Reforming of accounting for consequences of emergencies caused by hostilities as an element of state policy

Abstract. The authors of the article have improved the existing methodological framework related to accounting for enterprises' property and property transactions on the temporarily occupied territories with differing order of accounting which depends on accessibility (recognition of property loss, its disposition, preservation, and transportation), which appears to be an informational basis for decision-making concerning enterprises’ activities on the temporarily occupied territories. The article deals with methodological proceedings of accounting for economic and environmental consequences of the hostilities for enterprises fully or partly functioning within a territory during or in connection with hostilities with regard to: 1) business activities on the territory controlled by state authorities in the part of the structure of inventory objects and the relevant results, valuation of current and non-current assets and operation cost, as well as the reflection of loss of assets on the accounts, work in progress and the costs involved; 2) business activities on the territory outside the control of state authorities in the part of the preservation of property and the writing-off of loss of property, which is determined by the ability to receive official information.

Keywords: Accounting; Public Management; Accounting Legislation; Consequences of Emergencies; Loss; Property; Liabilities; Autonomous Republic of Crimea; Donetsk Region; Luhansk Region

JEL Classification: M40; M41

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1. Introduction

The crime situation in the country and worldwide, the long-term military operations in Eastern Ukraine have lead to both public and private business losses. As a result of hostilities, the business sector has already suffered on the territory of the anti-terrorist operation, in particular large industrial enterprises have been affected. Perceiving military operations, the extremists’ captures or the seizure of ships as an emergency, it is worth mentioning that there are essential economic and environmental consequences affecting economic and environmental security of the enterprises. Unstable economic conditions caused by both military actions and direct takeovers of the enterprises or their subsidiaries with the use weapons are crucial in this context. Certain dangerous events may make industrial enterprises face the emergencies which are either of a purely economic nature or have combined economic, social and environmental effects that inevitably lead to the losses.
These effects can develop into the loss of the property or even the loss of entire property complexes due to the damage done to the production facilities, over the government, pollution, etc. This becomes particularly evident on the territories under the anti-terrorist operation in certain areas of Donetks and Luhansk regions. According to Director General of the State Concern «UkrOboronProm» [16], 12 companies of the Group have been damaged on the territory where the hostilities are currently taking place, while 13 more are under reorganisation. However, economic and environmental consequences of the mentioned emergencies are not solely measured by the quantitative loss of businesses; they also cause heavy social, environmental, and economic losses.

All the issues outlined above point to a need for developing sufficient organisational and methodological statements that would consider the status of such territories, and provide the complete identification of economic and environmental consequences for security management at the industrial enterprises.

The designated problem is urgent for Ukraine and for other countries of the world. Firstly, for the countries residents of which have property or production capacities in the occupied territories or the territories where the hostilities are taking place; secondly, for foreign investors who have made investments in the business entities which are situated in the specified territories; thirdly, for the international organisations giving financial support to Ukraine. These effects can develop into the loss of the property or even of whole property complexes due to the damage done to the production facilities, over the government, pollution, etc. This becomes particularly evident on the territories under the anti-terrorist operation in certain areas of Donetks and Luhansk regions. According to Director General of the State Concern «UkrOboronProm» [16], 12 companies of the Group have been damaged on the territory where the hostilities are currently taking place, while 13 more are under reorganisation. However, economic and environmental consequences of the mentioned emergencies are not solely measured by the quantitative loss of businesses; they also cause heavy social, environmental, and economic losses.

• in terms of accounting for assets, «According to part 3 of Article 11 of the Law on individuals, regardless of their acquisition of refugee status or other special legal status, enterprises, institutions and organisations retain the right of ownership and other property rights to the property, including real estate and land, located on the temporarily occupied territory if it was acquired in accordance with the laws of Ukraine. Assets, located on the temporarily occupied territory are to be disclosed in financial statements by public joint companies in accordance with IFRS. According to International Accounting Standard 36 «Impairment of assets>, one of the indicators of impairment of assets is changes with substantial negative effect on business entity in technology, markets, economy, or law environment of business entity’s functioning, or in the market an asset is intended for. Taking into account, the Ministry of Finance of Ukraine has clarified that the objects, located on the temporarily occupied territory of Ukraine, are to be recognised as assets of the company. At the same time, the company has to assess the negative impact changes in the economic and legal environment and to recognise the amount of impairment loss related to these objects» [8];

