

Implications of the Russian government's invasion of Ukraine

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At a glance

The world continues to focus on the recent events in Ukraine and the devastating impact they have had on the people in that region; their safety and well being continues to be the primary concern of all of us.

The situation has created pervasive uncertainty and risk. The combination of the Russian government's invasion of Ukraine and the resultant sanctions imposed by the US and other governments—which are designed to inflict severe consequences on the Russian economy—are impacting business continuity, liquidity, and asset values in Ukraine and Russia as well as roiling markets worldwide. Consequently, all companies should be assessing the potential accounting and reporting implications.

Senior finance leaders should team with their peers in legal, compliance, and operations to ensure risks that may impact a company's liquidity, operating results, and financial reporting are identified timely and assessed appropriately. In making these assessments and accounting judgments, it is critical that management consider company-specific evidence as well as the broader situation and implications, including the stated intention of the sanctions. While the situation continues to evolve, that uncertainty alone is not a basis to defer accounting recognition of the events that have already occurred (e.g., suspending operations, loss of customers or end markets, current inability of customers or debtors to pay). As a result, we expect that many companies will reflect impairments, valuation allowances, and other write downs in the current period, absent compelling evidence that would suggest otherwise. In addition, companies should ensure robust controls are operating to address the review and documentation of what may be unique accounting and reporting issues.

Further, management should assess the need for transparent disclosure around the impact on current and future financial performance and the related risks and uncertainties. Timely company-specific disclosure is essential, even though it may be difficult to assess or predict the effects of the conflict with precision. Disclosures about the risks, including how the company is responding to them, are expected to be specific to a company's situation as seen through the eyes of management.

This *In depth* was updated on March 31 to add additional questions related to inventory costing, taxes, and depreciation considerations for idle facilities, and to clarify Question 6.1 related to a company's assessment of the need for a valuation allowance on deferred tax assets. Additionally, this *In depth* was updated on April 21 to add Question 2.2 related to consolidation. On May 5 we added Question 6.9 regarding the SEC's new "Dear CFO" letter.



The Russian government's invasion of Ukraine has had profound and immediate impacts on business operations within the conflict zone as well as reverberating more broadly through the world economy. The physical interruption of business operations has been compounded by economic sanctions imposed by the US and other governments, voluntary actions by businesses to cut ties with their Russian operations, and disruptions to commodity exports including oil, natural gas, and wheat.

As companies contemplate upcoming financial reporting, specific matters which may require consideration include:

- [Disruption of operations](#)
- [Impact of Russian laws and regulations](#)
- [Exposure to customers affected by the conflict](#)
- [Supply chain disruptions](#)
- [Volatility in foreign currency and capital markets](#)
- [General reporting considerations](#)

The following list of frequently asked questions is organized by these general sources of accounting and reporting issues. However, these matters are intrinsically interconnected and companies should consider the broad scope of issues in determining the potential impacts on their business. In addition, the final section of the document includes general financial reporting considerations and the accompanying appendix provides a complete list of the questions addressed.

Disruption of operations

Companies with operations, investments, customers, or other business activities in or related to Ukraine may have significant uncertainty around the status of their assets and the continued viability of their operations. In addition, many companies are actively working to support their employees and others in the region, continuing benefits and providing other forms of support.

The impact of US government and other sanctions, as well as voluntary decisions by companies to scale back or exit operations in Russia and relationships with Russian entities, have also created disruption that has accounting consequences.

The issues discussed in this section may apply to companies with operations in Ukraine and Russia and may also be applicable to companies with significant customer or other relationships with companies in that region. Companies with operations in Russia should also assess the accounting impact of Russian laws and regulations described in the [Impact of Russian laws and regulations](#) section.

Impairment of non-financial assets

QUESTION 1.1

Should companies recognize impairments for tangible and intangible assets located in, or dependent on operations in, the conflict zone?

PwC response

Companies should assess whether tangible and intangible assets located in, or dependent on operations in, Ukraine and Russia are impaired as of the balance sheet date. Preparers should think broadly about potential impacts (e.g., the far-reaching sanctions may have unexpected consequences reverberating through capital markets or the supply chain and customer environment). Assets potentially affected include fixed assets, right-of-use assets, goodwill, and intangibles assets. It is critical to have a reasoned judgment (and positive evidence) of how assets impacted by the conflict will be recovered in order to not impair them as of the end of the first quarter of 2022.

In some cases, buildings or other assets may have been damaged or destroyed as a result of the conflict. In other cases, a company's operations or financial performance may be significantly affected by the loss of a significant supplier or customer that has been restricted or eliminated as a result of the conflict, volatility within markets, or other events such as those resulting from international sanctions.

When assessing impairment, a company should distinguish between assets that are damaged and those whose value is impacted by changes in projected cash flows as a result of the conflict. Assets that are destroyed should be written off to expense. Assets that are damaged may need to be written down, or their useful lives may need to be revisited.

Assets impacted by changes in cash flows (e.g., output declines due to reduced demand due to sanctions or otherwise) should be evaluated for impairment. The nature of the impairment test and the level at which assets are tested (i.e., individual asset, asset group, or reporting unit), will vary depending on the type of asset.

ASC 350-20-35-3C and ASC 350-30-35-18B list examples of indicators for when an interim impairment test of goodwill and indefinite-lived intangibles, respectively, may be required and what factors may affect the determination of fair value. ASC 360-10-35-21 includes examples of events or changes in circumstances that may indicate an impairment for definite lived intangibles and other long-lived assets.

Foreign currency considerations

When the impairment assessments are performed at the local entity level in the respective functional currencies, the significant decrease in the Russian ruble and Ukrainian hryvnia by itself may not indicate or result in an impairment.

ASC 360-10 and ASC 830-30-45-13 do not specifically address whether cumulative foreign currency translation adjustments (CTA) included in AOCI should be included when measuring the carrying amount of an asset group

that is held and used. In the absence of specific guidance, we believe that CTA and other amounts included in AOCI should be excluded when measuring the carrying amount of an asset group that is held and used. Such amounts should only be considered when measuring the carrying amount of a disposal group that meets the held for sale criteria. A decrease in the value of a subsidiary's assets measured in US dollars solely due to the foreign currency devaluation would be reflected in the CTA through the consolidation process of the subsidiaries' financial statements.

When a disposal group is classified as held for sale, the carrying amount of the disposal group should include the CTA that will be eliminated upon sale when measuring the disposal group at the lower of its fair value less cost to sell or carrying amount. However, such amounts should remain classified within AOCI until the disposal group's sale date in accordance with ASC 830-30-40-1. See [Section 5.3.3.4](#) in PwC's *Property, plant, equipment and other assets* guide.

When testing the goodwill of a reporting unit for impairment, the carrying amount of the reporting unit should include assets and liabilities at their currently translated amounts in accordance with [ASC 350-20-35-39A](#) (see Example BCG 9-5 in PwC's *Business combinations and noncontrolling interests* guide).

Resources

- PwC's *Property, plant, equipment and other assets* guide, [Chapter 5](#)
- PwC's *Business combinations and noncontrolling interests* guide, [Chapter 9](#)
- [ASC 350](#), *Intangibles—Goodwill and other*
- [ASC 360](#), *Property, Plant, and Equipment*
- [ASU 2017-04](#), *Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*

QUESTION 1.2

What are some of the implications of the conflict and related economic sanctions on the determination of fair value?

PwC response

ASC 820-10-20 defines fair value as: "The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." Inherent in this definition are a number of inputs that may be affected by current events.

Price

Depending on the asset or liability valued, historically available market-based prices may no longer be available, because, for example, the respective markets are affected by global sanctions or the Russian responses to such.

Information used in fair value models, other than market-observable prices, should consider all information that is known or knowable to market participants as of the measurement date, whether that information is obtained prior or subsequent to the balance sheet date. For events that occur after the measurement date that provide information about facts that were not in existence on the measurement date, including market price movements, the

nature and significance of the event may warrant disclosure. This will require the use of professional judgment and should be based on the individual facts and circumstances related to the assessed asset or liability.

To the extent management is determining expected prices based on discounted cash flow analysis and similar valuation methodologies, they should document the significant judgments related to such cash flows and associated uncertainties, including the consideration of various scenarios and the applied valuation methodology. Management will also have to consider the significant uncertainties around inputs such as interest and foreign currency rates.

Principal or most advantageous market

ASC 820-10-35-5 through ASC 820-10-35-6C describe the principal market as the market with the greatest volume and level of activity for the asset or liability from the perspective of a market participant. In the absence of a principal market, the most advantageous market should be used. The most advantageous market is the market that maximizes the amount that would be received to sell the asset or minimizes the amount that would be paid to transfer the liability, after taking into account transaction costs and transportation costs. In evaluating the principal or most advantageous markets, ASC 820 restricts the eligible markets to only those that the company can access at the measurement date.

