IFRS news
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Accounting implications of the UK's Brexit decision for December 2018 period ends

The UK is due to leave the European Union on 29 March 2019. As the UK continues to negotiate its exit, UK businesses should be considering how this new political landscape will impact their organisations. Irrespective of the outcome of the negotiations, whether that be with or without a deal, there will likely be significant changes for many UK businesses. But this is not just a concern for UK businesses, Brexit might also impact overseas entities doing business with the UK, as well as groups with substantial UK operations.

For some businesses, the shape of the UK's future relationship with the EU remains too uncertain to take action.

However, in our view, by now management should have identified and assessed the Brexit-related risks that apply to their business and should be considering the impact on accounting and reporting. In particular, we believe this would include:

Disclosures - Detailed and entity specific disclosure of the Brexit-related risks should be made in the accounts to explain the judgements taken, assumptions made and the impact on the entity's operations.

The FRC has made it clear that it expects entities to disclose information about the specific and direct challenges to their business model and operations, as distinct from information about broader economic uncertainties. Where there are particular threats, for example the possible effect of changes in import/export taxes or delays to their supply chain, the FRC expects entities to identify these clearly and for management to describe any actions they are taking, or have taken, to manage the potential impact. The broad uncertainties that may still attach to Brexit when companies report will require disclosure of sufficient information to help users understand the degree of sensitivity of assets and liabilities to changes in management's assumptions.

Subsequent events - Careful analysis is required to identify whether the impact of events that occur between the year end and the date of signing the financial statements would require either an adjustment to the amounts recognised at period end or disclosure only, or whether the ability of the entity to continue as a going concern is called into question.

Impairments and valuations - Valuations, measurements and recoverable amount calculations that use market inputs should reflect market data at the balance sheet date. If valuation techniques and estimates are applied, cash flow models for impairment testing will likely require a wider range of outcomes than usual to reflect a broad spectrum of possible Brexit scenarios.

Restructuring - Some entities have already or are considering reorganising their business in preparation for a potential Brexit. It is unlikely that contemplated restructuring will have an immediate impact on the financial statements at, say, 31 December 2018. However, plans over time could result in an impairment/disposals of assets, recognition of provisions or changes to segments and disclosure.

In addition, the accounting for group restructurings in separate accounts can be complex, in particular, for the individual entity receiving a business in a common control transaction.

Directors duties and dividends - Directors need to consider, apart from statutory duties, their fiduciary duties to safeguard the company's assets and ensure that the company is able to pay its debts as they fall due. This would be relevant when deciding on dividend payments during 2019 as Brexit might affect the company's financial position.

Tax - The withdrawal agreement and any new trade agreement, when finalised, could result in significant changes to the tax law that applies to UK and EU companies.

Some of the main areas that could be impacted by Brexit include tax on rolled-over gains from certain previous reorganisations, withholding taxes on certain dividends and measurement of deferred tax assets.

Interim reporting - Entities need to consider the extent to which additional disclosures are necessary in any interim report, to explain changes since the last annual report.

See our detailed In depth for further information.

We will continue to update our financial reporting guidance as the full impact of Brexit develops.

Hyper-inflationary economies at 31 December 2018 - PwC In brief

Issue

IAS 29, 'Financial reporting in hyper-inflationary economies' requires entities to apply the standard from the beginning of the period in which the existence of hyper-inflation is identified. This document presents the countries that are hyper-inflationary at 31 December 2018, and those that are not expected to be hyper-inflationary at that date but that should be kept under review in 2019. The quantitative data referred to in this document is based on International Monetary Fund data (World Economic Outlook database– October 2018).

Impact

IAS 29 should be applied in 2018 to entities with a functional currency of the countries listed below:

- Angola;
- Argentina;
- South Sudan;
- Sudan;
- Syrian Arab Republic; and
- Venezuela.

The following economies are not hyper-inflationary in 2018, but should be kept under review in 2019:

- Democratic Republic of the Congo;
- Iran;
- Libya; and
- Suriname.

Other potentially hyper-inflationary economies:

- Yemen.

Insight

Hyper-inflationary economies

Angola

Angola was classified as a hyper-inflationary economy at the end of 2017. IMF data shows that the three-year cumulative inflation rate is expected to remain above 100% in 2018.

Local inflation data is consistent with the IMF projections for 2018. The qualitative indicators are mixed, but they also suggest that Angola is hyper-inflationary. Entities with the currency of Angola as their functional currency should continue to apply IAS 29 in 2018.

Argentina

Inflation in Argentina has been high for several years, and local inflation data has not been reported consistently. Inflation increased significantly in 2018. The three-year cumulative inflation rate, using different combinations of retail price indices, exceeded 100% during the first half of 2018. Local forecasts also suggest that three-year cumulative retail price inflation at the end of 2018 will be above 100%. Three-year cumulative inflation using the wholesale price index has also exceeded 100%, and it is unlikely to fall significantly below 100% in 2019.