• in terms of inventorying, the changes into the order of the financial statements presentation have been introduced, in particular: «Companies located on the temporarily occupied territory and/or on the territory of the anti-terrorist operation or their units and affiliates with the separate property, which are located on such territory, have to undertake inventorying only if the authorised persons are with the safe and unimpeded access to assets, source documents and accounting ledgers where liabilities and equity of an enterprise are reflected. In the annual financial statements information about assets, to which safe and unimpeded access is impossible to ensure, as well as equity and liabilities cannot be clarified by the sufficient documents due to lack of access to relevant source documents and accounting ledgers, is to be disclosed according to a simplified accounting. Enterprises belonging to the defined category are required to undertake inventorying as on the first day of the month following the month, in which access to assets, source documents and accounting ledgers was terminated, and to disclose the results of the inventorying in the accounting in the reporting period» [12];

• in terms of inventorying of inventory, «Companies located on the temporarily occupied territory and the territory of military operations. As a result, the companies could incur losses such as the fixed assets damaged or destroyed, production losses, the stocks of inventories and finished goods destroyed and damaged, etc. Secondly, the companies located on the territory of Ukraine where there are no hostilities may have property or property complexes within the combat zone or territories temporarily not under control of the Ukrainian authorities. In this case, accounting for such property seems to be problematic, considering the necessity for recognising the objects of fixed tangible assets, writing off current assets with terminated useful life, closing the production process, writing off production costs incurred earlier due to failure of production cycle, etc. Thirdly, domestic enterprises have assets located on the temporarily occupied territory of the Autonomous Republic of Crimea, causing a problem of re-recognising the assets in accounting system. Thus, according to the Law of Ukraine «On guaranteeing the rights and freedoms of citizens and legal regime on the temporarily occupied territory of Ukraine», a temporarily occupied territory is referred to as: «1) the land territory of the Autonomous Republic of Crimea and the city of Sevastopol, inland waters of Ukraine of these areas; 2) internal sea waters and territorial sea of Ukraine around the Crimean Peninsula, the area of the exclusive (maritime) economic zone of Ukraine along the coast of the Crimean peninsula and adjacent to the coast of the continental shelf of Ukraine that are within the jurisdiction of the government of Ukraine in accordance with international law, the Constitution and the laws of Ukraine; 3) the airspace over the territories referred to above» [7];

In connection with the events, the public authorities have adopted a number of regulations and the Ministry of Finance of Ukraine has submitted clarifications, which affect accounting of the peculiar objects as follows:
The anti-terrorist operation or their units and affiliates with the separate property, which are located on such territory, have to undertake inventorying in cases, set as obligatory for its carrying out only when it becomes possible to guarantee safe and unimpeded access by the authorised persons to assets, source documents and accounting ledgers, where liabilities and equity of such enterprises are reflected. The defined category of the enterprises are required to undertake inventorying as on the first day of the month following the month in which barriers to assets, source documents and accounting ledgers have disappeared, and to disclose inventorying results in accounting entries of the appropriate period [10].

Despite the regulations which have been enacted and provide guidelines and explanations concerning accounting reflection of the property, the main problem still remains unsolved. In particular, the Autonomous Republic of Crimea has been declared a temporarily occupied territory for over a year. Consequently, its production capacity hasn’t been used by Ukrainian industrial enterprises since then and, therefore, they do not have economic benefits. Additionally, those enterprises don’t have access to some objects. A similar situation can be observed in certain areas of Donetsk and Luhansk regions, which are not controlled by the Ukrainian authorities.

Generally, the effects of the temporary occupation of the Autonomous Republic of Crimea and the anti-terrorist operation in Donetsk and Luhansk regions are shown in conjunction with accounting objects at industrial enterprises (Figure 1). Moreover, the temporarily occupied territories and areas that are beyond the control of the Ukrainian authorities have been proposed in this connection. It is necessary to develop organisational and methodological principles of accounting for losses at the industrial enterprises as a result of the temporary occupation and military operations on the territory where their property is located. While considering the organisational and methodological aspects, it is preferable to take into account all the possible transactions related to the studied type of emergencies.

