European Securities and Markets Authority

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PUBLIC STATEMENT

Implications of Russia's invasion of Ukraine on half-yearly financial reports

ESMA is issuing this Statement to promote transparency and consistent application of European requirements for information provided in half-yearly financial reports with regards to Russia's invasion of Ukraine. ESMA recognises that Russia's invasion of Ukraine and the sanctions imposed against Russia and Belarus pose significant challenges to business activities and introduce a high degree of uncertainty on the expected development of those activities and the associated knock-on effects on the economic and financial system, at both European and international level.

This Statement addresses the preparation of interim financial statements according to IFRS Accounting Standards and the interim management reports for the 2022 half-yearly reporting periods. It highlights the need for issuers to provide information that is useful to users and adequately reflects the current and, to the extent possible, expected impact of Russia's invasion of Ukraine on the financial position, performance and cash-flows of issuers. ESMA also highlights the importance of providing information on the identification of the principal risks and uncertainties to which issuers are exposed. The considerations in this Statement are also applicable to the reporting of financial information in other interim periods prepared in accordance with IAS 34 *Interim Financial Reporting* or to annual financial statements prepared in accordance with IAS 1 *Presentation of Financial Statements*.

In order to facilitate users' access to information on material impacts of Russia's invasion of Ukraine in financial statements, issuers are encouraged to include all relevant information, including that concerning expected credit losses or exposures to the affected markets, in one single note or to provide a mapping of where different notes address Russia's invasion. The disclosures should be tailored to the specific circumstances of individual issuers. Issuers with operations in the affected markets or significantly exposed to commodities affected by Russia's invasion of Ukraine (e.g., energy or agriculture) should either explain the impact of the invasion or are encouraged to clearly explain why Russia's invasion of Ukraine has not had a material impact on their financial statements despite the exposure to significant risks.

ESMA calls on the management and supervisory bodies, including audit committees, of issuers and, where applicable, their auditors, to take due consideration of the recommendations included in this Statement when preparing the interim financial reports. Given the complexities of the current environment, ESMA encourages audit committees to enhance their oversight role which is key to contributing to high-quality half-yearly financial reports.

Finally, ESMA reminds issuers of their obligation to disclose as soon as possible any relevant material information about the impact of Russia's invasion of Ukraine on their fundamentals, prospects or financial situation in accordance with their transparency obligations under the Market Abuse Regulation.

Half-yearly financial statements

Application of IAS 34

When preparing their interim financial statements in accordance with IAS 34, issuers are reminded that the extent of the information provided should be proportionate to the objective of providing an update on the latest complete set of annual financial statements, including, as indicated in paragraph 6 of IAS 34, new activities, events and circumstances that have not been captured in the most recent annual financial statements.

ESMA also expects that, for issuers with significant exposures to Russia, Belarus and/or Ukraine's markets and/or significantly exposed to certain commodities (e.g., energy or agriculture sector), Russia's invasion of Ukraine constitutes a significant event under paragraphs 15 - 15C of IAS 34. Therefore, ESMA urges those issuers to adjust and potentially expand the level of detail of the information provided in half-yearly financial statements (e.g., provide a breakdown of assets and liabilities potentially exposed to Russia's invasion of Ukraine and to the sanctions). ESMA emphasises that paragraphs 17 and 31 of IAS 1[1] require disclosures in addition to those required by individual IFRSs – thus also beyond the minimum disclosures required by IAS 34 – when necessary to enable a user's understanding of the impact of particular transactions, other events and conditions. On this basis, some of the disclosures that are normally required by individual IFRSs for a complete set of (annual) financial statements may be necessary to provide relevant information on the consequences arising from Russia's invasion of Ukraine in the condensed financial statements for the half-year.

