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iGAAP in Focus
Financial reporting
Closing Out 2022

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As 2022 comes to a close, entities are faced with significant uncertainty brought about by the current macroeconomic and geopolitical environment. As a result of significant global supply-chain disruptions, energy prices and labour shortages, many product and employment costs have increased. At the same time, global central banks are raising interest rates in an attempt to temper the impact of historically high inflation rates.

Entities need to bring greater transparency to how they are dealing with this challenging landscape and also respond to the growing investor demand for consistent, comparable, and timely sustainability and climate information.

In this special edition of *iGAAP in Focus,* we set out financial reporting issues that may be relevant for years ending on or after 31 December 2022 in view of the current economic and geopolitical environment and also highlight areas of regulatory focus and changes in accounting standards applicable to this year-end.

Uncertainty and financial reporting

In an interconnected world it is not always possible to isolate the wider economics effects of, for example, Russia's invasion of Ukraine from the increase in energy prices, increase in the general cost of living, the ongoing effects of the COVID-19 pandemic or myriad national or regional factors. However, similar economic phenomena are being experienced across a wide range of jurisdictions. Major effects of some of these on financial reporting are highlighted below.

A Deloitte *IFRS in Focus* details the financial reporting considerations related to the Russia-Ukraine war.

In addition, the European Securities and Markets Authority (ESMA) released a public statement on the implications of Russia's invasion of Ukraine on half-yearly financial reports. In its European common enforcement priorities for 2022 annual financial reports, ESMA considers that most of these messages are also relevant in the context of annual financial statements.

Increases in energy prices

The increase in energy prices and the possibility of energy shortages due to the depletion of gas reserves could have a significant effect on a wide range of entities and several aspects of financial reporting.

This could result in, amongst other things, disruption to production, higher costs (particularly in energy intensive industries), higher revenues for energy producers and lower revenues elsewhere (for example, in industries sensitive to levels of disposable income in a market where higher energy costs might limit consumers' spending power).

Such effects are clearly relevant to an impairment review conducted under IAS 36 *Impairment of Assets*, both in ensuring that forecasts are properly updated to reflect events and expectations as at the reporting date and in determining the appropriate disclosures to accompany that exercise. For example, a forecast of future energy prices might become a key assumption to be disclosed for the first time.

For some entities, as discussed in more detail below, the effect of energy prices might be severe and form a major part of disclosures explaining doubts over the entity's ability to continue as a going concern.

Less direct effects could include changes in the value of energy derivatives (for example, forward contracts to purchase or sell gas or electricity), with resultant impacts on hedge accounting or disclosures of market risks under IFRS 7 *Financial Instruments: Disclosures.*

General inflation and interest rate rises

Increases in energy prices have also contributed to the increase in general inflation levels. This has been accompanied by increases in interest rates reflecting lenders' perception of increased credit risk and interventions by central banks seeking to control inflation. Growing inflation and market interest rates affect multiple aspects of financial reporting which depend on forecasts of future cash flows and present value calculations.

In respect of impairment of non-financial assets, IAS 36 identifies an increase in market interest rates as an indicator to be assessed in determining whether an asset may be impaired and may lead to a full impairment review, unless the increase in market interest rate does not indicate the existence of a material impairment. This may be the case where an increase in market interest rates does not affect the appropriate discount rate for the asset in question (for example, if short-term interest fluctuations would not affect the rate of return demanded of a longer-life asset) or if the entity expects to recover higher interest charges through prices charged to its customers, or the increased rate is too small to raise concerns over the headroom of an asset's recoverable amount over its carrying amount. However, the possibility of an impairment loss should not be overlooked and a general increase in interest rates should lead to a proper consideration whether a full impairment review is required.

Inflation can have an impact on the measurement of longer-term provisions such as decommissioning obligations, as its effects on future outflows of economic resources should be reflected in either the forecast cash flows or the discount rate applied to longer-term liabilities. Entities should ensure that the inputs used in measuring provisions follow a consistent approach in incorporating the effects of inflation. Nominal cash flows, which include the effect of inflation, should be discounted at a nominal rate and real cash flows, which exclude the effect of inflation, should be discounted at a real rate.

Inflation and the resulting increase in the cost of living may lead to products becoming less affordable (either because of increased production costs or reduced customer spending power). Write-downs of inventory to net realisable value and recognition of onerous contract liabilities in respect of commitments to purchase inventory which cannot then be sold at a profit may be required. Inflation, specifically in salaries, can also be an important actuarial assumption factored in the measurement of defined benefit obligations accounted for under IAS 19 *Employee Benefits*. Where inflation is a major source of estimation uncertainty, an entity should consider the need to disclose the information required by paragraphs 125-133 of IAS 1 *Presentation of Financial Statements,* such as a sensitivity analysis.

Both interest rates and inflation can affect measurement of lease liabilities and right-of-use assets under IFRS 16 *Leases*. They can also lead to additional exposure to credit losses as borrowers' ability to repay their obligations is reduced, resulting in:

- Increases in expected credit losses to be recognised under IFRS 9 *Financial Instruments,* if it is expected that levels of default might increase due to increases in borrowers' cost of living. Changes in expected models used by financial institutions or 'management overlays' to supplement those models should be accompanied by disclosures to enable users of financial statements to understand the effect of credit risk on the amount, timing and uncertainty of future cash flows
- Expected credit losses becoming more significant to entities other than financial institutions if they expect increase in bad debts as customers struggle to pay outstanding amounts

Assumptions used for discount rates and cash flows should be internally consistent within a particular calculation and consistent across calculations performed for different purposes.