ASC 820-10-35-6C acknowledges that there may not always be an observable market: “Even where there is no observable market to provide pricing information about the sale of an asset or the transfer of a liability at the measurement date, a fair value measurement shall assume that a transaction takes place at that date, considered from the perspective of a market participant that holds the asset or owes the liability. That assumed transaction establishes a basis for estimating the price to sell the asset or to transfer the liability.”

The conflict and the global reaction to it may cause significant disruption to certain markets and the ability to obtain observable inputs/prices.

Market participant

The above definition of an assumed transaction, in the absence of market-based pricing, puts significant focus on the determination of the appropriate market participants with whom the company would transact. As a result of the conflict, the historically applied perspectives may no longer be valid and certain counterparties may not be available. As such, management will have to assess if historical assumptions are still sustainable or who presently would be a relevant market participant and how that may affect the price or other aspects of determining fair value.

When there is no market available to the company, it may have to determine the characteristics of a market participant to which it would hypothetically sell the asset if it were seeking to do so. Once the market participant characteristics have been determined, the company would identify the assumptions that those market participants would consider when pricing the asset. The company should construct a hypothetical or “most likely” market for the asset based on its own assumptions about what market participants would consider in negotiating a sale of the asset or transfer of the liability.

Resources

- PwC's *Fair value measurements* guide, [Chapter 4](#)
 - [ASC 820](#), *Fair Value Measurements*
-

QUESTION 1.3

Should companies write down inventory located in Ukraine or otherwise impacted by the conflict?

PwC response

Determining the net realizable value (NRV, or “market” under ASC 330, in the case of LIFO inventories) at the balance sheet date requires consideration of all available data, including changes in prices experienced or anticipated subsequent to the balance sheet date.

Write downs as of an interim period

ASC 270-10-45-6 and ASC 330-10-55-2 require that inventories be written down during an interim period to the lower of cost and NRV unless substantial evidence exists that the NRV will recover before the inventory is sold within the same fiscal year. Situations in which an interim write-down would not be necessary are generally limited to seasonal price fluctuations. Given the significant uncertainties associated with the current market conditions as a consequence of the conflict, we believe it would be challenging for a company to conclude that such substantial evidence exists for inventory intended to be sold in markets impacted by the conflict. Recoveries of such losses on the same inventory in later interim periods of the same fiscal year should be recognized as gains in the later interim period. Such gains cannot exceed previously recognized losses.

As indicated in SAB Topic 5.BB, a write-down of inventory to the lower of cost and NRV at the close of a fiscal period creates a new cost basis that subsequently cannot be marked up based on changes in underlying circumstances after the company's fiscal year end.

Losses on firm commitments

Losses expected to arise from firm, non-cancelable, and unhedged commitments for the future purchase of inventory items should be recognized in a manner similar to a NRV adjustment unless the losses are recoverable through firm sales contracts or other means pursuant to paragraphs ASC 330-10-35-17 through ASC 330-10-35-18.

Subsequent events

A decrease in prices subsequent to the balance sheet date that is not the result of unusual circumstances generally should be considered in determining NRV at the balance sheet date. However, when a specific event results in the loss of value of the inventory, such as discrete governmental actions (e.g., sanctions) or the disappearance of a market due to the conflict which was not reasonably predictable as of the balance sheet date, the inventory would not be impaired as of the balance sheet date and, instead, the impairment loss would be recognized in the same period that the specific event occurred. As such, any losses as a result of the conflict would not be recorded in periods ended prior to February 24. However, in this situation,

companies should consider disclosure of the event and the pending write down in the ensuing accounting period as appropriate.

Resources

- PwC's *Inventory* guide, [Section 1.3](#)
- [ASC 330](#), *Inventory*

Insurance recoveries

QUESTION 1.4

Can companies record a receivable for expected insurance recoveries?

PwC response

Companies may have insurance policies that cover physical damage and losses related to business interruption. An insurance recoverable asset can be recorded when there is an enforceable insurance contract in place that covers the event causing the loss. The timing of the initial recognition of an insurance recovery asset depends on assessing the enforceability of the claim under the insurance policy and whether the expected proceeds would result in a recovery of a recognized loss or represent a gain contingency. Under a loss recovery model, a company would recognize a receivable if recovery under the policy is probable. We understand that some property insurance companies and similar market participants have already communicated their position that the conflict represents force majeure or claim that “act of war” or other similar exemptions in the relevant policies apply. As such, we believe it may be challenging for an insured party to conclude that any insurance proceeds are probable until agreed to by the insurance carrier. Amounts in excess of recorded losses should be accounted for as gain contingencies and therefore are not recognized until realized or realizable.

Investments accounted for by the equity method

QUESTION 1.5

What are potential accounting considerations for equity method investments located in, or dependent on operations in, Ukraine or Russia?

PwC response

Companies holding equity method investments located in, or dependent on significant operations in, Ukraine or Russia should assess whether an impairment charge should be recorded due to an other-than-temporary impairment (OTTI) of the investment as of the balance sheet date. The unit of

account for assessing impairment is the carrying value of the investment as a whole.

All available evidence should be considered in assessing whether a decline in value is other than temporary. The relative importance placed on individual factors may vary depending on the situation. Factors to consider in assessing whether a decline in value is other than temporary include:

- the length of time (duration) and the extent (severity) to which the market value has been less than cost,
- the financial condition and near-term prospects of the investee, including any specific events that may influence the operations of the investee, such as changes in costs for raw materials for their product or decreases in demand for their products that may affect the future earnings potential, and
- the intent and ability of the investor to retain its investment in the investee for a period of time sufficient to allow for any anticipated recovery in market value (e.g., a decision to divest an investment in a Russian oil and gas enterprise would likely affect this assessment).

Consideration should also be given to the reasons for the impairment and the period over which the investment is expected to recover. The longer the expected period of recovery or the greater the uncertainty associated with recovery, the stronger and more objective the positive evidence needs to be in order to overcome the presumption that the impairment is other than temporary. Given the circumstances in the conflict zone, it may be difficult to support an assertion that a decline in value is other than temporary.

Once a determination is made that an OTTI exists, the investment should be written down to its fair value, which establishes a new cost basis. The use of an “undiscounted cash flow” approach is not an appropriate means of assessing the amount of an impairment charge. In addition, bifurcation of declines in value between “temporary” and “other than temporary” is not allowed.

Timing of assessment

Fair value is determined at the reporting date for the purposes of an impairment, regardless of whether the investor accounts for the investment on a lag. Therefore, subsequent declines or recoveries after the reporting date are not considered in the determination of fair value. A previously recognized OTTI cannot subsequently be reversed if fair value increases above the carrying amount.

Consideration of cumulative translation adjustment balances

An investor may have an equity method investment in, or within, a foreign entity and a related cumulative translation adjustment balance. Unless an entity has committed to a plan that would cause reclassification of some amount of CTA into earnings (i.e., the equity method investment is a part of disposal group classified as held for sale), any effects from foreign currency translation adjustments should be excluded from the carrying value of an equity method investment when assessing it for impairment. See [Section 8.4](#) in PwC’s *Foreign currency* guide.

Resources

- PwC's *Foreign currency guide*, [Chapter 8](#)
 - PwC's *Equity method investments and joint ventures guide*, [Chapter 4](#)
-

Payments to employees

QUESTION 1.6

How should companies account for payments made to or benefits provided to employees displaced by the conflict?

PwC response

Companies may choose to continue to pay salaries and benefits to employees even if they are unable to work or have been displaced.

The accounting guidance for payments to employees varies and depends on the nature of the compensation arrangement and the way in which they are communicated to employees.

- Certain types of payments are accrued either as service is provided or when the events giving rise to the payments become probable and the amounts are estimable in accordance with ASC 712 (e.g., pre-existing plans to continue to provide medical benefits to furloughed employees or provide paid severance benefits for permanent termination of employment that varies based upon years of service).
- Special termination benefits offered for an employee's voluntary termination of service would be recognized when the employee irrevocably accepts the offer.
- One-time involuntary termination benefits would not be recognized until the criteria in ASC 420 are met and may be recognized over time if continued service is required to earn the benefit.

Management should evaluate the arrangements to determine whether one of the accounting models described above specifically applies to those payments.

For payments to employees that are not clearly addressed by the existing accounting models, judgment will be required.