First of all, the peculiarities of accounting of assets located on the temporarily occupied territory will be studied. The organisational and methodological principles of accounting for business transactions of this kind should consider all the alternatives of property movement. A new approach towards accounting of such operations is presented in Figure 2.

Thus, the Law of Ukraine «On guaranteeing the rights and freedoms of citizens and legal regime on the temporarily occupied territory of Ukraine» has regulated only few economic and legal aspects of business activities of industrial enterprises or their subdivisions in the Autonomous Republic of Crimea.

In turn, the effective recommendations on accounting of such property do not provide a solution to the main problem of usage of property. Thus, provided that the company has access to its property, three alternatives are available as follows.

**Alternative A** - disposition / sale of property. This option seems to be a logical one, provided that the company is willing to discontinue its activity on the temporarily occupied territory, as there is no assurance that such activity will comply with the legislation of Ukraine in the future. Moreover, the temporarily occupied territories have had such a status for nearly two years already, which corresponds to the reporting period; production capacity has not been used, which, in turn, influenced the financial performance. As for the definite transactions of property sale, there can be two alternatives if such operations are carried out in the Autonomous Republic of Crimea: the first one is the sale of property to a resident of Ukraine and the second one is the sale of property to non-residents. In case of selling a property to a resident of Ukraine, the accounting system will record the process of disposition of assets (current and noncurrent assets, finished goods) in compliance with the requirements of the National Accounting Standards (Provisions) and pay the proper taxes in accordance with the provisions of the Tax Code of Ukraine. A completely different situation is faced in case the property is sold to non-residents. This situation is specific because of the necessity to record export transactions without actual crossing the border. Consequently, the transactions will be reflected in accounting system with the proper tax assessments in compliance with the Tax Code of Ukraine, however excluding payments of customs duties.

**Alternative B - preservation of non-current tangible assets.** Provided that the company is willing to temporarily discontinue its activity on the temporarily occupied territory, we find it reasonable to allow to preserve such objects of fixed assets at the state level by introducing amendments to the Law of Ukraine «On guaranteeing the rights and freedoms of citizens and legal regime on the temporarily occupied territory of Ukraine» as follows: «The companies that possess property (or integral property complexes) located on the temporarily occupied territory and intend to temporarily suspend their business activities on such territory can preserve such property». Preservation of the property shall be subject to the Provision on the preservation of fixed assets of enterprises [11]. In accordance with the Provision, preservation is referred to as «a set of measures aimed at long-term (but not more than three years) storage of fixed assets of enterprises in case of termination of production and other business activities with the possibility of restoring their functioning». This provision obligates enterprises of strategic importance for the country’s economy and national security, as well as state-owned enterprises. Private sector enterprises may use the Provision as an advisory regulation. However, under terms of preservation of objects located on the temporarily occupied territory, such procedure must fully comply with the mentioned regulations. In the accounting system, such business transactions are to be recorded by recognising the status of the object by introducing more detailed accounts. At the same time, the objects of non-current assets with the expired useful life are to be written off in accordance with the current legislation under which the residual value is to be reflected on the account 976 «Writing off non-current assets» (according to the National Chart of Accounts of Ukraine).

The situation turns to be different in relation to the current assets. Preservation of the fixed assets assures that current assets can be disposed in a way as described in Alternative A. However, if damaged due to the termination of production cycle under uncertainty of the status of temporarily occupied territory, the value of inventories and finished goods can be suggested to be written off and recognised as part of economic loss from emergencies with the accounting entry:

**Alternative C -**

- An enterprise re-recognises noncurrent tangible assets and writes off current assets.
DR 978.1 «Economic loss from emergencies»
CR 20 «Inventories», CR 26 «Finished goods».
Production costs, which did not result in generating finished goods, are to be written off to losses from emergencies as well: DR 978.1 «Economic loss from emergencies»
CR 23 «Work-in-process» 91 «Overhead production costs».