Government interventions

The current economic climate (particularly in respect of energy prices) has led to government interventions to, for example, limit prices that can be charged to customers or provide direct economic assistance to entities adversely affected by current economic conditions.

It will be important to correctly characterise these arrangements as a government grant in the scope of IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*, a tax credit in the scope of IAS 12 *Income Taxes*, a below-market loan subject to the requirements of IAS 20:10A or potentially (if, for example, a government acts to limit the rates a utilities supplier can charge) simply a lower cost than might otherwise be the case.

More broadly, government assistance may impact an entity's cash flow forecasts and assessments that utilise such forecasts (e.g. impairment reviews and going concern assessments). The assessment of an entity's best estimate of the impact of government assistance on cash flow forecasts, including the expected duration of a scheme, should be conducted carefully and, when significant to the outcome of the assessment, disclosed.

In many jurisdictions, governments have introduced (or announced plans to introduce) so called 'windfall taxes' targeted at entities operating in specific industries and that benefitted from higher profits as a result of rising prices, notably in the energy sector. Entities affected will need to assess the nature of the tax to determine if it should be accounted for as an income tax applying IAS 12 or as a levy applying IFRIC 21 *Levies*. This distinction is important as it will determine whether the related charge is presented in the income tax line in profit or loss or above that line. If IAS 12 applies, the entity will also need to consider whether to recognise a deferred tax asset or liability. Where the tax is announced but not yet effective, entities will need to consider whether they should disclose the expected impact of the tax on the entity's operations.

Restrictions on access to markets and cessation of operations

Following Russia's invasion of Ukraine, a number of entities announced their intention to exit the Russian market or experienced practical or political issues in continuing to access or manage operations in the region.

IAS 36 requires entities to assess whether there are any indications that an asset in the scope of IAS 36 may be impaired by considering internal and external sources of information. In making this assessment, entities should carefully consider whether the effects of Russia's invasion of Ukraine (direct and indirect) constitute an indication that one or more assets may be impaired. Decisions to abandon, dispose of or suspend operations, or cancel investments in Ukraine, Russia or Belarus could represent indicators of impairment necessitating a full impairment review of affected assets.

It is also possible that plans to dispose of operations give rise to classification of assets as held for sale or presentation as discontinued operations. Caution should be applied, however, as this is only appropriate when the strict criteria of IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* are met. In particular, a plan to abandon a non-current asset or disposal group does not result in its classification as held for sale and judgement may be required to assess whether a sale can be considered highly probable in an uncertain political environment.

At the point when an entity's relationship with a foreign operation changes (either through choice or otherwise), it will also be necessary to consider whether the level of influence has reduced such that control, joint control or significant influence have been lost.

Climate-related risks in financial statements

For some time, regulators have been urging entities to pay particular attention to climate-related matters and their effects when providing a balanced and comprehensive analysis of the development and performance of the entity's business and of its position together with a description of the principal risks and uncertainties that it faces (for example, climate-related matters are a repeated feature of the ESMA common enforcement priorities).

In particular, entities should consider whether the degree of emphasis placed on climate-related matters elsewhere in the annual report is consistent with how climate matters have been reflected in the judgements and estimates applied in the financial statements and whether the immediate actions necessary to meet a stated longer-term decarbonisation commitment are reflected in the financial statements. Forecasts used for financial reporting purposes should reflect the entity's strategic plans and planned actions at the reporting date and should be based on best estimates at the reporting date.

If climate-related matters are material, it is expected that they are considered in the preparation of IFRS financial statements, even if IFRS Accounting Standards do not explicitly refer to those matters. It cannot be assumed that investors or regulators will deem boilerplate disclosures stating that climate-related matters have been considered (for instance, in impairment tests) without further explanation as to how and to what extent it affects (or does not affect) financial statements as sufficient to provide information that is relevant to an understanding of the financial statements. For example, investors want to understand whether an entity's forecasts used for financial reporting are aligned with the goals of the Paris Agreement[1]. There are multiple possible scenarios and ranges of possible outcomes under different climate change trajectories. It is important for entities to be clear about the assumptions used and to make greater use of sensitivity analyses.

1. Discussed in more detail in A Closer Look – Investor demand for corporate reporting in line with the Paris Agreement on climate change

Where entities have concluded, in particular in highly exposed sectors, that no material financial impact from climate-related matters on their operations and/or in the measurement of their assets and liabilities is expected, regulators expect those entities to disclose the assessments performed, judgements made and the time horizon used to reach such a conclusion. Disclosures should be tailored to the specific circumstances of individual entities.

A Deloitte *A Closer Look* provides a background on investor expectations in respect of climate as well as what requirements are highlighted by the IFRS Foundation's publication 'In Brief: IFRS Standards and climate-related disclosures' and the IASB's educational material on the effects of climate-related matters on financial statements and how they might apply in practice.

Task Force on Climate-related Financial Disclosures (TCFD)

Pending finalisation of standards by the International Sustainability Standards Board (ISSB) and others (see discussion below), TCFD is used as a generally accepted framework for entities to explain their strategic response to climate change and its potential financial impacts. Many jurisdictions have incorporated TCFD disclosures into mandatory or recommended reporting requirements and regulators are increasingly focusing on the quality of that reporting.