- *Decision to pay salaries to employees unable to work* - A company's discretionary decision to continue to pay salaries to employees unable to work might be similar to the continuation of compensation and benefits under ASC 712. However, because the employees' rights to that compensation do not vest or accumulate based on past service, they would be accrued when they are probable and estimable, in accordance with ASC 450, *Contingencies*. Under this approach, the communication of the company's intention to continue to pay salaries for a period of time to employees who are displaced or otherwise unable to work could lead to a determination that the payment of such amounts are probable. Significant judgment would

be needed in the determination of what amounts are reasonably estimable.

- The continued payment of salaries to employees unable to work could alternatively be seen as a discretionary one-time action, in which case it would not represent a mutually understood “plan.” Under this view, payments of salaries to employees who were unable to work due to government-imposed restrictions on access to facilities are expensed as incurred, unless the criteria for accrual for compensated absences are met. In most cases, the criteria would not be met, as the right to these payments did not vest or accumulate based on past service. Therefore, the payments would be expensed as incurred.
- If accrual of future compensatory payments is considered appropriate, management needs to assess whether any of the payments, or portions thereof, will provide any current benefit to the company. ASC 710-10-25-4 prohibits the accrual of future costs that will provide a benefit to the employer as they are incurred. In this context, while employees may not be directly providing services, the payments may be designed to keep the company’s active workforce available when the company is able to re-commence operations. In that case, recognizing the cost of the employee compensation as paid, rather than accruing an estimate of the total amount to be paid at the point at which employees ceased working, may be appropriate.
- Companies may also decide to make advance payments to employees for humanitarian reasons. Management will have to consider the likelihood of those employees actually being able to return and perform services in exchange for those prepaid salaries and benefits. Unless it is probable that the employees will provide future services thus supporting recognition of a prepaid asset, which may be difficult to assess at this juncture, such payments would be expected to be expensed as paid.

Based on the above considerations, we generally believe that arrangements that are not covered by a “substantive plan” and under which the rights to compensation do not vest or accumulate based on past service would result in recognizing the related payments as an expense when the payment is made.

This assessment would be appropriate for any type of continued payments to employees who are unable to work including, for example, salary, medical benefits, other fringe benefit costs, vacation accruals, and stock-based compensation.

Resources

- [ASC 710](#), *Compensation*
 - [ASC 712](#), *Compensation - Nonretirement postemployment benefits*
 - [ASC 420](#), *Exit or Disposal Cost Obligations*
 - [ASC 450](#), *Contingencies*
-

Idle facilities

QUESTION 1.7 (Added March 31)

If production facilities are idle, should a company consider changes in depreciation?

PwC response

Depreciation ceases when an asset is derecognized or when the asset is classified as held for sale in accordance with ASC 360-10-35-43. Facilities that are temporarily vacant or idle due to the conflict or related sanctions should continue to be depreciated. However, if an asset or component of an asset remains idle for more than a short period of time, it may indicate a potential impairment or demonstrate the need to reassess the asset's useful life.

Impact of Russian laws and regulations

The economy in Russia has been severely impacted by the combination of US and other government sanctions against Russia as well as voluntary actions by companies to halt their Russian operations or trade. In addition, Russian laws and regulations may affect accounting conclusions in areas such as consolidation.

The questions below are specific to the impact of Russian laws and regulations or sanctions imposed by the US and other governments. Companies with operations in, or dependent on, Russia should also consider the accounting issues highlighted in the "Disruption of operations" as these matters may apply to Russian operations.

Deconsolidation

QUESTION 2.1

How does the Russian government's invasion of Ukraine and related sanctions imposed by the US and other governments potentially affect consolidation assessments for entities located in Russia and Ukraine?

PwC response

Pursuant to ASC 810, *Consolidation*, a reporting entity consolidates another entity if it has a financial interest and ability to exert control over such entity. The conflict and related sanctions may affect the assessment of whether a reporting entity continues to have control over entities in the region.

Evidence of a lack of control, in spite of the legal ownership of a subsidiary's outstanding equity, includes a parent's inability to repatriate funds of a subsidiary because of long-term exchange restrictions, political uncertainties, threats of expropriation of a subsidiary's assets, and other similar situations.

As sanctions around Russian financial institutions continue to rise, the Russian government has maintained a regime of strict currency controls. Multinational companies should expect to face significant difficulties in repatriating earnings from Russian entities as there continues to be significant uncertainty about exchange rates, the amount that can be repatriated at a given exchange rate, and the timing of repatriation as inflation rises within Russia. These difficulties should be considered when assessing whether there continues to be a controlling financial interest in Russian subsidiaries.

In the past, for example in respect to the currency crisis in Venezuela, the International Practices Task Force of the SEC Regulations Committee of the Center for Audit Quality (IPTF) and its discussions with the SEC staff have provided valuable insights on the regulators perspective regarding consolidation. While private entities are not subject to the SEC's regulations and interpretations, the IPTF deliberations may still provide valuable insights. The IPTF has not yet addressed the current conflict specifically.

In the absence of further guidance, we believe that short-term disruptions to the ability to repatriate funds or communications with local management would by themselves not be expected to result in deconsolidation. However, the Russian response to global sanctions is increasing in severity. Russia has proposed a draft law which is a first step in potential nationalization of assets or entities in certain circumstances. Depending on how this situation evolves, there may be a de facto loss of ability to make significant decisions by the parent and hence deconsolidation may be appropriate.

We expect that a reporting entity's decision to deconsolidate its operations would, at a minimum, be supported by considering the following:

- The inability to access various exchange mechanisms at the level required by the scope and size of its operations
- The demonstrated impact of government regulations on the reporting entity's decision-making authority, including its ability to manage the capital structure, product development, purchasing, production scheduling, product pricing, and labor relations
- An evaluation of the current political and economic situation

Furthermore, companies may experience such significant financial difficulties from the conflict that they are forced to enter into the local equivalent of a bankruptcy process. In such a case, management will have to assess the applicable legal framework and if the parent still maintains control over the bankrupt entity or if deconsolidation is appropriate at that point.

If deconsolidation is deemed appropriate *within* a foreign entity (i.e., a portion of a foreign entity), the parent would not release any of its cumulative translation adjustment (CTA) from AOCI into earnings unless such deconsolidation represents a complete or substantially complete liquidation of the foreign entity. In contrast, if it is deemed a deconsolidation event of a foreign entity, the parent would release all of its CTAs related to the derecognized foreign entity, even when a noncontrolling investment is retained. See Chapter 8 in PwC's *Foreign currency* guide for additional information regarding this determination.

Resources

- PwC's *Foreign currency* guide, [Chapter 8](#)
 - PwC's *Consolidation* guide
 - PwC's *Bankruptcy and liquidations* guide, [Section 3.18](#)
 - [ASC 810](#), *Consolidation*
 - [ASC 830](#), *Foreign Currency*
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QUESTION 2.2 (Added April 21)

How should call options and other contractual arrangements to recover a disposed business be considered in a reporting entity's deconsolidation assessment?

PwC response

In connection with the disposal of its operations in Russia due to the geopolitical situation, a reporting entity may negotiate terms that allow it to reacquire such operations if the situation changes. These repurchase rights may be structured as call options or rights of first refusal and may specify a repurchase price at fair value, a fixed price, or based on a formula.

Upon disposal of such operations, a reporting entity will need to assess if it lost control and hence should derecognize the related assets and liabilities from its balance sheet. The existence of call options could affect that assessment and should be considered in several steps of the de-consolidation assessment:

- *Variable interest:* A call option at other than fair value written by the new owner of the disposed business may represent a variable interest retained by the reporting entity.
- *Determining if the disposed entity is a variable interest entity (VIE):* A call option at other than fair value would limit the new equity holder's participation in the economics of the disposed business (i.e., because the new equity holders may be required to sell their investment in the future at less than fair value). The call option would need to be considered in the determination of whether the disposed business is a VIE pursuant to [ASC 810-10-15-14\(b\)\(3\)](#).
- *Determination of the primary beneficiary:* If the disposed entity is a VIE, the reporting entity would need to determine the primary beneficiary, which includes determining whether the call option conveys the power to direct the activities that most significantly impact the economic performance of the VIE to the holder. When making this assessment, the holder should consider the voting rights exercisable through the shares underlying the option, as well as any other rights that may transfer to the holder upon exercising the option. As further described in [Section 5.3.5](#) of the *Consolidation* guide, we believe that the following factors should be considered in making this evaluation:
 - Whether the option is currently exercisable
 - The strike price and other key terms of the call option

- The substance of the call option
- The overall level of control held by the holder of the option
- Barriers to exercise the option
- Conditions that make exercise not prudent, feasible, or substantially within the control of the holder

The determination of the primary beneficiary is a continuous assessment and hence many of the factors noted above require continuous monitoring by a reporting entity.