The qualitative indicators are still mixed; however, taking into account the developments in the country, including the devaluation of the currency, they do not contradict the conclusion that Argentina is now a hyper-inflationary economy for accounting purposes.

Argentina should be considered a hyper-inflationary economy for accounting periods ending after 1 July 2018. Therefore, IAS 29 should be applied by all entities with a functional currency of the Argentine peso from that date, and it should be applied as if the economy had always been hyper-inflationary.

IAS 29 requires financial statements of an entity whose functional currency is the currency of a hyper-inflationary country to be restated into the current purchasing power at the end of the reporting period. Therefore, transactions in 2018 and non-monetary balances at the end of the period should be restated to reflect a price index that is current at the balance sheet date.

The comparatives and the opening statement of financial position at the beginning of the earliest period presented should also be restated to reflect a price index that is current at the balance sheet date. Entities are not required to present an additional balance sheet as at the beginning of the preceding period.

Multinational companies that have subsidiaries with a hyper-inflationary currency as their functional currency should consider paragraph 43 of IAS 21, which requires the financial statements of a subsidiary entity that has the functional currency of a hyper-inflationary economy to be restated in accordance with IAS 29 before being included in the consolidated financial statements. Comparative amounts presented previously in a stable currency are not restated.
For further details about the initial application of IAS 29, please refer to 'PwC In depth INT2018-12 – IAS 29 becomes applicable in Argentina'.

South Sudan

IMF data shows that the three-year cumulative inflation rate is expected to significantly exceed 100% at 31 December 2018 and is expected to remain significantly above that threshold in future years. South Sudan continues to be a hyper-inflationary economy in 2018. Entities with the currency of South Sudan as their functional currency should continue to apply IAS 29 in 2018.

Sudan

Sudan became a hyper-inflationary economy in 2013. In 2016, it ceased to be hyper-inflationary, because the three-year cumulative inflation rate at the end of that year was below 100% and was forecast to remain below 100%. Based on IMF data for 2018, the three-year cumulative inflation rate has increased significantly and is expected to be above 100% in 2018, and to remain above that threshold in 2019. Therefore, IAS 29 should be applied by all entities with the currency of Sudan as their functional currency in 2018, and it should be applied as if the economy had always been hyper-inflationary. For further details about the initial application of IAS 29, please refer to the section about Argentina above.

Syrian Arab Republic

There is no reliable inflation data for the Syrian economy. However, the situation in this country has not changed from last year. European Union and United Nations trade sanctions remain in force. The information that is available suggests that Syria remains a hyper-inflationary economy in 2018. Entities with the currency of Syria as their functional currency should continue to apply IAS 29 in 2018.

Venezuela

Venezuela became hyper-inflationary in 2009. IMF data shows that the three-year cumulative inflation rate is expected to significantly exceed 100% at 31 December 2018 and is also expected to increase in future years. Venezuela remains a hyper-inflationary economy in 2018. Entities with the currency of Venezuela as their functional currency should continue to apply IAS 29 in 2018.

Watch list for 2019

Democratic Republic of the Congo

IMF data shows that there was a significant increase in the expected three-year cumulative inflation rate for 2018, and that cumulative inflation might exceed 100% by the end of 2018. However, recent local data from the Central Bank and the National Statistics Institute indicates an expected cumulative inflation rate below 100% at 31 December 2018. The inconsistent data suggests that entities with the currency of Democratic Republic of the Congo as their functional currency should not apply IAS 29 in 2018. Such entities should monitor inflation during 2019.

Iran

IMF data shows that the three-year cumulative inflation rate for 2018 is below 100%, but there was a significant increase when compared to the same index for 2017. Entities with the currency of Iran as their functional currency should not apply IAS 29 in 2018. Such entities should monitor inflation during 2019.

Libya

IMF data shows that the three-year cumulative inflation rate is slightly above 100%, but it is expected to decrease in 2019. Local data suggests that cumulative inflation is lower than the IMF estimates. The inconsistent data suggests that entities with the currency of Libya as their functional currency should not apply IAS 29 in 2018. Such entities should monitor inflation during 2019.

Suriname

IMF data shows that the three-year cumulative inflation rate is below 100% at 31 December 2018. Local inflation data does not show recent high levels of inflation. Entities with the currency of Suriname as their functional currency should cease to apply IAS 29 in 2018. Such entities should monitor inflation during 2019.

Paragraph 38 of IAS 29 states that the amounts in the financial statements as at the end of the previous reporting period are considered as the carrying amounts for the subsequent financial statements. That is, the restated amounts are the cost bases of the non-monetary items in subsequent financial statements.