For example, in 2022 the UK Financial Reporting Council (FRC) conducted a thematic review of TCFD disclosures and climate in the financial statements. The output of the review provides more clarity on expectations for entities who have taken a more traditional 'wait and see' approach to reporting and disclosure in these areas, as examples of best practice do exist. The FRC emphasised that climate reporting should now be firmly established as a board level topic.

The FRC thematic review noted key issues where entities can improve. These areas may provide useful consideration for entities that report on TCFD outside the UK or on sustainability information more broadly:

- **Granularity and specificity—**Entities should provide information about risks and opportunities across the entity, breaking this down by business, sector, and geography where appropriate
- **Balance—**Discussion of climate-related risks and opportunities should be proportionate to their expected size, including a discussion of any dependencies on the development of new technologies when explaining the potential of climate-related opportunities
- **Interlinkage with other narrative disclosures—**TCFD disclosures should be well integrated with other elements of narrative reporting, for example by incorporating the results of scenario analysis into the entity's description of overall strategy within the narrative report
- **Materiality—**Entities should provide an explanation of how they incorporate the TCFD all-sector guidance and supplemental guidance. Where disclosures are not given, a reason for the omission should be included. In particular, it should be clear whether the entity has considered these disclosures and determined them not to be material, or whether the matters covered by these disclosures have not been addressed in the entity's internal assessments
- **Connectivity between TCFD and financial statements disclosures—**Climate risks and opportunities identified within TCFD reporting should be properly integrated into the judgements and estimates which underpin the financial statements. Entities should also consider re-evaluating the presentation of their segmental reporting and disaggregated revenue disclosures in response to climate change and transition plans
- **Governance—**Entities should provide specific information on the oversight of climate-related matters, such as consideration of climate-related performance objectives and the effect of climate on decisions about major capital expenditure, acquisitions, and disposals. Entities should also consider disclosing how climate-related risks are controlled and how climate-related metrics affect remuneration policies
- **Strategy—**Information on strategy should be granular and the level of detail included in scenario analyses should be consistent, including quantitative measures. Entities' discussions of risks and opportunities should not be disproportionately weighted towards opportunities
- **Risk management—**Climate-related matters should be integrated into overall risk management processes. Particularly, processes for assessing the priority and materiality of climate-related risks should be well explained
- **Metrics and targets—**Metrics should not only focus on Scope 1 and 2 emissions but also include other climate-related risk and opportunity metrics. Historical data and explanation for movements should be provided to support the reader's understanding of progress against targets
- **Assurance—**Entities should clearly explain the level of any assurance given and what it covered. Terms such as 'verified' should be avoided as it may imply a higher level of assurance than has actually been obtained

In view of the pervasive nature and significance of climate-related risks and growing stakeholder expectations and regulatory focus, entities should consider the points above irrespective of whether they are providing voluntary or mandatory TCFD disclosures.

Sustainability and climate corporate reporting developments

Investors' and other stakeholders' demand for sustainability information relevant to understanding of how businesses create, sustain or erode value over time has led to a rapid move towards introduction of mandatory sustainability reporting.

International Sustainability Standards Board (ISSB)

The ISSB is emerging as the global standard-setter for standards on sustainability reporting for capital markets. In March 2022, the ISSB published two Exposure Drafts (EDs) for its first IFRS Sustainability Disclosure Standards:

- [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information
- [Draft] IFRS S2 Climate-related Disclosures

The ISSB is currently redeliberating the proposals in the EDs in view of the responses received to its consultation and publication of the final standards is expected early in 2023. A recent Financial Stability Board report indicated that 14 out of 24 jurisdictions that are its members reported that they are putting in place structures and processes to bring the ISSB standards into local requirements.

IOSCO has set out its expectations that both disclosures and assurance standards should be ready for use by corporates for their end-2024 accounts. At COP 27 in November 2022, IOSCO Board Chair Jean-Paul Servais said, "In 2023, the ISSB will issue its standard for climate disclosures and general requirements. IOSCO will move promptly to decide on endorsement and will develop a support program for its members to assist them in moving forward immediately should IOSCO decide to endorse these standards. IOSCO also supports the efforts of the ISSB in seeking to be inclusive through its capacity building partnership initiative."

A Deloitte *iGAAP in Focus* gives background information on the ISSB and summarises its first two EDs.

Jurisdictional developments with significant extraterritorial reach

In November 2022, the **European Union**'s Corporate Sustainability Reporting Directive (CSRD) was adopted by the European Parliament and approved by the Council of the European Union. The CSRD aims to improve sustainability reporting in an entity's management report for investors, civil society and other stakeholders, thereby contributing to the transition to a fully sustainable and inclusive economic and financial system in line with the European Green Deal and the UN Sustainable Development Goals (SDGs).

The scope of the CSRD is very wide and extends to many non-EU undertakings not listed on an EU regulated market.

Entities will have to report on a wide range of sustainability matters using European Sustainability Reporting Standards (ESRS) developed by EFRAG.

The first set of draft ESRS was submitted to the European Commission (EC) in November 2022 and the EC will now consult EU bodies and Member States on the draft standards, before adopting the final standards as delegated acts in June 2023 (expected), followed by a scrutiny period by the European Parliament and Council.

A Deloitte iGAAP in Focus explains the worldwide reach of the CSRD.