To the extent the disposed business is not a VIE, the reporting entity's loss of control should be evaluated under the voting interest model. A call option or similar contractual terms would typically not impact this assessment as the voting interest entity model is not an effective control model. However, in certain limited circumstances, the terms and conditions of a repurchase option may make them so highly likely of exercise that a reporting entity may be deemed to have a controlling financial interest in the entity even though the instruments have not been exercised. In making this assessment, a reporting entity should consider all facts and circumstances, including its relationships with the entity and other investors.

Resources

- PwC's *Consolidation guide*, [Section 3.3.3](#), [Chapter 4](#), [Section 5.3.5](#), and [Section 7.2.3](#)

Stock compensation and share-settled agreements

QUESTION 2.3

How do recent Russian Presidential Decrees impact the accounting for potentially share-settled agreements (e.g., convertible debt or equity instruments)?

PwC response

The recent adoption of Russian Presidential Decree No. 81, "On Additional Temporary Measures of Economic Nature to Secure Financial Stability of the Russian Federation," on March 1, which follows decree No. 79, "On the Application of Special Economic Measures in Connection with the Unfriendly Actions of the United States of America and Foreign States and International Organizations who have Joined the United States of America" on February 28, may restrict the ability to transfer securities to residents of Russia. Companies should evaluate the potential impact these decrees may have on their arrangements with potential share-settlement features, such as convertible debt or equity instruments, contingent consideration in a business combination, warrants and other derivatives, and other equity-linked transactions. (See Question 2.3 for considerations related to stock-based compensation arrangements.)

The decrees are not particularly specific, and companies may need to obtain legal counsel's advice on how the decrees apply to their specific transactions. If it is determined, for example, that an existing arrangement cannot legally be settled in shares and, thus, settlement in cash or other assets is required, the arrangement may need to be reclassified to a liability or asset. While GAAP provides for a number of different accounting models depending on the specific circumstances and context, frequently such liabilities or assets are required to be recognized at and periodically remeasured to fair value. Furthermore, the change in the manner of required settlement of the transaction may impact a company's calculation and presentation of earnings per share.

Resources

- PwC's *Financing transactions* guide, [Chapter 5](#), [Chapter 6](#), [Chapter 7](#), and [Chapter 8](#)
- PwC's *Financial statement presentation* guide, [Chapter 7](#)
- PwC's *Business combinations and noncontrolling interests* guide, [Section 2.6.4.2](#)
- [ASC 260](#), *Earnings per Share*
- [ASC 805-30-25-5](#), *Business Combinations*
- [ASC 480](#), *Distinguishing Liabilities from Equity*
- [ASC 815](#), *Derivatives and Hedging*

QUESTION 2.4

How do recent Russian Presidential decrees impact the accounting for stock-based compensation?

PwC response

The recent adoption of Russian Presidential Decrees No. 79 and No. 81 may restrict the ability to transfer securities to residents of Russia (see Question 2.2).

Companies should evaluate the impact these decrees may have on existing share-based compensation arrangements with employees and others who reside in Russia. If it is determined, for example, that an existing arrangement cannot be settled in shares and thus settlement in cash or other assets is likely, the arrangement may need to be reclassified as a liability. See further discussion of equity-to-liability modification accounting in [Sections 3.3.4](#) and [4.4.1](#) of PwC's *Stock-based compensation* guide.

Exposure to customers affected by the conflict

Even companies without operations located in the conflict zone may have accounting considerations from the Russian government's invasion of Ukraine due to its direct and indirect impact on their customers. For example, companies will need to consider the collectibility of accounts receivable and assess whether revenue can be recognized for new or ongoing transactions with impacted customers. Other indirect impacts may include the inability of

counterparties to perform on supply or purchase agreements or impairment of assets used to produce goods or services for companies in the conflict zone.

Contracts with customers

QUESTION 3.1

How could revenue recognition be impacted by the disruption caused by the conflict?

PwC response

We believe revenue recognition may be affected in several ways due to the conflict, among them, collectibility of consideration and estimates of variable consideration.

If a company concludes it is not probable it will collect substantially all of the consideration it is entitled to for a new contract with a customer, ASC 606, *Revenue from Contracts with Customers*, precludes the recognition of revenue for such contract. Similarly, for contracts that are currently in process, a significant change in facts and circumstances, such as a significant deterioration in a customer's ability to pay or request for extended payment terms, would be an indicator that a company should reassess whether it is probable that it will collect the remaining consideration under the contract for future goods and services. Revenue recognized for goods and services transferred prior to a significant change in facts and circumstances (e.g., prior to the conflict) is generally not adjusted, unless the company concludes it has or intends to provide a price concession related to those sales.

A customer's ability or intention to pay consideration may be affected by interrupted operations or by the implemented sanctions and Russia's response to such. For example, certain Russian banks' access to the SWIFT system has been limited. The limitations on the SWIFT system mean that alternative payment mechanisms must be used to transfer funds within the banking system and this could limit the ability of customers to pay loans, settle receivables, or receive funds, and hence impact the customer's cash flows or liquidity. Companies may also have limitations on the ability to access deposits in the Russian banking system.

The assessment of a customer's ability to pay should consider not only the direct impacts of the conflict on counterparties, but also the impacts of the sanctions imposed by various regimes. For example, a company may believe they are not impacted by the conflict as their customers are all in the US and western Europe, but fail to recognize that its major customers' generate their revenue substantially from Russia and, therefore, their customers' products may be subject to sanctions. This may raise uncertainties regarding the ability of these customers to pay consideration when it becomes due, even though such customers are not physically located in the conflict region.

If a company continues to sell products and services to a customer when it is uncertain whether collection is probable—due to the potential deterioration of its customer's financial position or that customer's current inability to settle outstanding receivables—the question arises as to whether revenue can be

recognized on new transactions with that customer. ASC 606 requires a company to first consider any potential price concessions that it expects to provide, which reduce the transaction price, before assessing collectibility. Additionally, as part of the collectibility assessment, a company should consider whether it has the ability and intent to cease providing service if the customer fails to pay. In many cases it may be challenging to conclude that collection for new sales is probable when the customer has been unable to pay existing receivables. Importantly, contracts with and receivables from customers in the affected region or with significant exposure to that region, warrant new and careful consideration in the current environment even if the customer has a strong history of payment. This type of situation requires judgment and is dependent upon facts and circumstances; however, if a company cannot conclude collection is probable, it cannot recognize revenue from the arrangement.

If a company concludes collection is not probable, it should continue to reassess this conclusion each reporting period as collection may become probable at a later date. If collection is not probable, but the customer subsequently makes a payment, revenue can only be recognized when one or more of the following occurs:

Excerpt from ASC 606-10-25-7

- a. The entity has no remaining obligations to transfer goods or services to the customer, and all, or substantially all, of the consideration promised by the customer has been received by the entity and is nonrefundable.
- b. The contract has been terminated, and the consideration received from the customer is nonrefundable.
- c. The entity has transferred control of the goods or services to which the consideration that has been received relates, the entity has stopped transferring goods or services to the customer (if applicable) and has no obligation under the contract to transfer additional goods or services, and the consideration received from the customer is nonrefundable.

The potential disruption to supply chains or the “normal course of business” upon which many estimates of variable consideration may have originally been based will likely necessitate a reassessment of variable consideration in a variety of contexts. Under ASC 606, management determines the total transaction price, including an estimate of any variable consideration, at contract inception and reassesses this estimate at each reporting date until the uncertainty is resolved. Variable consideration is included in the transaction price only to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. The transaction price is recognized as revenue when, or as, the related performance obligation is satisfied.

Variable consideration takes many forms, including volume discounts, rebates, returns, refunds, and royalties. Consideration is also variable if it is contingent on a future event occurring or not occurring, such as meeting performance goals (early completion bonus or commercialization milestone) or failing to meet a contractual deadline (liquidated damages), or a customer achieving a certain outcome, such as a distributor meeting a target level of

gross margin upon resale. Estimates of variable consideration should be updated as facts and circumstances evolve. Any changes in the transaction price would be allocated to all performance obligations in the contract unless the variable consideration relates only to one or more, but not all, of the performance obligations.

QUESTION 3.2

What should companies consider when modifying contracts or terminating relationships with customers in Russia?

PwC response

Contracts with customers may be modified or terminated as a result of a decision to exit operations in Russia or other current events. A modification is a change in the scope of the contract, the price of the contract, or both. A modification is accounted for as a separate contract only if distinct goods or services are added to the contract for a price equal to standalone selling price (adjusted for contract-specific circumstances). The accounting for a modification that is not a separate contract depends on whether the remaining goods or services are distinct from the goods or services transferred before the modification:

- If the remaining goods or services are not distinct (e.g., a single performance obligation is being modified), the modification is accounted for on a cumulative catch-up basis. Estimates of the transaction price and measure of progress are updated and cumulative revenue recognized is adjusted (increased or decreased) accordingly.
- If the remaining goods or services are distinct (including goods or services that are part of a series), the modification is accounted for prospectively as if it were a termination of the existing contract and the creation of a new contract. The sum of: (a) unrecognized consideration from the original contract and (b) additional consideration promised as part of the modification is allocated to the remaining goods or services to be provided based on relative standalone selling prices as of the modification date.