Disclosures reflecting judgements made, significant uncertainties and going concern risks linked to Russia's invasion of Ukraine

Russia's invasion of Ukraine has introduced uncertainty in the conduct of businesses and, as a result, a significant risk of material adjustment to the carrying amounts of assets and liabilities may have arisen. In these cases, ESMA urges issuers to update the assessment made at year-end on significant judgements, on the assumptions about the future and other major sources of estimation uncertainty as provided in accordance with paragraphs 122 and 125 of IAS 1. In this respect, ESMA notes that paragraph 16A(d) of IAS 34 requires disclosures of the nature and amount of changes in estimates of amounts reported in prior interim reporting periods of the current financial year or changes in estimates of amounts reported in prior financial years.

ESMA reminds issuers of the importance of updating the disclosures relating to the sensitivity analyses (e.g., by expanding the range of reasonably possible changes in key assumptions or reassessing assumptions used when, for instance, determining cash-flows estimations).

[1] These requirements are also applicable to interim financial statements (paragraph 4 of IAS 1).

ESMA highlights that the disclosure of sensitivity analysis may be particularly relevant in the context of testing assets for impairment.[2]

Finally, ESMA notes that the uncertainties arising from Russia's invasion of Ukraine may, in some cases, cast doubt on an issuer's ability to continue as a going concern. In this respect, ESMA reminds issuers that the going concern assumption is assessed at group level. If the going concern assumption at group level is appropriate, the consolidated financial statements are prepared on a going concern basis even if there is significant doubt about a subsidiary's ability to continue as a going concern. If material uncertainties exist related to the going concern assumption at group level, the entity shall disclose those uncertainties in accordance with paragraph 25 of IAS 1.[3] ESMA expects that in making the assessment of their ability to continue as a going concern, issuers shall take into account all available information about the future, including the expected profitability and any restrictions to readily access financial resources. In this respect, ESMA expects that issuers disclose the amounts of significant cash and cash equivalents balances not available for use by the group.[4]

Impairment of non-financial assets

ESMA reminds issuers that, in accordance with paragraphs 9 and 12 of IAS 36 *Impairment of Assets*, they should assess whether there are any indications that an asset in the scope of IAS 36 (e.g., tangible, goodwill, intangible, right-of-use) may be impaired by considering internal and external sources of information. In making this assessment, issuers should carefully consider whether the effects of Russia's invasion of Ukraine (direct and indirect)[5] constitute an indication that one or more assets may be impaired. ESMA expects that decisions to abandon, dispose of, suspend operations, or cancel investments in Ukraine, Russia or Belarus will be taken into account when assessing whether recognition of impairments and/or write-down of assets are necessary.

In this respect, ESMA reminds issuers that while impairment indicators with regards to interests accounted for using the equity method (such as associates and joint ventures) should be assessed in accordance with paragraphs 40 and 41A-41C of IAS 28 *Investments in Associates and Joint Ventures*, the impairment test should be undertaken applying IAS 36.

ESMA notes that determining the recoverable amount in the current uncertain environment requires a careful assessment of the cash-flow projections. Such projections may require, especially in the current circumstances and depending on the level of risk associated with the assets being tested, consideration of multiple scenarios. The weighting of the different scenarios needs to be calibrated on the basis of reasonable, supportable and realistic estimates and assumptions (e.g., cash flow projections and assumptions may need to be updated to reflect observable trends related to decreases of revenue and/or increases in costs

[2] Paragraphs 134(d), (e)and (f) of IAS 36. For instance, when there are significant changes in the operational and financial assumptions used in comparison with the last impairment test performed.
[3] In making this assessment issuers are encouraged to consider the educational material issued by the IASB in January 2021: https://www.ifrs.org/content/dam/ifrs/news/2021/going-concern-jan2021.pdf.
[4] Paragraph 48 of IAS 7 *Statement of Cash Flows*.
[5] Such as cost increases due to higher commodity prices, business interruptions due to disruptions to supply chains and the effects of sanctions.

of production, such as increases in energy costs). In particular, ESMA calls for consistency between (i) the cash-flows projections and assumptions used for impairment testing and (ii) any changes made or announced to strategic plans due to Russia's invasion of Ukraine and its implications (e.g., disinvestments in operations).