In the **US,** the SEC consulted on climate-related disclosures in March 2021 and issued the proposed rule *The Enhancement and Standardization of Climate-related Disclosures for Investors* in March 2022. Among other things, the proposed rule would apply to foreign private issuers, and the SEC requested input as to whether foreign private issuers should be permitted to report under substantially similar requirements to those in the proposed rule.

Integrated reporting

In 2021, the International Integrated Reporting Council (IIRC) published revisions to the International Integrated Reporting Framework (<IR> Framework), originally released in 2013. The revisions place more emphasis on value creation, preservation and erosion; provide for more disclosure from those charged with governance to promote further the integrity of reporting; and expand the coverage of outcomes. The revised <IR> Framework is maintained under the auspices of the IFRS Foundation and is applicable for reporting periods commencing 1 January 2022. Where an entity chooses to adopt the <IR> Framework only in part, the Framework now encourages it to identify which requirements have not been applied and the reasons why.

Currency and hyperinflation

The steep rise in global energy prices has contributed to higher levels of general inflation in many jurisdictions, increasing the number of jurisdictions that are subject to hyperinflation (as that term is defined in IAS 29 *Financial Reporting in Hyperinflationary Economies*). Entities are therefore increasingly facing the following challenges:

- Determining whether an economy is hyperinflationary as defined in IAS 29 can sometimes prove difficult. The definition includes several characteristics of hyperinflation, although hyperinflation is most often evidenced when the cumulative inflation rate over three years approaches or exceeds 100%. It can also be challenging to decide which general price index should be applied to amounts in the financial statements
- Entities may face difficulties in determining an entity's functional currency in circumstances where both a local and international currency are in common use. This can be particularly significant where the local currency is hyperinflationary. IAS 29 is only applied by entities whose functional currency is the currency of a hyperinflationary economy (rather than by any entity operating in that economy). It should also be noted that IAS 21 The Effects of Changes in Foreign Exchange Rates specifically states that "[a]n entity cannot avoid restatement in accordance with IAS 29 by, for example, adopting as its functional currency a currency other than the functional currency determined in accordance with this Standard (such as the functional currency of its parent)"
- When exchanges between a local currency and globally traded currencies are restricted, it may be difficult to identify a suitable exchange rate for translating monetary items in individual financial statements and translating the financial statements of a foreign operation in its parent's presentation currency. Although this issue is not specific to hyperinflationary economies, a shortage of 'hard' currency and therefore a need for exchange restrictions is often a feature of economies whose local currency is losing value

When inflation or exchange issues result in a significant judgement or give rise to a source of estimation uncertainty, disclosure should be provided as required by IAS 1:122 and 125.

Based on data available at the time of writing, including inflation forecasts from the International Monetary Fund (IMF) and the indicators laid out in IAS 29, the following economies should be considered hyperinflationary economies for the purposes of applying IAS 29 and for retranslation of foreign operations in accordance with IAS 21 in financial statements for the year ending 31 December 2022:

- Argentina
- Ethiopia
- Iran
- Lebanon
- South Sudan
- Sudan
- Suriname
- Syria
- Türkiye
- Venezuela
- Yemen
- Zimbabwe

Ethiopia and Türkiye (formerly known as Turkey) have become hyperinflationary during 2022.

Other reporting considerations

Events after the reporting date

The emergence of new issues or new developments after the period-end may require careful consideration to distinguish between adjusting events providing evidence of conditions that existed at the end of the reporting period and non-adjusting events indicative of conditions that arose after the reporting period.

As well as determining in which reporting period the event itself should be accounted for, this distinction is also important to forward-looking calculations and related disclosures. For example, an impairment review under IAS 36 or expected credit loss calculation under IFRS 9 and disclosure of sensitivities to reasonably possible changes in forecasts should be based on conditions at the reporting date and are not affected by subsequent, non-adjusting events. It may be helpful to provide additional disclosure of how assessments have changed since the reporting date, but this should be clearly identified as being distinct from the information as at the reporting date.

Disclosure of significant judgements and key sources of estimation uncertainty

When reporting in uncertain times, it is particularly important to provide users of the financial statements with sufficient information to enable them to understand the key assumptions and judgements made when preparing financial information. Depending on an entity's specific circumstances, many of the areas discussed in this publication may give rise to a significant judgement over the characterisation of an item or transaction or a source of estimation uncertainty over its measurement, for which disclosures may be required by IAS 1:122-133.

The disclosure provided about the key assumptions, including the sensitivity analysis based on a range of reasonably possible outcomes, should reflect the conditions at the reporting date. When key assumptions, or the range of reasonably possible changes to those assumptions, are affected significantly as a result of non-adjusting events after the reporting date, information about those changes, including an estimate of the financial effect, should be provided separately.

In respect of estimation uncertainty, it is also important to distinguish between estimates which have a significant risk of material adjustment to the carrying amount of assets and liabilities in the next financial year (and hence require disclosure under IAS 1:125) and those which might affect asset and liabilities over a longer timescale (and hence are not within the scope of that paragraph but might usefully be disclosed separately).