The partial or complete termination of a contract will typically also be accounted for as a modification as it is a change to the scope and price of the contract. Companies should consider any penalties, refunds, or other payments it may be liable for upon contract termination, particularly if a company unilaterally ceases performing, which may constitute a breach of contract. This will often be a legal determination and require evaluation of contract termination rights, force majeure clauses, and contractual remedies upon breach of contract. Payments made to a customer are presented as a reduction of revenue in accordance with ASC 606-10-32-35 unless the payment is in exchange for a distinct good or service received from the customer. Companies should also evaluate in which period any contract liabilities (i.e., deferred revenue) related to a terminated contract have been satisfied through performance or otherwise extinguished. Judgment may be required to determine when such amounts can be recognized and whether they represent additional revenue from the contract or other income.

Resources

- PwC's *Revenue from contracts with customers* guide, [Section 2.6.1](#), [Section 2.6.2](#), [Section 2.6.3](#), [Section 2.9](#), and [Section 4.2](#)
 - [ASC 606](#), *Revenue from Contracts with Customers*
-

Receivables

QUESTION 3.3

How should companies consider the conflict in developing their estimate of current expected credit losses (CECL) for customer receivables?

PwC response

The CECL model requires companies to consider current conditions and reasonable and supportable forecasts in developing an estimate of expected credit losses. This estimate requires the use of judgment, especially in times of economic uncertainty. Absent changes in circumstances, we expect that companies will likely recognize additional allowances for credit losses related to their trade receivables, loans, and other amortized cost balances connected to Russia and Ukraine.

Beginning in February, companies should update their models and estimates to reflect the revised economic outlooks due to the direct effects of the conflict as well as implications arising from the implemented or announced sanctions (e.g., the inability to collect loans or accounts receivable due to sanctions on Russia's banking system - see further discussion in Question 3.1), perform sensitivity analyses based on the new forecasts, adjust probability weighting on alternative scenarios, and consider qualitative adjustments.

Companies should also consider the impact of current conditions and economic forecasts relating to specific sectors, geographical areas, and borrower-specific exposures. Factors to consider include whether models reflect specific risks, whether data used in estimates (e.g., ratings or other indicators) reflect current conditions and reasonable and supportable forecasts, and changes in the value of any collateral.

In addition, the CECL model requires consideration of all of the effects of a troubled debt restructuring (TDR) on estimated credit losses when it has a reasonable expectation at the reporting date that it will execute a TDR with the borrower.

Disclosure

In addition, companies should consider transparent disclosures on the impact of the subsequent developments, including the assumptions used, and their impact on the estimate for credit losses, to the extent deemed material.

Resources

- PwC's *Loans and investments* guide, [Chapter 7](#)
 - [SEC Staff Accounting Bulletin No. 119](#) (Topic 6.M)
-

Supply chain disruptions

Supply chain disruptions stemming from the COVID-19 pandemic may be further exacerbated by the Russia-Ukraine conflict. For example, supply contracts with companies located in Russia may be interrupted by the economic sanctions imposed by the US and other governments. Due to Russia's limited access to the SWIFT system, companies purchasing goods from Russia will also find it more difficult to pay Russian payables on a timely basis.

The accounting considerations discussed below may also apply to other contractual relationships such as sales commitments.

QUESTION 4.1

What is the impact of the change in the probability of a hedged forecasted transaction?

PwC response

Companies that have designated forecasted transactions in cash flow hedging relationships, such as raw materials purchases, sales or revenues, debt issuances, or interest payments, may experience a delay in the occurrence of the actual transaction as compared to the forecasted date as a result of the conflict, the related economic sanctions, or the voluntary withdrawal of operations from Russia.

The accounting impact will depend on the likelihood of the forecasted transaction occurring within two months of the originally specified time period:

- *Transaction is still probable of occurring* - If the forecasted transaction is probable of occurring by the end of the originally specified time period (or within an additional two-month period), hedge accounting should still be permissible and deferred derivative gains or losses should continue to be reported in accumulated other comprehensive income.
- *Transaction is no longer probable of occurring* - If at any time the likelihood of the hedged forecasted transaction ceases to be probable of occurring, hedge accounting will cease prospectively and all future changes in the fair value of the derivative would be recognized directly in earnings. Any derivative gains or losses deferred in AOCI prior to the change in likelihood will remain in AOCI until the forecasted transaction impacts earnings (or until the forecasted transaction becomes probable of not occurring).
- *Transaction is probable of not occurring* - If a company determines that the hedged forecasted transaction is probable of not occurring by the end of the originally specified time period (or within an

additional two-month period), amounts deferred in AOCI are required to be recognized in earnings immediately.

Due to the far reaching nature of the global sanctions, in assessing the probability of a forecasted transaction, companies should carefully evaluate the potential impact on sales to their counterparties as well as, forecasted purchases of raw materials and other supplies. For example, a customer's products may be subject to such sanctions and in turn the company's forecasted sales to this customer may decrease.

Resources

- PwC's *Derivatives and hedging* guide, [Chapter 7](#)
-

QUESTION 4.2

What is the impact of supply chain disruptions or changes in sales forecasts on the application of the normal purchases and normal sales (NPNS) derivative scope exception to purchases and sales contracts?

PwC response

Some companies apply the derivative scope exception for normal purchases and normal sales to commodity contracts. To qualify for this exception, a company must conclude that it is probable—at inception and throughout the term of the contract—that the contract will not net settle (i.e., physical delivery will occur).

Companies may be prohibited from buying goods from Russia, or may conclude that delivery under “take or pay” contracts is no longer probable due to supply chain disruptions, changes in sales forecasts, or other business developments. Overall market developments in response to the conflict should be closely monitored.

If a company determines that it is no longer probable that a contract will result in physical delivery, it may need to discontinue its application of the NPNS exception. Whether and when a company should discontinue application of the NPNS scope exception partially depends on the form of net settlement (see Figure DH 3.4 in Section 3.2.4.3 of PwC's *Derivatives and hedging* guide).

Resources

- PwC's *Derivatives and hedging* guide, [Chapter 3](#) and [Chapter 10](#)
 - [ASC 815](#), *Derivatives and Hedging*
-

QUESTION 4.3 (Added March 31)

How might idle capacity, decreased production, or increased costs associated with acquiring and moving goods through the supply chain impact inventory costing?

PwC response

[ASC 330-10-30-3](#) through [ASC 330-10-30-4](#) indicates that variable production overhead costs should be allocated to each unit of production on

the basis of the actual use of the production facilities. The allocation of fixed production overhead costs, however, is required to be based on the “normal capacity” of the production facilities, which is defined as the production expected to be achieved over a number of periods under normal circumstances, taking into consideration loss of capacity resulting from planned maintenance. Judgment is required to determine what represents an abnormally low production level and the range of normal capacity will vary based on business and industry factors.

While production from some operations in the conflict zone may have been reduced due to supply chain challenges or the temporary shut down of certain facilities in the affected regions, the amount of fixed overhead costs allocated to each unit of production should not be increased as a consequence of such abnormally low production. Unabsorbed fixed overhead costs should be expensed in the period in which they are incurred.

In addition, ASC 330-10-30-7 requires that abnormal amounts of freight, handling costs, and wasted material (spoilage) be recognized as current period charges and not included in the cost of inventory. Higher than normal or higher than anticipated costs for otherwise routine activities are not “abnormal costs” in this context. In addition, the concept of spoilage refers specifically to goods that are damaged, destroyed, or lost during the production process. Merely incurring higher costs when acquiring inventory from third parties is not considered “wasted materials.” Those higher costs should be capitalized, subject to lower of cost and net realizable value considerations.

Also, companies should consider additional disclosures around the current and expected impact of increased costs on their financial results, particularly those entities that use the last-in, first out (LIFO) inventory cost flow assumption.

Based on SEC guidance, disclosures might include any material adverse impacts on the supply chain or the methods used to distribute products or services and any material changes in the relationship between costs and revenues.

Resources

- PwC's *Inventory guide*, [Chapter 1](#)
- [ASC 330](#), *Inventory*

Volatility in foreign currency and capital markets

Volatility in foreign currency and capital markets may have implications for valuation of financial assets and liabilities held at the balance sheet date. In addition, companies may need to consider whether financial assets are impaired as a result of market changes, economic sanctions, or other current events.

