Year-end Updates

Financial Reporting Webinar Series

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Thursday, 7 December 2023

Looking back: challenges during the year

- Geopolitical risk
- Market volatility
- Business interruption
- Rising interest rate
- Tax reforms
- Climate change

Financial reporting implications:

- **Financial instruments**
- **Impairment**
- **Fair value measurement**
- Onerous contracts assessment
- Income tax
- Cash & cash equivalents and cash flow statement
- Disclosure on going concern
- **Connectivity with other information**

Macroeconomy – Interest rate risk

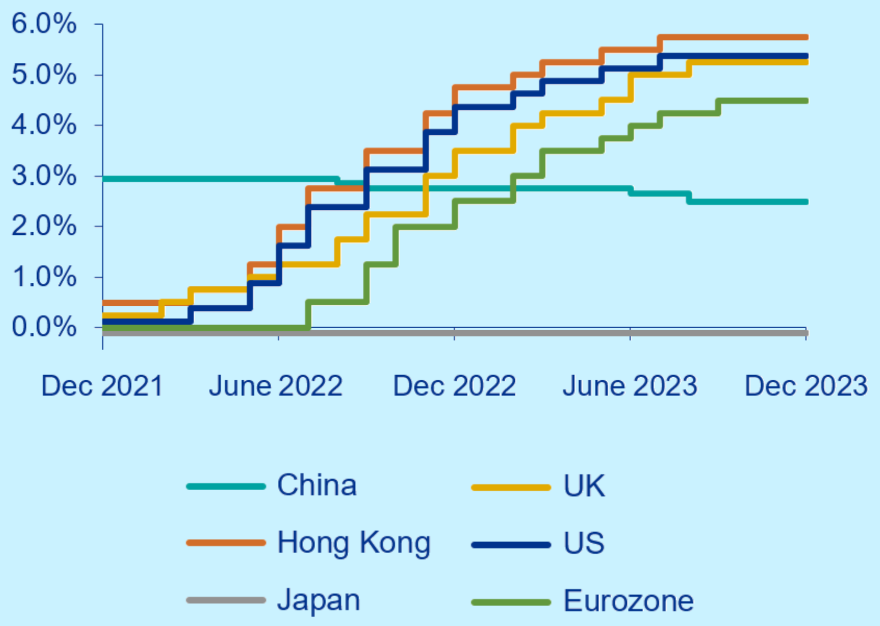
Consider the effects of interest rate volatilities on:

01 Your entity's risk exposures and how the risks are managed

02 Your entity's ability to meet loan covenants

03 Sensitivity analysis

Policy interest rates



Source: Bloomberg

Macroeconomy – Liquidity risk and hedge accounting

Interest rate risk and other market risks

Credit risk and expected credit losses (ECLs)

Hedge accounting

Hedge effectiveness

Potential discontinuation

Liquidity risk

- Maturity analysis
- Risk concentration
- Renegotiations of borrowings and their implications

Borrower

Lender

Under the spotlight – Relevance of inputs for ECL assessment

01 Probability of default

- Likelihood that a borrower will fail to pay 'on time'
- Forward-looking

03 Exposure at default

- Total value the lender is exposed to when the debt instrument defaults

$$ECL\ allowance = \sum_{t=1}^{T} PD_t \times LGD_t \times EAD_t \times D_t$$

Application to intra-group balances

02 Loss given default

- Estimated amount of loss *in case that* a borrower defaults
- Forward-looking

04 Discounting

- All cash flow shortfalls discounted at the effective interest rate

IAS 36 impairment – reminders

Ensure that the assumptions used by the management are supportable by market evidence

Given the increased uncertainty and market volatility at present, critically challenge the key assumptions, including but not limited to projected revenues.

Disclosures continued to be the regulatory focus

If the company has a material impairment (or impairment reversal) and/or material intangible assets, regulators (e.g. HKEX) are expecting additional disclosures.

Also consider climate-related matters and consistency between financial statements and non-financial information, see later slides.

HKEX's recommended disclosures related to impairments

Material asset impairments

- Details of the value of the inputs together with the bases and assumptions
- Reason for any significant changes in the value of the inputs and assumptions
- Valuation method and reasons for using that method
- Explanation of any subsequent changes to valuation method

Material intangible assets

- Additional quantitative data of key assumptions, comparative information in previous year and any significant changes
- Negative statement on reasonably possible changes in key assumptions would not cause an impairment loss
- Recoverable amount of the CGU and headroom available
- Whether the impairment assessment is assisted by an independent professional valuer
- Details of further development of the CGU or segment

Reference material:

- Review of Issuers' Annual Reports (2022) (Paragraphs 28 and 80)

Example of connectivity : Imerys SA

How climate related matters impact key assumptions in the VIU calculation.