In making high quality disclosure of estimation uncertainty, it is also important to:

- Quantify the specific amount at risk of material adjustment
- Provide sufficient granularity in the descriptions of assumptions and/or uncertainties to enable users to understand management's most difficult, subjective or complex judgements
- Clearly distinguish the disclosure of other estimates, and associated sensitivities, from significant estimates and explain their relevance
- Provide meaningful sensitivities and/or ranges of reasonably possible outcomes for significant estimates (which, due to the economic factors discussed above, might be wider than in previous years); these should not be limited to those required by specific IFRS Accounting Standards
- Quantify the assumptions underlying significant estimates when investors need this information to fully understand their effect
- Explain any changes to past assumptions if the uncertainty remains unresolved

A Deloitte *IFRS in Focus* provides more detail on the disclosure of significant judgements and sources of estimation uncertainty.

Non-GAAP and alternative performance measures

Significant economic changes or unusual events often lead to a desire to highlight their effects on performance or what an entity's profit may have been had an event not occurred. However, care must be taken in following such an approach.

The pervasive nature of the impact of such changes or events means that a separate presentation may not faithfully represent an entity's overall financial performance and may be misleading to users' understanding of the financial statements. For example, an 'excluding impact of the increase in energy prices' profit figure would reflect an economic environment that did not exist in 2022.

In general, when evaluating whether the effect of an economic or geopolitical event can appropriately be reflected via a non-GAAP measure or alternative performance measure (APM), factors including, but not limited to, the following should be considered:

- Can the item to be excluded from an adjusted measure be demonstrated to directly relate to the event or economic condition?
- Is the item incremental to normal operations rather than a reflection of 'the new normal'?
- Is the item objectively quantifiable, as opposed to an estimate or projection?
- Is the item discrete, rather than part of the measurement of a larger item?

Instead of seeking to present the wide-ranging impacts of such an event separately in profit or loss, it is more likely to be appropriate to disclose, in the notes, qualitative and quantitative information on the significant impacts, the judgements and assumptions applied in the recognition, measurement and presentation of assets, liabilities and impacts on the numbers in profit or loss.

Such impacts should be provided in a clear and unbiased way. When including non-GAAP measures or APMs in management reports, entities should also consult the IOSCO Statement on Non-GAAP Financial Measures and ESMA Guidelines on Alternative Performance Measures (updated in 2020) that remain relevant.

Income tax and recognition of deferred tax assets

Entities should consider how lower or more volatile profit levels stemming from the current macroeconomic environment might influence income tax accounting. For example, a reduction in current-period income or the incurrence of losses, coupled with a reduction in forecast income, could result in a reassessment of whether it is probable that some or all of an entity's deferred tax assets can be recovered. If declining earnings or impairments generate losses, entities will need to consider whether there is sufficient income within the carry-back and carry-forward periods available under tax law to fully or partially realise the related deferred tax asset.

Applying IAS 12, an entity may not have recognised deferred tax liabilities for taxable temporary differences associated with subsidiaries, branches and associates, and interests in joint arrangements, because it concluded that it controlled the timing of the reversal of the temporary difference and it had been deemed probable that the temporary difference would not reverse in the foreseeable future. Conversely, an entity may have recognised deferred tax assets for deductible temporary differences associated with such investments because it determined it probable that the temporary difference would reverse in the foreseeable future (and it was determined to be probable that the deferred tax asset could be recovered). If an entity or its subsidiaries have liquidity issues or other challenges resulting from the current macroeconomic environment such that there is a change in intent with respect to the repatriation of undistributed earnings in an investee, it may be appropriate to reconsider these conclusions.

Disclosure is also important in this area, in particular of entity-specific information about the nature of the evidence supporting the recognition of deferred tax assets when there is a recent history of losses, and deferred tax judgements and estimates, including relevant sensitivities and/or the range of possible outcomes in the next 12 months.

OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS)

In March 2022, the OECD released technical guidance on its 15% global minimum tax agreed as the second 'pillar' of a project to address the tax challenges arising from digitalisation of the economy. This guidance elaborates on the application and operation of the Global Anti-Base Erosion (GloBE) Rules agreed and released in December 2021 which lay out a co-ordinated system to ensure that Multinational Enterprises (MNEs) with revenues above €750 million pay tax of at least 15% on the income arising in each of the jurisdictions in which they operate.

Over 135 countries and jurisdictions have agreed to incorporate the 'Pillar Two' into tax law. It is not anticipated that substantive enactment in any of these countries and jurisdictions will occur before the end of 2022 (meaning that tax balances calculated under IAS 12 as at 31 December 2022 will not be affected), but it should be noted that IAS 10 *Events after the Reporting Period* gives as an example of non-adjusting events that generally require disclosure "changes in tax rates or tax laws enacted or announced after the reporting period that have a significant effect on current and deferred tax assets and liabilities."

Accordingly, entities should assess whether the OECD technical guidance together with the level of commitment of the applicable governments to its implementation constitute the announcement of a change in tax laws in the jurisdictions in which they operate. If this is the case and if the entity concludes that the rules may have a significant effect on its operations, it would disclose that fact in its financial statements along with an estimate of the impact or a statement that such an estimate cannot be made.

Relevant to this disclosure might be the considerations of the IASB on how to deal with the challenges of applying IAS 12 (particularly in respect of deferred tax) to a Pillar Two framework. At its November 2022 meeting, the IASB tentatively decided to introduce a temporary exception from accounting for deferred taxes arising from the implementation of Pillar Two, together with targeted disclosures requirements for affected entities.

Publication of an exposure draft of these proposals is expected in January 2023, with finalisation of any amendments targeted for the second quarter of 2023.