Alternative C - transportation (exfiltration) from the temporarily occupied territory. This option is possible for the enterprises to fulfil. Besides, such an operation does not entail any customs duties. In the accounting system, entries are made to show the change of the analytical accounts in terms of changing of financially responsible person and the location of the property. Such an option provides for the closing of the business activity of an enterprise on the temporarily occupied territory. Regarding the fact that the occupation of the territory is referred to as an emergency, the costs incurred to transport fixed assets are to be reflected as losses from emergency.

Consequently, the accounting entries will be made as follows: DR 978.1 «Economic loss from emergencies», CR 20 (Material costs), CR 66 (Labour costs), CR 65 (Social insurance costs), CR 13 (Accumulated depreciation), CR 685 (Other accounts payable). The cost of current assets and work-in-process damaged and lost, as well as other costs incurred are to be expensed as losses from emergency.

The lack of accessibility to the property of an enterprise on the temporarily occupied territory assumes that assets can be reflected in accounting in two ways:

• the first method reflects preservation of fixed assets, leading to reclassification of the objects of PPE (Property Plant Equipment). In addition, the residual value of fixed assets with the expired useful life is to be recognised as part of the losses from emergencies. All current assets, finished goods and work-in-process are to be written off to losses;

• the second method assumes writing-off noncurrent and current assets and recognising them as losses from emergencies; the residual value of fixed assets should be estimated at fair value if it exceeds the residual value. Reflection of value difference is made by reducing goodwill. Current and non-current assets, finished goods and work-in-process are expensed to losses from emergencies.

Thus, it has been proposed to apply a new approach towards accounting reflection of losses from emergencies arising from the occupation of territories. The implementation of this approach at the national level is possible by enacting the Methodical Guidelines by the Ministry of Finance of Ukraine or the Cabinet of Ministers of Ukraine. This will enable resolving of the problems arising from the temporary occupation of the Autonomous Republic of Crimea.

The issue of accounting the consequences of hostilities is becoming particularly relevant for the industrial enterprises in Ukraine. These consequences for the industry can be applied in two situations: firstly, in the area of hostilities being under the control of the Ukrainian authorities and, secondly, on the territory of the military operations, which is not controlled by the Ukrainian authorities. The worked out approach towards accounting economic and environmental consequences of the hostilities on the territory controlled by the state authorities is presented in Table 1.

The presented methodological principles of accounting for losses at the industrial enterprises as a result of hostilities and military operation is a logical continuation of the comprehensive organisational and methodological approach towards accounting and analytical support of management of economic and environmental consequences of the emergencies in order to provide economic and environmental security [5].

Regarding the enterprises that function on the territories outside the control of the Ukrainian authorities, the following ways of keeping accounting records of their assets can be considered (see table 1).

ACCONTING, ANAL YSIS AND AUDIT

Fig. 2: Accounting for operations with property located on the temporary occupied territories

Source: Developed by the authors

1. Preservation of property and write-off of current assets using one of the suggested methods for businesses property of which is located on the temporarily occupied territory. This variant is possible under the absence of public information disclosed by the government on the status of property on the mentioned territories. For example, when a company’s management has no information about the property available in a particular area and, consequently, is not capable of controlling it;

2. The company writes off the cost of the current and non-current assets, and work-in-progress to the losses on condition that information on the destruction of property on the territory is available and published by the government. Reflection on accounts is identical to the situation related to writing-off of assets located on the temporarily occupied territories in the lack of access to production facilities.

The practical application of such accounting methods is possible only if provided with the appropriate regulations at the level of the Ministry of Finance of Ukraine and the Cabinet of Ministers of Ukraine, as well as in cases when the permission has to be regulated for legal preservation and writing off of property of industrial enterprises to the losses and result from the emergencies caused by military operations or social issues in terms of terrorist attacks.

The proposed approaches will contribute to defining the directions as well as the way of state financing to bear the losses resulting from hostilities. The suggestions will enable to get clear and transparent information about the enterprise’s losses in the aggregate for further financing of the restoration at the cost of public and the international sponsorship, as well as obtaining deferral or instalment payments of tax liabilities and writing off bad tax debts.