EXAMPLE 8 – IMERYS SA

Pages 213; 238

ESMA emphasis added in *Orange*

Exposure to climate risks.
Given their geographic location, the Group's entities may potentially be exposed to physical risks related to climate change, such as flooding, heat waves, wildfires and droughts. At December 31, 2022, the carrying amount of these sites represented **10.2% of the Group's consolidated assets (2.5% at December 31, 2021).** Criteria for the identification of these sites are described in Note 19.
(…)
Note 19 Impairment Tests
(…)
Furthermore, Imerys **calculated its sensitivity to risks arising from climate change with respect to the global warming scenario of +2°C by 2050**, as projected by the International Energy Agency (IEA) in its Stated Policies Scenarios published in the World Energy Outlook in 2019. Executive Management selected this scenario, which represents one of the three trajectories modeled by the IEA, **for the sensitivity tests as it is deemed to be reasonably possible. Risks accounted for in this model are heat waves as identified by the S&P Global Trucost Assessment, wildfires as identified by the FM Global Assessment and the Angström index and drought as identified by the Water Risk Filter of the World Wild Fund for Nature and the Deutsche Investitions- und Entwicklungsgesellschaft. Sites included in the sensitivity exercise are those where risks are recognized as uninsurable in the long term, based on the most recent information available at December 31, 2022** as well as **those which are usually insurable, but are specifically recognized as uninsurable due to specific climate conditions**. On this basis, Executive Management **has estimated the frequency of planned closure for each site, as well as the corresponding cash flow losses**.

As summarized in the table below, the sensitivity calculated in the mid case scenario indicates, in Performance Minerals, Asia Pacific (PMAPAC) excluding G&C, **an impairment of -€12.5 million in the event of a 1.00% increase in the discount rate and an impairment of -€4.5 million in the event of a 1.00% decline in terminal growth rates. However, the sensitivity calculated on risks and opportunities arising from climate change did not indicate any impairment.**
(…)

Quantitative information regarding tangible assets' exposure to climate risks.

Details of sensitivity analysis performed to risks arising from climate change with respect to **2°C by 2050.**

Disclosure of the external sources used and rationale for selecting this source.

Source:
[Report - Disclosures of Climate Related Matters in the Financial Statements]

Fair value measurement of investment properties– reminders

Issuers should be able to explain key inputs used in valuation even external experts are used

Adoption of additional valuation method if comparable transactions are limited and not reflecting macroeconomic condition

Preparation of sensitivity analysis on key unobservable inputs are encouraged

Disclosing significant changes in valuation techniques and input and the reasons, as appropriate

NRV test for real estate properties inventory – carefully consider the assumptions used for estimates

Standards and amendments effective from 1 January 2023

IFRS 17 *Insurance Contracts* and amendments

Amendments to other IFRSs[1]

- IAS 1 and IFRS Practice Statement 2 *Disclosure of Accounting Policies*
- IAS 8 *Definition of Accounting Estimates*
- IAS 12 *Deferred Tax Related to Assets and Liabilities Arising from a Single Transaction*
- **IAS 12 *International Tax Reform – Pillar Two Model Rules***

New HKICPA guidance on the accounting implications of the abolition of the MPF-LSP offsetting mechanism in Hong Kong[2]

Other amendments

- **IAS 1 *Classification of Liabilities as Current or Non-current*[1]**
- IFRS 16 *Lease Liability in a Sale and Leaseback*
- IAS 7 and IFRS 7 *Supplier Finance Arrangements*
- IAS 21 *Lack of Exchangeability*