Going concern

It is possible that economic pressures or changes might render a business model unviable or access to necessary debt financing might be limited. In such circumstances, it is necessary to assess whether the entity might be unable to continue as a going concern for a period of at least, but not limited to, 12 months from the reporting date.

Financial statements are prepared on a going concern basis unless management intends either to liquidate the entity or to cease trading or has no realistic alternative but to do so. When making its assessment, if management is aware of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity must disclose those uncertainties or significant judgements taken in reaching a conclusion that no material uncertainty exists.

The IASB published educational material on the assessment of going concern and related disclosure requirements in 2021. This guidance is summarised in a Deloitte *IFRS in Focus.*

Application of IFRS 17 *Insurance Contracts*

IFRS 17 is effective for annual reporting periods beginning on or 1 January 2023. Given limited early adoption, both insurers and non-insurers need to consider the disclosure requirements under IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* of the impact of new IFRSs issued but not effective. The impact of IFRS 17 for insurers will be significant as may the impact of IFRS 9 for those insurers that chose to defer the application of IFRS 9 as they will also be applying IFRS 9 for the first time. As December 2022 annual reports will be published after the date of initial application of IFRS 17, the analysis of the impact of implementation of the new Standard will be more advanced than was the case a year ago, allowing further elaboration and development of information provided in previous financial statements. As such, the provision of entity specific, quantitative disclosures on the likely changes in accounting is expected to be an area of increased regulatory focus. The level of disclosure, and particularly the extent to which quantification is possible, will be affected by the status of each entity's implementation project, but when practicable should include:

- Accounting policies to be applied, including the use of scope exceptions and transition reliefs
- The methodology to be applied to key aspects of accounting for insurance contracts such as discounting, adjustment for non-financial risks, allocation of premia and recognition of the contractual service margin (CSM) as revenue
- If known or reasonably estimable, the quantum of IFRS 17's effect on financial position, financial performance and equity at the start of the start and end of 2022
- The expected effect on accounting for financial assets, for entities that will be applying IFRS 9 for the first time, as well as changes in classification elections for financial assets where IFRS 9 is currently applied.

If quantitative information is not disclosed because it is unknown or not reasonably estimable, the importance of qualitative information enabling users to understand the nature and likely magnitude of the expected impact on the financial position is heightened.

IFRS 3 *Business Combinations*

Business combinations can be highly significant, in some cases fundamentally changing the nature or scope of an entity's operations. As such, entities should give clear and consistent explanations of the reasons for, and the impact of, a business combination throughout the annual report, with careful thought given as to how to convey the information in an understandable and concise way. Similarly:

- An explanation of factors giving rise to goodwill should be provided and, if possible, should include considerations specific to the business combination in question, rather than only providing boilerplate disclosures
- Disclosures related to contingent consideration should include entity-specific explanations of the arrangements and the potential variability in the amounts payable

The mechanics of business combination accounting can also be complex, with significant judgement sometimes needing to be applied in determining, for example, whether elements of a deal form part of the business combination for accounting purposes or should instead be accounted for as separate transactions (for example, the requirements to determine whether share-based payments form part of consideration or are accounted for as a post-combination expense are complex). Care should be taken in performing this exercise and clear disclosure provided of the judgements made in either applying IFRS 3 or (in cases where it is not clear whether a transaction meets the definition of a business combination or should be accounted for as an asset purchase) determining whether IFRS 3 is applicable at all.

IAS 33 *Earnings per share*

Basic and diluted EPS are often seen as important metrics of an entity's performance and, as such, are often included in the first announcement of results for a period as well as in the full financial statements. However, the calculation of those figures can be highly complex and might not always be well understood by users. Although the disclosure requirements of IAS 33 itself are relatively limited in this respect, it should be noted that the general requirements of IAS 1 to disclose significant judgements made in preparing the financial statements can also apply to the calculation of EPS (for example, if judgement is needed in determining the substance of a share reorganisation).

The following are also noted as details of EPS calculations that can easily be misapplied:

- The determination of whether potential ordinary shares are dilutive or antidilutive must be based on profit or loss from continuing operations
- Share reorganisations that involve a bonus element require retrospective adjustment in the weighted average number of ordinary shares used for the calculation of basic and adjusted EPS for all periods presented
- When preference shares are classified as equity, earnings used for the calculation of basic and adjusted EPS are adjusted for all the effects of those preference shares, including dividends and any premiums arising on redemption

The guidance on the use of non-GAAP measures discussed above is also applicable to the presentation of adjusted EPS figures. In particular, these should not be given more prominence that 'statutory' EPS measures and the methodology applied in their calculation, including the basis used for tax on adjusting items, should be clearly disclosed.

Significant agenda decisions from the IFRS Interpretations Committee

As detailed in the appendix to this publication, the IFRS Interpretations Committee (the Committee) has published a number of agenda decisions providing guidance on the appropriate accounting for specific transactions. Some of the matters addressed that might apply more widely are discussed below.

Demand Deposits with Restrictions on Use arising from a Contract with a Third Party (IAS 7 *Statement of Cash Flows*)

In April 2022, the Committee published an agenda decision about whether a demand deposit that is subject to contractual restrictions on use agreed with a third party meets the definition of 'cash' in IAS 7. In the fact pattern discussed, the entity had to keep a specified amount of cash in a separate demand deposit and could use the cash only for specified purposes.