ESMA highlights that, in accordance with paragraphs 55 and 56 of IAS 36, the discount rates used in the determination of an asset's value in use shall reflect current market assessments of the time value of money and the risks specific to the asset being tested and exclude risks and uncertainties that were already taken into account in the projected cash-flows. In this respect, ESMA notes that Russia's invasion of Ukraine has impacted the interest rates and inflation trends. Consequently, the discount rate used to determine the recoverable amount may need to be updated to reflect these developments, unless the future cash flows have been adjusted for the effect of these risks such as by using different scenarios.

ESMA expects issuers to disclose explanations regarding significant changes, if any, compared to the last tests performed. For instance, where applicable, issuers should disclose key financial and operational assumptions and their significant changes (including, the scenarios used and their probability weights).

Impairment of financial instruments and other financial risks

In assessing the impairment of the debt securities and loans, as well as of lease and trade receivables and contract assets (IFRS 15 *Revenue from Contracts with Customers*) entities may need to consider the effect of invasion-induced events on whether there has been a significant increase in credit risk (SICR) and on the measurement of expected credit losses (ECL) taking into account forward-looking information. Issuers who rely to a large extent on historical information should consider requirements of paragraph B5.5.52 of IFRS 9 *Financial instruments* and carefully reassess whether their ECL-measurement models reflect the impact of Russia's invasion of Ukraine and related events on credit risk and ECL-measurement. In case issuers encounter difficulties in identifying the effects of Russia's invasion of Ukraine at instrument level, it may be necessary to perform the assessment on a collective basis (i.e., on a group or sub-group of financial instruments).[6] ESMA notes that for non-financial issuers, incurred or expected defaults of debtors could have an impact on the ECL-measurement for trade receivables and contract assets recognised applying IFRS 15.

ESMA highlights that the validity of credit enhancements, such as financial guarantees, may also be affected. Issuers should, therefore, carefully analyse the contractual terms of credit enhancements and assess possible accounting implications including effects on measuring ECL which depends on whether the credit enhancements are considered an integral part of the contractual terms of related financial assets or not and whether they are recognised separately by the issuer. Furthermore, issuers may need to consider potential impacts on their hedge accounting relationships, in particular whether the hedged forecasted transactions (e.g., sales to customers in Russia) are still highly probable.

[6] Paragraphs B5.5.1-B5.5.5 of IFRS 9.

ESMA reminds issuers to consider the requirements in IFRS 7 *Financial Instruments: Disclosures*. Issuers are expected to provide sufficient transparency regarding their significant exposures to credit, liquidity, currency (Russian rouble), commodity and other risks and the related sensitivities including (if material) the effects on the ECL-measurement with respect to their investments affected by Russia's invasion of Ukraine. Disclosures may also include the impact of issuers' risk hedging activities. In relation to transactions in derivative instruments, ESMA notes that increased volatility in financial markets can trigger significant cash outflows resulting from margin calls.

ESMA emphasises the importance of disclosures on sensitivity analysis with regards to currency risk, commodity risk or other types of market risk at an appropriate level of disaggregation.[7] Moreover, issuers should consider providing disclosures that will enable users of financial statements to understand the impact of credit enhancements on the ECL.[8]

Loss of control, joint control or the ability to exercise significant influence

As a result of Russia's invasion of Ukraine, issuers may need to reassess,[9] for the purpose of interim financial statements, whether they still have control of investees located in affected regions in accordance with paragraphs 6 and 7 of IFRS 10 *Consolidated Financial Statements*, significant influence as prescribed in paragraphs 5 and 6 of IAS 28, or joint control as defined in paragraph 7 of IFRS 11 *Joint Arrangements*. Issuers should carefully consider whether, as a result of the invasion or the sanctions imposed, there are changes in facts and circumstances that may significantly limit their ability to exercise their rights or governance provisions with respect to a subsidiary, an associate or a joint arrangement. In this respect, ESMA notes that the decision to abandon operations in the affected areas, restrictions on access to information or on the use of financial resources may not necessarily lead to the loss of control or significant influence over an investee.