QUESTION 5.1

In determining the fair value of an investment or other financial instrument, can a company adjust or disregard a quoted price in an active market (that is, a level 1 input) in a period of significant market volatility?

PwC response

The objective of “fair value” is to determine a price at which an orderly transaction would take place between market participants under conditions that existed at the measurement date. It would not be appropriate to adjust or disregard observable transactions unless those transactions are determined to not be orderly. Generally, there is a high bar to conclude that a transaction price is not orderly under ASC 820. Although ASC 820-10-35-54I provides a list of factors to consider that may indicate a transaction is not orderly, we believe there is an implicit rebuttable presumption that observable transactions between unrelated parties are orderly and therefore, evidence to the contrary should be incontrovertible. Accordingly, we would expect that the fair value of an investment in an active market would continue to be calculated as the product of the quoted price for the individual instrument times the quantity held (commonly referred to as “P times Q”), even in times of significant market volatility.

As the level and severity of sanctions on Russia continue to evolve, companies will need to consider market conditions relating to securities trading in Russia and whether market participants may no longer be able to access an active market for such shares. Investments that may have previously had an active market and quoted prices may be reduced to level 2 or level 3 inputs for valuation purposes.

See Question 1.2 for considerations related to the determination of fair value.

Resources

- PwC’s *Fair value* guide, [Chapter 7](#)
-

QUESTION 5.2

How should a company determine whether an allowance is necessary for an available-for-sale debt security (post-ASC 326)?

PwC response

An available-for-sale debt security is considered impaired if the fair value of the security is less than its amortized cost basis.

Company does not intend to, and more likely than not will be required to, sell the security

If a company concludes that it does not intend to sell an impaired security (and it is not more likely than not that it will be required to sell the security) before recovery of its amortized cost basis, a company should establish an allowance for credit losses, with an offsetting entry to net income, for any portion of the impairment related to credit losses. This is determined based on an analysis of the present value of contractual cash flows expected to be collected as compared to the amortized cost basis.

The amount of the allowance for credit losses is limited to the amount fair value is less than the amortized cost basis. In practice, in applying the guidance, many companies may evaluate whether an allowance may be necessary based upon qualitative filters (e.g., credit rating). Given current events, those filters may not be sufficient to identify credit losses for periods subsequent to year end. However, it should be noted that a decrease of the fair value due to exchange rate changes in and of itself will not result in an impairment loss.

Company intends to, or more likely than not will be required to, sell the security

If the security is impaired and the company intends to sell the security (or will more likely than not be required to sell the security) before recovering its amortized cost basis, a company should first write off any previously recognized allowance for credit losses with an offsetting entry to the security's amortized cost basis. If the allowance has been fully written off and fair value is less than amortized cost basis, a company should directly write down the amortized cost basis of the asset to its fair value with an offsetting entry to net earnings.

Resources

- PwC's *Loans and investments* guide, [Chapter 8](#)
- [ASC 326](#), *Financial Instruments—Credit Losses*

QUESTION 5.3

For held-to-maturity and available-for-sale debt securities, how should companies consider whether declines below carrying value are other than temporary (pre-ASC 326)?

PwC response

An investment in a debt security is considered impaired if the security's fair value is less than its amortized cost at the balance sheet date. Prior to the adoption of the credit losses standard, if impairment exists, the accounting and reporting model, including the determination of whether that impairment is "other than temporary," differs depending on the facts and circumstances.

If a debt security is impaired (i.e., the security's fair value is less than its amortized cost at the balance sheet date), additional analysis is needed to determine whether the impairment is temporary or other than temporary:

- If an investor intends to sell or it is more likely than not the investor will be required to sell an impaired debt security, the impairment is considered to be other than temporary. The impairment would be measured as the difference between fair value and amortized cost.
- If an investor does not intend to sell the impaired debt security, the investor must consider available evidence to assess whether it will more likely than not (MLTN) they will be required to sell the security before the recovery of its amortized cost basis (e.g., whether its cash or working capital requirements, or contractual or regulatory obligations, indicate the security will be required to be sold before a forecasted recovery occurs).

- If the investor does not intend to sell the impaired security but MLTN will be required to sell the security before recovery of its amortized cost basis, the impairment is considered to be other than temporary. The impairment would be measured as the difference between fair value and amortized cost.
- If the investor does not intend to sell the impaired security and it is not more likely than not that the investor will be required to sell the impaired security, an analysis should be performed to determine whether a credit loss exists. If the present value of the cash flows expected to be collected is less than the amortized cost basis of the security, the entire amortized cost basis of the security will not be recovered (i.e., a credit loss exists), and an other-than-temporary impairment is considered to have occurred. The impairment recorded in earnings would be based on the difference between the amortized cost basis and present value of future cash flows. In practice, in applying the guidance, many companies may evaluate whether an impairment is necessary based upon qualitative filters (e.g., credit rating). Given current events, those filters may not be sufficient to identify credit losses incurred.

Resources

- PwC's *Loans and investments* guide, [Chapter 8](#)

QUESTION 5.4

How does the conflict impact the accounting for equity instruments when a company applies the measurement alternative under ASC 321?

PwC response

When a company elects the measurement alternative in ASC 321, the equity interest is recorded at cost, less impairment. The carrying amount should be subsequently remeasured to its fair value when observable price changes (i.e., observable prices in orderly transactions for an identical or similar investment of the same issuer) occur as of the date the transaction occurred or it is impaired. Companies should be alert for observable transactions as investors may be adjusting their investment strategies in light of the political and economic consequences of the conflict.

An ongoing assessment will need to be performed to determine whether an equity interest for which the measurement alternative has been elected has become impaired.

In assessing an equity investment for impairment, the measurement alternative model does not include a significance threshold or the ability to avoid an impairment if a company believes the decline in fair value is temporary. The impairment model under ASC 321 is a one-step impairment model under which a company should compute the fair value of an equity investment in accordance with ASC 820 if it has reason to believe the investment's fair value is below the carrying value. If the equity investment's fair value is below the carrying value, the company must reduce the carrying amount of the equity interest to fair value and record the difference in net income.

Resources

- [ASC 321](#), *Investments—Equity Securities*
 - [ASC 820](#), *Fair Value Measurement*
-

General reporting considerations

Companies should be aware of a variety of other general reporting considerations related to the Russian government’s invasion of Ukraine and related events. Companies that record pre-tax adjustments as a result of the conflict will also need to consider the tax effects as well as the impact of changes in operations on the estimated annual effective tax rate. Further, there are existing SEC requirements that may call for incremental disclosures related to the conflict in Ukraine in interim and annual SEC filings. We also discuss a company’s assessment of subsequent events in this context.

Income taxes

QUESTION 6.1 (Updated March 31)

How does the conflict impact a company’s assessment of the need for a valuation allowance on deferred tax assets?

PwC response

When assessing the realizability of deferred tax assets, ASC 740 requires the consideration of “all available evidence,” which may at times include subsequent events. However, not all subsequent events should factor into determining the need for a valuation allowance. Namely, we do not believe that the impact of the conflict on a company’s operations represents information that should be considered in valuation allowance assessments performed for periods ended prior to February 24.

However, the impact of the conflict on a company’s operations will have to be considered in valuation allowance assessments for periods ending after February 24. Further, in interim periods, companies will need to consider how any change in valuation allowance should be reflected: (1) discretely in the period in which judgment is changed or (2) through the effective tax rate.

In accordance with ASC 740-270, reporting entities should include changes in valuation allowance in determining the annual effective tax rate for interim periods during the year when the change relates to (1) deductible temporary differences and carryforwards expected to originate during the current year and (2) decreases to the beginning -of-year valuation allowance caused by anticipated current year income. However, if the change in valuation allowance (1) increases the beginning-of-year valuation allowance as a result of a change in expectations about current year income, or (2) is a result of an change in expectation about income in future years, the change in the valuation allowance should be recognized discretely in the interim period in which the change occurs.

QUESTION 6.2

For purposes of interim reporting, how should a company estimate its annual effective tax rate if it is unsure how the conflict will impact operations?

PwC response

At each interim period, a company is required to estimate its forecasted full-year annual effective tax rate (AETR). That rate is applied to year-to-date ordinary income or loss in order to compute the year-to-date income tax provision. In order to compute the AETR, a company needs to estimate its full year ordinary income and its total tax provision, including both current and deferred taxes. When a company is subject to tax in multiple jurisdictions, one overall (i.e., worldwide) estimated AETR is developed and applied to consolidated ordinary income (loss) for the year-to-date period.