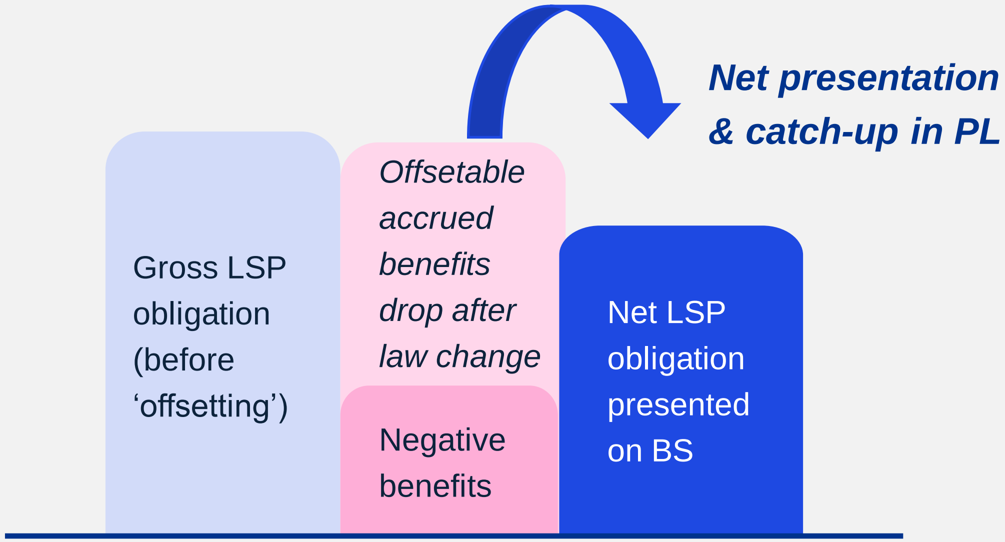
2023 → **Beyond 2023**

1. Playback of our webinar Interim Reporting Reminders and IASB Developments
2. Playback of our webinar Abolition of MPF-LSP Offsetting and Its Accounting Considerations

HKICPA guidance on long service payment accounting

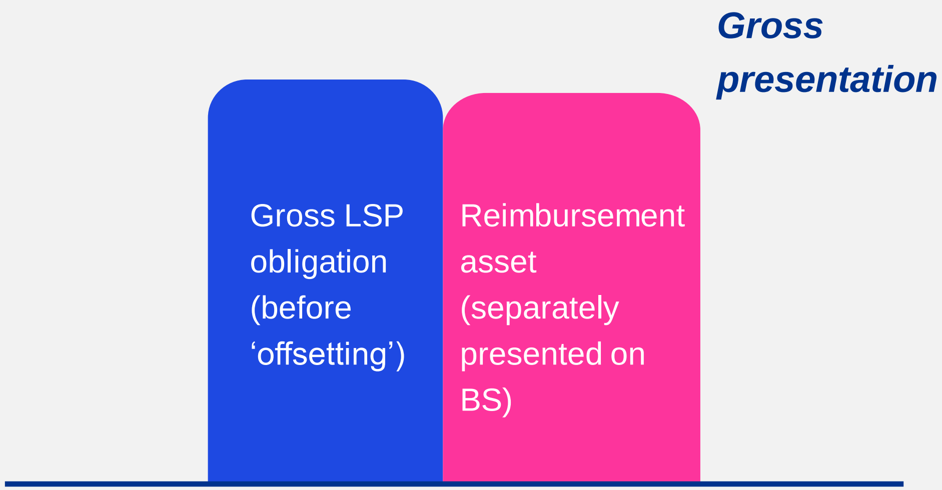
Approach 1

Amount offset is deemed the employee contribution towards his LSP benefits (by forgoing his offsetable accrued MPF benefits)



Approach 2

Amount offset is treated as the reimbursement to the employer for his LSP obligations (akin to a claw back of the offsetable accrued MPF benefits)



The practical expedient under HK/IAS 19.93(b) is no longer applicable

Connectivity between financial statements and front part of annual report

Users are interested in understanding how the key assumptions and judgements underlying the information on climate-related matters disclosed reconcile with financial statements.

Financial statements

Same assumptions, as appropriate

Disclose differences and the reasons

Other information (include climate-related disclosures)

High-level principles used to identify connectivity

- Consistency and coherence
- Cross-referencing
- Complementarity
- Avoidance of repetition

Webinar dates and topics for 2023

- 22 February – Capital Market and HKEX Listing Rules Update
- 28 April – Sustainability Reporting Developments
- 2 June – Interim Reporting Reminders and IASB Developments
- 11 August – Abolition of MPF-LSP Offsetting and Its Accounting Considerations
- 11 September – Get Ready to Implement ISSB's IFRS S2 Climate Standard
- **7 December – Year-end Updates**

For more details and access to our webinar series:

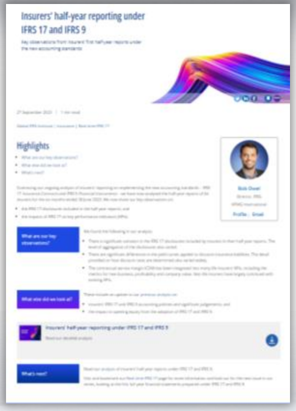
https://home.kpmg/cn/en/home/services/audit/ifrs-news/financial-reporting-webinar-series.html

Resources

Report
The Heat is On: Disclosures of Climate-Related Matters in the Financial Statements

Educational material
Effects of climate-related matters on financial statements

Our one-stop climate-change financial reporting page



Insurers' half-year reporting under IFRS 17 and IFRS 9 - KPMG Global

Global minimum top-up taxes in 2023 reports

Illustrative HK/IFRS illustrative disclosures

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