial reporting developments, [Impairment or disposal of long-lived assets](#)
- ▶ Financial reporting developments, [Intangibles – Goodwill and other](#)
- ▶ Financial reporting developments, [Discontinued operations – ASC 205-20](#)
- ▶ Financial reporting developments, [Equity method investments and joint ventures](#)
- ▶ Financial reporting developments, [Certain investments in debt and equity securities](#)
- ▶ Financial reporting developments, [Credit impairment under ASC 326](#)
- ▶ Financial reporting developments, [Credit impairment for short-term receivables under ASC 326](#)
- ▶ To the Point, [FASB eliminates TDR guidance for creditors and requires enhanced vintage disclosures](#)

Leases

- ▶ Financial reporting developments, [Lease accounting \(ASC 842\)](#)
- ▶ Financial reporting developments, [Lease accounting \(ASC 840\) \(before the adoption of ASC 842\)](#)

Exit or disposal activities

- ▶ Financial reporting developments, [Exit or disposal cost obligations](#)

Asset retirement obligations

- ▶ Financial reporting developments, [Asset retirement obligations](#)

Fair value measurement

- ▶ Financial reporting developments, [Fair value measurement](#)

Derivatives and hedge accounting

- ▶ Financial reporting developments, [Derivatives and hedging \(after the adoption of ASU 2017-12\)](#)

Debt modifications and loan covenants

- ▶ Financial reporting developments, [Issuer's accounting for debt and equity financings \(before the adoption of ASU 2020-06, Accounting for Convertible Instruments and Contracts in an Entity's Own Equity\)](#)
- ▶ Financial reporting developments, [Issuer's accounting for debt and equity financings \(after the adoption of ASU 2020-06, Accounting for Convertible Instruments and Contracts in an Entity's Own Equity\)](#)

Foreign currency matters

- ▶ Financial reporting developments, [*Foreign currency matters*](#)

Revenue recognition

- ▶ Financial reporting developments, [*Revenue from contracts with customers \(ASC 606\)*](#)

Share-based payment awards

- ▶ Financial reporting developments, [*Share-based payment*](#)

Income taxes

- ▶ Financial reporting developments, [*Income taxes*](#)

Consolidation

- ▶ Financial reporting developments, [*Consolidation*](#)

SEC reporting and disclosures

- ▶ SEC financial reporting series, [*2021 SEC annual reports – Form 10-K*](#)
- ▶ SEC financial reporting series, [*2022 SEC quarterly reports – Form 10-Q*](#)

Cybersecurity considerations

- ▶ To the Point, [*SEC proposes requiring more cybersecurity disclosures*](#)
- ▶ SEC Reporting Update, [*SEC issues guidance on cybersecurity*](#)