Given the financial impact of the conflict, it may be relevant for companies to consider [ASC 740-270-30-18](#), which indicates that if a reliable estimate cannot be made, the actual effective tax rate for the year-to-date period may be the best estimate of the annual effective tax rate. Two additional exceptions may also be relevant:

- When a company operates in a jurisdiction that has generated ordinary losses on a year-to-date basis, or anticipates an ordinary loss for the full fiscal year, and no benefit can be recognized on those losses, the company should exclude that jurisdiction's income (or loss) from the overall estimate of the AETR. In effect, any jurisdictions with losses for which no benefit can be recognized are removed from the base calculation of the AETR and a separate AETR is calculated for that jurisdiction.
 - When a company cannot make a reliable estimate of ordinary income for a particular jurisdiction, that jurisdiction should be excluded from the overall computation of the estimated AETR and a separate discrete calculation of its tax provision should be made. Determining whether an estimate is reliable requires the use of professional judgment. For example, in some cases, a small change in a company's estimated ordinary income could produce a significant change in the AETR. This might occur when a company that is anticipating only marginal pre-tax book profitability for the year has significant permanent differences that could result in wide variability in the tax expense (benefit) and, in turn, the AETR. In such cases, an estimate of the AETR would not be reliable if a small change in ordinary income were likely to occur. While there is a general presumption that companies will be able to make a reliable estimate of ordinary income, exceptional circumstances can exist in which a genuine inability to make a reliable estimate justifies exclusion of a jurisdiction from the worldwide effective tax rate. A company's assertion that it cannot develop a reliable estimate should be consistent with its other disclosures and communications to its investors, creditors, and other financial statement users.
-

QUESTION 6.3

What other potential tax accounting implications may companies encounter as a result of the conflict?

PwC response

The Russian government's invasion of Ukraine creates a number of pre-tax impacts that companies will need to assess for related tax accounting consequences. For example, the impairment of tangible and intangible assets may have an impact on a company's deferred taxes. The deferred tax accounting in connection with goodwill impairments can be particularly complex in certain instances.

In addition to the related tax accounting impacts of pre-tax items, companies may also have to consider any impact to their assertions with regard to deferred taxes on the outside basis difference in foreign subsidiaries in impacted territories. With the unprecedented international sanctions imposed against Russia, foreign investors and companies alike are faced with not only restrictions on the ability to extract cash, but also decisions of whether to exit business operations in certain markets. As prescribed in ASC 740-30-25-17, the presumption that all undistributed earnings will be transferred to the parent entity may be overcome and no income taxes accrued by the parent for entities that can evidence that a subsidiary has invested or will invest undistributed earnings indefinitely or that the subsidiary's earnings will be remitted in a tax-free liquidation. This non-recognition of a deferred tax liability for outside basis differences is an exception to ASC 740's model for the comprehensive recognition of deferred taxes for temporary differences. Therefore, an enterprise availing itself of that exception must continuously assert its intent to indefinitely reinvest its outside basis difference. Given the conflict, management should consider whether there are any changes to their assertions concerning their ability and intent to indefinitely prevent the outside basis difference of a foreign subsidiary from reversing with a tax consequence. Entities that are unable to assert indefinite reinvestment must record a deferred tax liability for any taxable temporary differences that would be incurred when the outside basis difference reverses.

It is important to remember that the indefinite reversal exception only applies to the transfer of unremitted earnings across national boundaries, and not for transfers of unremitted earnings between entities within the same foreign country (or consolidated/group tax return). As a result, management needs to consider book-over-tax outside basis differences within each legal entity in its organization.

US GAAP also prohibits a company from recording a deferred tax asset on its outside basis differences under ASC 740-30-25-9 unless the deferred tax asset will reverse in the foreseeable future. Generally "foreseeable future" is considered to be one year. In the case of a sale of a subsidiary, we believe that in most cases, such a deferred tax asset should be recognized when the held-for-sale conditions of ASC 360-10-45-9 are met.

Resources

- PwC's *Income taxes* guide, [Chapter 5](#), [Chapter 10](#), [Chapter 11](#), and [Chapter 16](#)

- [ASC 740](#), *Income Taxes*
 - PwC's *Business combinations* guide, [Chapter 9](#)
-

SEC considerations

QUESTION 6.4

What topics related to the conflict might a company consider discussing in a risk factor in an SEC filing?

PwC response

The preparation and disclosure of risk factors is the responsibility of management, often in consultation with the company's legal counsel. Preparing a complete list of material factors that make an investment in the company speculative or risky is not possible. However, some topics that a company might consider discussing in a risk factor include:

- the direct or indirect impact on liquidity, including the inability to transfer funds into Russia for various purposes (e.g., paying employees, suppliers) or repatriate assets due to banking or exchange restrictions; this includes payments from third parties, subsidiaries, and affiliates;
- the direct or indirect impact on operations for companies selling into or obtaining products or commodities from Russia, Ukraine, or other impacted territories;
- supply chain disruptions or increased commodity prices;
- the loss of key customers or suppliers;
- the impact of inflation, considering operations in Russia/Ukraine as well as the global implications;
- the risk of cyberattacks;
- impairments of operations impacted by the conflict (e.g., potential expropriation of operations); and
- impacts on stock price (e.g., due to investor sentiment related to a company maintaining operations in Russia).

Resources

- Regulation S-K [Item 105](#), Risk factors
-

QUESTION 6.5

What type of disclosures relating to the conflict might a company consider addressing in MD&A?

PwC response

When evaluating MD&A disclosures, a company might consider the principle purpose of MD&A, which is to provide material information relevant to an assessment of the financial condition and results of operations of the company, including an evaluation of the amounts and certainty of cash flows from operations and from outside sources. This includes not only how certain events have impacted the company in the past, but also those that are reasonably likely to cause reported financial information not to be necessarily indicative of future operating results or of future financial condition. The disclosure might include descriptions and amounts that are reasonably likely, based on management's assessment, to have a material impact on future operations.

The items that companies might wish to consider addressing in MD&A include some of the same factors described under Question 6.4 relating to risk factors, but with additional analysis of the potential impact to the company including, but not limited to:

- impairment of tangible and intangible assets, including deferred tax assets;
- assets that are at risk of future uncollectibility, impairment, or expropriation, along with implications to underlying businesses/operations;
- adjustment to assets or liabilities carried at fair value;
- the impact on results of operations;
- liquidity implications (either positive or negative);
- the potential accounting implications as well as implications to the business of a decline in value of the ruble; and
- enhancements needed to critical accounting estimates disclosures.

Companies with substantial operations in Russia or Ukraine may want to consider providing discrete summarized or condensed financial information about the businesses/operations in those countries to allow a reader to understand the significance of those businesses/operations and the potential exposure. Given the decline in the value of the ruble, companies might consider disclosing the rate that was used for consolidation and the current rate.

Resources

- Regulation S-K [Item 303](#), Management's discussion and analysis

QUESTION 6.6 (Updated April 29)

What other SEC rules may require specific disclosure related to the conflict?

PwC response

The following portions of Regulation S-K may require disclosure related to the material direct or indirect impact of the conflict, depending on a company's facts and circumstances:

- [Item 101](#), Description of business
- [Item 307](#), Disclosure controls and procedures
- [Item 308](#), Internal control over financial reporting

Some of these matters might need to be considered in connection with both annual and interim reporting. Companies might also consider the applicability of disclosures required by Form 8-K (e.g., under Item 2.05, *Costs associated with exit or disposal activities* or Item 2.06, *Material impairments*).

Instruction 2 to Item 2.01 of Form 8-K defines a disposition for purposes of reporting under that Item. Section 2110.1 of the Division of Corporation Finance Financial Reporting Manual indicates that as used in that instruction, a *disposition* "would include, but not be limited to, a requirement to deconsolidate a subsidiary."

QUESTION 6.7

What if a company is unable to obtain audited financial statements required in an SEC filing as a result of the conflict (e.g., financial statements required by [Rule 3-05](#) and [Rule 3-09](#) of Regulation S-X)?

PwC response

The company may wish to discuss the matter with legal counsel and evaluate the appropriateness of requesting a waiver from the SEC staff under [Rule 3-13](#) of Regulation S-X.

QUESTION 6.8

What are some items to consider if a company decides to prepare and present a non-GAAP financial measure that excludes one or more items related to the conflict?