Other potentially hyper-inflationary economies

Yemen

IMF data shows that the three-year cumulative inflation rate is close to 100%. Local data also shows a cumulative inflation rate below 100%. There is currently not enough information to determine whether Yemen has become a hyper-inflationary economy. Entities with the currency of Yemen as their functional currency should monitor developments in inflation at the end of 2018 and during 2019.

No let-up: Why insurers can't afford to lose sight of IFRS 9

The new accounting rules for insurers who have already elected to defer changes to their financial instruments accounting by 3 years, may have been delayed by an additional year, but they've not gone away. With so much to do and so many complex hurdles to overcome, to stand still is to fall behind.

Most market attention has focused on the extension of the deadline for the IFRS 17 Insurance Contracts standard, however the parallel deferral of IFRS 9 Financial Instruments for insurers also comes with significant pitfalls but also opportunities.

So why is it vital not to lose sight of IFRS 9? Given the importance of matching assets and liabilities, preparations for IFRS 17 and IFRS 9 should be as closely aligned as possible – the IASB's decision to put both accounting standards back to 2022 recognises this.

Imminent disclosure requirements

The immediate challenge is the IFRS 9 deferral disclosures that need to be incorporated within your upcoming 2018 financial statements.

Whilst relatively brief, the disclosures may require a considerable amount of background work, depending on your existing financial asset mix. This includes your justification for applying the temporary exemption to IFRS 9.

Other tricky elements include reporting fair value information separately for financial assets that meet the Solely Payments of Principal and Interest (SPPI) contractual cash flow test and those that will be measured at fair value through profit or loss (FVTPL).

You can't assume that classification and measurement will be the same as IAS 39 - the new business model criteria can produce some surprising results. If you currently hold available-for-sale or held to maturity investments, you also face the challenge of testing a large number of financial instruments to check whether they're SPPI-compliant or not – how can you make that process more manageable?

Balancing volatility and operational complexity

As you gear up for going live in 2022, key hurdles include determining the most appropriate classification of financial instruments and calculating the new expected credit loss impairment requirements.

The desire to minimise accounting mismatches may require you to go through all your financial assets to gauge the business model the financial instrument is held in, the cash flow criteria of the instrument and how this tallies with the corresponding insurance liabilities. Specifically, it should be noted that debt instruments that fail the SPPI criteria and most equity instruments are now expected to be measured at FVTPL, including puttable instruments on mutual funds.

Key considerations don't just include the asset-liability management (ALM) and the income statement implications of the accounting option, but also how much work is required.

For example, the Other Comprehensive Income (OCI) option under IFRS 17 can reduce volatility in profit or loss where financial assets are measured at fair value through OCI under IFRS 9. However, this option can greatly increase the operational complexity of preparing financial statements, due to the need to calculate impairment on the investment portfolio and complete SPPI testing on purchases.

Making the most of the benefits

The good news is that close alignment between IFRS 9 and IFRS 17 can help to improve the quality and efficiency of financial reporting. This includes opportunities to streamline the chart of accounts and data collection, data storage and data dictionary solutions.

Bringing implementation together could also provide an important foundation for any finance transformation. The potential benefits include a faster period end close process, real-time performance data and differentiating insights into commercial threats and opportunities.

So how much alignment in the implementation of IFRS 9 and IFRS 17 are we seeing? Surprisingly little given both the matching challenges and potential advantages. It would appear that the original deadlines may have led to a siloed 'needs-must' approach. Therefore, one of the key benefits of the extra year to prepare is bringing the two accounting challenges together and moving forward on one front.

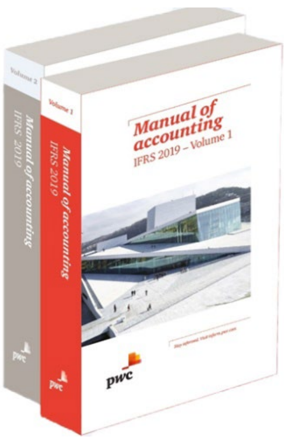
Look out for PwC's report on what IFRS 9 means for insurers of the future, which we'll be launching early in 2019.

Word on the Wharf?

The December 2018 IASB update has been published and the work plan updated.

The topics, in order of discussion, were:

- Insurance Contracts
- Updating a Reference to the Conceptual Framework (Amendments to IFRS 3)
- Provisions
- Dynamic Risk Management
- Business Combinations under Common Control
- Primary Financial Statements
- Research Programme
- Pension Benefits
- IBOR Reform and its Effects on Financial Reporting
- Rate-regulated Activities
- Disclosure Initiative: Accounting Policies
- Implementation matters—Accounting Policy Changes



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