The Committee concluded that restrictions on the use of a demand deposit arising from a contract with a third party do not result in the deposit no longer being cash unless those restrictions change the nature of the deposit in a way that it would no longer meet the definition of cash in IAS 7. In the fact pattern discussed, the contractual restrictions do not change the nature of the deposit—the entity can access those amounts on demand. Therefore, the Committee concluded that the entity includes the demand deposit as a component of 'cash and cash equivalents' in its statement of cash flows and in its statement of financial position.

When relevant to an understanding of its financial position, the entity would disaggregate the 'cash and cash equivalents' line item and present the demand deposit separately in an additional item. The demand deposit should be classified as current unless it is "restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period". The entity would also consider whether to disclose additional information in the context of the requirements in IFRS 7 about liquidity risk. Further disclosure may be appropriate if the information an entity provides in applying the disclosure requirements in IAS 7 and IFRS 7 is insufficient to enable users of financial statements to understand the impact of the restrictions on the entity's financial position.

Negative Low Emission Vehicle Credits (IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*)

In July 2022, the Committee published an agenda decision that discusses whether particular measures to encourage reductions in vehicle carbon emissions give rise to obligations that meet the definition of a liability in IAS 37. In the fact pattern discussed, entities receive positive credits if, in a calendar year, they have produced or imported vehicles whose average fuel emissions are lower than a government target. Entities receive negative credits if, in that year, they have produced or imported vehicles whose average fuel emissions are higher than the target.

In the fact pattern considered, an entity can settle an obligation to eliminate negative credits either by purchasing credits from another entity or by generating positive credits itself in the next year. The Committee concluded that either method of settling the obligation would result in an outflow of resources embodying economic benefits. These resources are the positive credits the entity would surrender to eliminate the negative balance. The entity could otherwise have used self-generated positive credits for other purposes (for example, to sell to other entities with negative credits).

The Committee concluded that in the fact pattern the activity that gives rise to a present obligation is the production or import of vehicles whose fuel emissions, averaged for all the vehicles produced or imported in that calendar year, are higher than the government target.

The Committee concluded that the measures described in the fact pattern could give rise to a legal obligation that arises from measures as a result from an operation of law. The sanctions the government can impose under the measures would be the mechanism by which settlement may be enforceable by law.

An entity would have a legal obligation that is enforceable by law if accepting the possible sanctions for non-settlement is not a realistic alternative for that entity. The Committee observed that determining whether accepting sanctions is a realistic alternative for an entity requires judgement—the conclusion will depend on the nature of the sanctions and the entity's specific circumstances.

The Committee concluded that, if an entity determines that it has no legal obligation to eliminate its negative credits, it would then need to consider whether it has a constructive obligation to do so. It would have a constructive obligation if it has both:

- In a calendar year, produced or imported vehicles with average fuel emissions higher than the government target
- Taken an action that creates valid expectations in other parties that it will eliminate the resulting negative credits—for example, made a sufficiently specific current statement that it will do so

Appendices

New and revised IFRS Standards and Interpretations mandatorily effective for years ending 31 December 2022

Amendments to IFRS 3—References to the Conceptual Framework

The amendments to IFRS 3 replace references to the 1989 *Framework* with references to the 2018 *Conceptual Framework.* They also add explicit requirements that:

- For obligations within the scope of IAS 37, an acquirer applies IAS 37 to determine whether at the acquisition date a present obligation exists as a result of past events
- For a levy that would be within the scope of IFRIC 21, the acquirer applies IFRIC 21 to determine whether the obligating event that gives rise to a liability to pay the levy has occurred by the acquisition date
- An acquirer does not recognise contingent assets acquired in a business combination

A Deloitte *IFRS in Focus* provides more details on the Amendments to IFRS 3—*References to the Conceptual Framework.*

Amendments to IAS 16 Property, Plant and Equipment—Proceeds before Intended Use

The amendments to IAS 16 require the recognition of proceeds from sales of items produced before an item of property, plant and equipment is available for use (for example, samples produced when testing whether the asset is functioning as intended) to be recognised in profit or loss together with the costs of that item, replacing a previous requirement for the net proceeds of such sales to be deducted from the cost of property, plant and equipment.

The costs of testing whether the asset is functioning properly continue to form part of the cost of property, plant and equipment.

A Deloitte *IFRS in Focus* provides more details on the Amendments to IAS 16 *Property, Plant and Equipment—Proceeds before Intended Use.*

Amendments to IAS 37—Onerous Contracts—Cost of Fulfilling a Contract

The amendments to IAS 37 specify that, in determining whether a contract is onerous, the costs that relate directly to that contract should be considered. The amendments also specify that these costs consist of both the incremental costs of fulfilling a contract (for example, direct labour and materials) and an allocation of other direct costs (giving the example of the depreciation charge for an item of property, plant and equipment used in fulfilling that contract among others).

A Deloitte *IFRS in Focus* provides more details on the Amendments to IAS 37—*Onerous Contracts—Cost of Fulfilling a Contract*.