Where applicable and relevant, ESMA expects issuers to provide – in line with the objectives and requirements of IFRS 12 *Disclosure of Interests in Other Entities* – detailed explanations with regards to any changes made to their assessment of control, joint control and/or significant influence and as to whether they consider that control, joint control or significant influence has been lost.

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

ESMA also reminds issuers that, in accordance with IFRS 5, non-current assets or disposal groups classified as held for sale must be available for immediate sale in their present condition

[7] Paragraphs 40-42 and B17-B21 of IFRS 7.
[8] Paragraph 35K of IFRS 7.
[9] Paragraph 8 of IFRS 10, paragraph 13 of IFRS 11 and Paragraph 8 of IAS 28.

and the sale must be highly probable.[10] Furthermore, ESMA notes that in accordance with paragraph 13 of IFRS 5, assets or disposal groups that are to be abandoned shall not be classified as held for sale, but results and cash flows from a disposal group that is to be abandoned shall be presented as discontinued operations if the criteria specified in paragraph 32 of IFRS 5 are met.

Other disclosure requirements applicable to half-yearly financial statements

Apart from the items explicitly mentioned above, ESMA highlights that issuers should consider whether other requirements in IFRS are also relevant in the context of their half yearly financial reporting. These requirements include, but are not limited to, the recognition of deferred tax assets[11] following IAS 12 *Income Taxes*, fair value measurement in accordance with IFRS 13 *Fair Value Measurement*, remeasurement of foreign currency transactions and translation of foreign currency financial statements in accordance with IAS 21 *The Effects of Changes in Foreign Exchange Rates*,[12] provisions and onerous contracts following IAS 37 *Provisions*, *Contingent Liabilities and Contingent Assets,* and insurance contracts liabilities.

Events after the balance sheet date

ESMA also reminds issuers to carefully consider the impact on their financial statements of any material events occurring after the end of the reporting period and to provide the relevant disclosures in accordance with paragraph 16A(h) of IAS 34.

Interim management reports

ESMA calls for consistency between the information disclosed in the interim management report and interim financial statements. Furthermore, ESMA recommends that issuers provide, where relevant and to the extent possible, detailed and entity specific information in their interim management reports regarding:

a) the direct and indirect impact that Russia's invasion of Ukraine and the sanctions imposed had on their strategic orientation and targets, operations, financial performance, financial position and cash-flows (in particular, details of the issuer's liquidity position and its liquidity risk management strategy, decrease of revenues, disruptions in supply chains and/or uncertainties regarding production, exposures to markets, impacts on staff);

b) measures taken to address and mitigate the direct and/or indirect impacts of the Russia's invasion of Ukraine and the sanctions imposed on their operations and performance and their progress/state of completion (including, but not limited to, information of whether issuers have applied or are considering to apply for public

[10] Paragraph 6 to 8 of IFRS 5.
[11] Public Statement, *Considerations on recognition of deferred tax assets arising from the carryforward of unused tax losses*, ESMA32-63-743, 15 July 2019, https://www.esma.europa.eu/sites/default/files/library/esma32-63-743_public_statement_on_ias_12.pdf
[12] In particular, the application of paragraphs 21 and 22 of IAS 21 to determine the appropriate foreign exchange rate.

support measures; details regarding the nature, amounts and conditions of such assistance; risk hedging strategy, actions taken to address cybersecurity); and

c) where available, the expected future impact on the issuers' financial performance, financial position and cash-flows, related risks and contingency measures planned to mitigate the expected future impact and risk and uncertainties identified.

In order to complement the information provided above and to facilitate users' understanding, issuers should also include narrative information regarding the estimates and judgements made as well as assumptions used to determine the future impact of Russia's invasion of Ukraine on the business of the issuer and how the different uncertainties faced affected the estimates made and the strategy undertaken by the issuer.

Finally, ESMA reminds issuers that, in accordance with paragraph 15B (j) of IAS 34 and Article 5 (4) of the Transparency Directive, the interim report shall also include information on related party transactions if they are significant. Where relevant, issuers are encouraged to provide transparency on related party transactions with companies and individuals subjected to sanctions and, where applicable, disclose how those sanctions affect the issuers' operations.