PwC response

[Item 10\(e\)](#) of Regulation S-K, [Regulation G](#), and related [Staff Compliance and Disclosure Interpretations](#) (C&DIs) should be considered when evaluating any non-GAAP measures. While not an exhaustive list, some items to consider when preparing and presenting non-GAAP information include:

- Not misleading – Non-GAAP information should not be presented in a manner that would be viewed as misleading in the context in which it is presented. While compliance with the rules and guidance referred to above is critical, the SEC staff has reminded companies in its C&DIs that non-GAAP information can be in technical compliance with the various regulations but still be considered misleading.
- Prominence – When a non-GAAP measure is being presented, Regulation S-K requires the most directly comparable GAAP measure to be presented with equal or greater prominence. The staff's C&DIs on non-GAAP measures list certain examples of when

the staff would consider a non-GAAP measure to be presented with more prominence, including:

- a non-GAAP measure that precedes the most directly comparable GAAP measure (including in an earnings release headline or caption) and
 - presenting a full income statement of non-GAAP measures or presenting a full non-GAAP income statement when reconciling non-GAAP measures to the most directly comparable GAAP measures.
- Disclosure – Robust disclosure relating to any adjustments associated with the conflict will be important.
 - A reader should be able to understand the objective of presenting a non-GAAP financial measure that reflects adjustments related to the conflict and what the measure is intended to convey. It would be appropriate to explain why management considers the measure useful and how the measure is useful to an investors' understanding.
 - If management is using the non-GAAP financial measure (e.g., to operate or evaluate the business), the disclosure should address how it is being used (to the extent material).
 - The disclosure should clearly identify the nature of the items that are being adjusted.
 - Consistency – The SEC staff stated in its C&DIs relating to non-GAAP measures that a non-GAAP measure can be misleading if it is presented inconsistently between periods. The company should consider whether there is consistency between periods in any adjustments. If a company does make a change, they should consider disclosing that fact, and whether to recast the non-GAAP measures for prior periods.
 - Income taxes – Consistent with the SEC staff's existing guidance, the gross amount of adjustments should be presented separately from tax effects.

Companies might also consider the following characteristics when evaluating non-GAAP adjustments related to the conflict:

- Attributable – Is the adjustment clearly attributable to the conflict? Would the item have been incurred absent the conflict? Is it expected to continue?
- Incremental – Is the amount incremental to normal operations?
- Actual – Is the adjustment based on actual amounts (vs. hypothetical costs or lost opportunities)? For example, we understand the SEC staff would generally not view it as appropriate to prepare a non-GAAP measure that adjusts for lost revenue because of closing an operation or facility.
- Quantifiable – Are the adjustments sufficiently defined to allow reasonable quantification?

Companies should also consider their controls and procedures surrounding the presentation of non-GAAP measures. These controls would typically include appropriate governance practices and policies to, among other things, prevent error or manipulation and address matters relating to

consistency in identifying the adjustments and how the adjustments are being described.

QUESTION 6.9 (Added May 5)

What guidance has the SEC staff issued on disclosures about Russia's invasion of Ukraine?

PwC response

On May 3, the staff of the Division of Corporation Finance issued an illustrative letter ([Sample Letter to Companies Regarding Disclosures Pertaining to Russia's Invasion of Ukraine and Related Supply Chain Issues](#)) which provides sample comments the Division may issue to companies directly or indirectly impacted by Russia's invasion of Ukraine and the international response thereto. While not an exhaustive list of disclosures a company should consider, the sample comments covered the following areas. Where relevant, we have included a reference to the question elsewhere in this *In depth* that addresses the specific topic.

- Direct and indirect impact of Russia's invasion on a company's business, such as government actions (including expropriation), reaction of investors, employees, and/or other stakeholders (see Question 6.4)
- The extent and nature of the board of directors' role in overseeing risks
- Cybersecurity (see Question 6.4)
- Disclosure of known trends or uncertainties, including impairment of tangible and intangible assets, contract modifications, and recoverability and collectability issues (see Question 6.5)
- Enhancements needed to critical accounting estimates disclosures (see Question 6.5)
- Disclosure of any material import or export bans (see Question 6.4)
- Supply change impacts, including by segments, products, lines of service, projects, or operations (see Question 6.5)
- Use of Non-GAAP measures (see Question 6.8)
- Disclosure controls and procedures and internal control over financial reporting (see Question 6.6)

A company that has a material direct or indirect impact from Russia's invasion of Ukraine should consider this guidance in developing disclosures to include in their SEC filings.

Subsequent events

QUESTION 6.10

How should a company consider whether events subsequent to the balance sheet date, but prior to issuance of the financial statements, should be reflected in the financial statements?

PwC response

Under ASC 855-10-25, information that becomes available after the end of the reporting period that provides additional evidence about conditions that existed as of the balance sheet date are recognized subsequent events. The financial statements may need to be adjusted to recognize the effects of that subsequent information. In contrast, subsequent events related to conditions that did not exist at the date of the balance sheet, but arose subsequent to that date, are not recognized in the financial statements, although disclosure may be necessary based on the nature of the event to keep the financial statements from being misleading.

While there has been long-standing geopolitical tension between Russia and Ukraine, there was an absence of a conclusive threat of invasion prior to February 24. As a result, the conflict is a non recognized subsequent event for periods that ended prior to that date. For financial statements that have yet to be released for periods ended prior to February 24, companies should consider the need for appropriate subsequent event disclosures.

While the conflict is a nonrecognized event, other events after the reporting date may provide additional information about uncertainties that existed at the reporting date. For example, the bankruptcy of a customer subsequent to the reporting date might reflect additional information about conditions that existed at the reporting date, independent of the subsequent escalation of the geopolitical tensions. Management should ensure that the measurement and presentation of assets and liabilities reflects only the conditions that existed at the reporting date.

The decision regarding when to disclose a nonrecognized subsequent event is based on specific facts and circumstances, including materiality, and requires judgment. Generally, a subsequent event should be disclosed if it meets both of the following criteria:

- The event should have a determinable (even if not yet definitively quantified) significant effect on the balance sheet at the time of occurrence or on the future operations of the company.
- Without disclosure of it, the financial statements would be misleading.

ASC 855 does not require a company to include all subsequent event disclosures in a single footnote. Rather, management may determine where to include the disclosures in the context of the financial statements.

This disclosure should be transparent and specific to the company, and should include the nature of the event and an estimate of its financial effect. Companies should consider disclosing the impact of developments related to the conflict that occurred after the reporting date on the carrying amount of assets and liabilities (for example, the need to impair assets or remeasure

fair values), restrictions on assets due to sanctions imposed, and the impact of the conflict on revenue or borrowing covenants.

When financial statements are reissued (e.g., in reports filed with the SEC or other regulatory agencies for transactions such as equity or debt offerings), events that require disclosure in the reissued financial statements in order to keep them from being misleading may be required to be made through amendments to the subsequent events disclosure within the originally issued financial statements. For example, if a company filed its Form 10-K on February 15 and reissues its financials on March 22 as part of a debt offering, subsequent event disclosures may need to be amended for material events occurring between the two issuances.

Resources

- PwC's *Financial statement presentation* guide, [Chapter 28](#)
- [ASC 855](#), *Subsequent Events*

QUESTION 6.11 (Added March 31)

What are some of the tax implications to consider when a company concludes that an event is unusual or infrequent?

PwC response

ASC 220-20-45-1 provides guidance for reporting events that are unusual and infrequent. If a company concludes that a material event is of an unusual nature and/or occurs infrequently, it should be reported as a separate component of income from continuing operations in the income statement or disclosed in the notes to the financial statements. This guidance also prohibits net-of-tax reporting (including per-share effects) of such items on the face of the income statement.

For these purposes, unusual nature is defined as possessing a high degree of abnormality and clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the company. Infrequent means that the event should not be reasonably expected to recur in the foreseeable future. Both of those characteristics are, therefore, highly dependent on the environment in which a company operates.

While the scope and severity of the economic impacts of the conflict between Russia and Ukraine may be significant to many entities, it is important to consider that many of those impacts are a function of inherent economic uncertainty that is present in all circumstances (e.g., demand risk, geopolitical influences on sources of supply). Nevertheless, it is likely that many companies will consider some of the effects of the conflict to, at a minimum, be infrequent even if not of an unusual nature. ASC 220-20 does not provide guidance on how to quantify the impact of a material event that is of an unusual nature and/or infrequent, and, thus, determining the incremental amount is a matter of significant judgment. We believe that a reasonable approach would be to identify those impacts that are direct and incremental related to the conflict (e.g., severance). Costs that would be incurred with or without the ongoing conflict would likely not be direct and incremental (e.g., overhead, payroll and benefits). For certain costs, judgment will be required to determine what is incremental.

ASC 740 provides that the AETR only applies to the tax effect of ordinary income. ASC 740-270 provides that the tax related to significant unusual or infrequently occurring items that will be separately reported should not be included in the AETR.

Companies will need to analyze the financial effects of the conflict and related events in order to determine if they represent unusual items to the company. They will then need to determine which losses and costs are attributable to the unusual event and consider whether there are related impacts to the calculation of the estimated AETR.

Resources

- PwC's *Income taxes guide*, [Chapter 16](#)
 - [ASC 220](#), *Comprehensive Income*
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