Annual Improvements to IFRS Standards 2018-2020—Amendments to IFRS 1, IFRS 9, IFRS 16 and IAS 41

The annual improvements make narrow scope amendments to four IFRS Standards:

- *IFRS 1—Subsidiary as a First-time Adopter*—Permitting a subsidiary adopting IFRS Standards later than its parent which uses the existing provision in IFRS 1 *First-time Adoption of International Financial Reporting Standards* to measure its assets or liabilities at the carrying amounts that would be included in its parent's consolidated financial statements to measure cumulative translation differences on its foreign operations on the same basis. As with the existing relief, a similar election is available to associates and joint ventures
- *IFRS 9—Fees in the '10 per cent test' for Derecognition of a Financial Liability*—Specifying that only fees paid or received between the entity (the borrower) and the lender, including fees paid or received by either the entity or the lender on the other's behalf, should be included in a quantitative assessment of whether the revised terms of a financial liability are substantially different from the terms that existed before the instrument was amended
- *IFRS 16—Lease Incentives*—Removing the illustration of reimbursement of leasehold improvements from Illustrative Example 13
- *IAS 41—Taxation in Fair Value Measurements*—Aligning the fair value measurements of IAS 41 *Agriculture* with those of IFRS 13 *Fair Value Measurement* by removing a requirement to exclude tax cash flows from that measurement

A Deloitte *IFRS in Focus* provides more details on *Annual Improvements to IFRS Standards 2018-2020—Amendments to IFRS 1, IFRS 9, IFRS 16 and IAS 41.*

IFRS Interpretations Committee agenda decisions in 2022

Along with its activity developing formal interpretations of IFRS Accounting Standards and proposing that the IASB make amendments to these standards, the Committee regularly publishes summaries of issues that it has decided not to add to its agenda, generally accompanied by a discussion of the accounting issue submitted.

In August 2020, The Trustees of the IFRS Foundation issued an updated IFRS Foundation Due Process Handbook establishing that the explanatory material in the agenda decisions published by the IFRS Interpretations Committee derives its authority from the IFRS Standards themselves and, therefore, that its application is required with the generally requirements of IAS 8 for retrospective application applying when an agenda decision results in a change of accounting policy.

The IFRS Foundation Due Process Handbook and each *IFRIC Update* also note that it is expected that an entity would be entitled to sufficient time to make that determination and implement any necessary accounting policy change (for example, to obtain new information or adapt its systems). Determining how much time is sufficient to make an accounting policy change is a matter of judgement that depends on an entity's particular facts and circumstances. Nonetheless, an entity would be expected to implement any change on a timely basis and, if material, consider whether disclosure related to the change is required by IFRS Standards.

The following agenda decisions have recently been published by the Committee:

November 2021 *IFRIC Update*	IFRS 16—Economic Benefits from Use of a Windfarm
February 2022 *IFRIC Update*	IFRS 9 and IAS 20—TLTRO III Transactions
March 2022 *IFRIC Update*	IAS 7—Demand Deposits with Restrictions on Use arising from a Contract with a Third Party
April 2022 *IFRIC Update*	IFRS 15—Principal versus Agent: Software Reseller
June 2022 *IFRIC Update*	IFRS 17—Transfer of Insurance Coverage under a Group of Annuity Contracts
	IAS 32 *Financial Instruments: Presentation*—Special Purpose Acquisition Companies (SPAC): Classification of Public Shares as Financial Liabilities or Equity
	IAS 37—Negative Low Emission Vehicle Credits
September 2022 *IFRIC Update*	IFRS 9 and IFRS 16—Lessor Forgiveness of Lease Payments
	IFRS 17 and IAS 21—Multi-currency Groups of Insurance Contracts
	Special Purpose Acquisition Companies (SPAC): Accounting for Warrants at Acquisition

New and revised standards available for early application in years ending 31 December 2022

Paragraph 30 of IAS 8 requires entities to consider and disclose the potential impact of new and revised IFRS Standards that have been issued but are not yet effective. As discussed above, the sufficiency of these disclosures is a current area of regulatory focus.

The list below reflects a cut-off date of 30 November 2022. The potential impact of the application of any new and revised IFRS Standards issued by the IASB after that date, but before the financial statements are issued, should also be considered and disclosed.

For each, a link is provided to a Deloitte publication presenting an overview of the new or amended IFRS Standard.

IFRS	Effective date—periods commencing on or after:
New standards	
IFRS 17 *Insurance Contracts* including Amendments to IFRS 17 and Initial Application of IFRS 9 and IFRS 17—Comparative Information	1 January 2023
Amended Standards	
Amendments to IFRS 10 and IAS 28—*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*	The IASB decided in December 2015 to defer indefinitely the effective date of these amendments. Early application is permitted.
Amendments to IAS 12—*Deferred Tax related to Assets and Liabilities arising from a Single Transaction*	1 January 2023
Amendments to IAS 1 and IFRS Practice Statement 2 *Making Materiality Judgements*—*Disclosure of Accounting Policies*	1 January 2023
Amendments to IAS 8—*Definition of Accounting Estimates*	1 January 2024
Amendments to IAS 1—*Classification of Liabilities as Current or Non-current*	1 January 2024
Amendments to IAS 1—*Non-current Liabilities with Covenants*	1 January 2024
Amendments to IFRS 16—*Lease Liability in a Sale and Leaseback*	1 January 2024

The Deloitte Accounting Research Tool (DART) is a comprehensive online library of accounting and financial disclosures literature. iGAAP on DART allows access to the full IFRS Standards, linking to and from:

- Deloitte's authoritative, up-to-date, iGAAP manuals which provide guidance for reporting under IFRS Standards
- Model financial statements for entities reporting under IFRS Standards

In addition, our *Beyond the numbers* volume of iGAAP provides guidance on disclosure requirements and recommendations which businesses must consider in light of the broader environmental, social and governance matters which can significantly drive the value of an entity.

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