Application of the author’s approach at the industrial enterprises will promote the development of a high-quality information system for managing economic and environmental security. However, these issues have not been fully regulated recently, which requires necessary and appropriate amendments to the effective legal and regulatory acts and approval of guidelines governing accounting for economic and environmental consequences of emergencies in general.
Table 1: Methodological aspects of accounting for economic and environmental consequences of hostilities on the territory not under control of state authorities

<table>
<thead>
<tr>
<th>INVENTORYING</th>
<th>DAMAGES PROPERTY</th>
<th>LOST PROPERTY</th>
<th>UNDAMAGED PROPERTY</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Non-current Assets</strong></td>
<td><strong>Current Assets</strong></td>
<td><strong>Work-in-Process</strong></td>
<td></td>
</tr>
<tr>
<td>Reversible</td>
<td>Irreversible</td>
<td>RESULT IN DETERMINING:</td>
<td></td>
</tr>
<tr>
<td>Assets, available for usage</td>
<td>Evaluation method</td>
<td></td>
<td></td>
</tr>
<tr>
<td>is carried in regard to: noncurrent assets at the book value and fair value, current assets at book value</td>
<td>Cost of the similar assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-current assets:</td>
<td>Work-off</td>
<td>Value type</td>
<td></td>
</tr>
<tr>
<td>lost</td>
<td>lost</td>
<td>Value at fair value</td>
<td></td>
</tr>
<tr>
<td>damaged</td>
<td>damaged</td>
<td>Fair value of the damage</td>
<td></td>
</tr>
<tr>
<td>Current assets:</td>
<td></td>
<td>Independent assessor</td>
<td></td>
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<tr>
<td>lost</td>
<td>Book value</td>
<td></td>
<td></td>
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<tr>
<td>damaged</td>
<td>Book value</td>
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<td></td>
<td>Book value less completion costs</td>
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<tr>
<td></td>
<td>Cost of the similar assets</td>
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<tr>
<td></td>
<td>Average price for the similar assets</td>
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<td></td>
</tr>
<tr>
<td>reversible</td>
<td>Quantitative assessment</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Amount of generated waste</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

ACCOUNTING POLICIES AND PROCEDURES CHART

<table>
<thead>
<tr>
<th>NONCURRENCE ASSETS</th>
<th>CURRENT ASSETS</th>
<th>WORK-IN-PROCESS</th>
</tr>
</thead>
<tbody>
<tr>
<td>DR Accumulated depreciation</td>
<td>DR Property, Plant, Equipment</td>
<td>DR Economic loss from emergencies</td>
</tr>
<tr>
<td>Writing off value not exceeding residual value</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
<td>DR Economic loss from emergencies</td>
</tr>
<tr>
<td>DR Economic loss from emergencies</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
<td>DR Economic loss from emergencies</td>
</tr>
<tr>
<td>Writing off the difference between fair value and residual value</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
</tr>
<tr>
<td>DR Goodwill loss from emergencies</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
</tr>
<tr>
<td>WASTES resulting from hostilities (Evaluation report, invoice)</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
<td>DR Inventories, CR Inventories, CR Finished goods</td>
</tr>
</tbody>
</table>

5. Conclusions

At present, the organisational and methodological approaches presented in the paper can be adapted to the legislation, particularly, in terms of tax regulations by implementing internal regulations and introducing changes into Accounting Policies and Procedures Chart of Accounts at the enterprise.

5. Conclusions

The lack of methodic guidelines on accounting the consequences of hostilities and occupation of public territories has led to misstatement of financial reports. Thus, it is suggested to take into account the specifics of the situation described in the paper in order to solve the problem mentioned above. With regard to accounting the economic and environmental consequences of emergencies both in the combat zone and on the occupied territories the following developments have been disclosed in the paper:

a) a methodology of accounting for consequences involving the peculiarities of emergencies;

b) an algorithm of accounting for assets and transactions with property located on the temporarily occupied territories; the algorithm determines the order of accounting the preservation, writing-off, transportation and disposition/sale of the property as an element of foreign economic activity;

c) a methodology of accounting for economic and environmental consequences of military operations on the territory both under and out of control of the state; the methodology determines accounting for consequences of hostilities, reclassification and re-recognition of non-current assets located on the uncontrolled territory.

The suggestions can be used for drafting regulatory acts in the sphere of accounting and assets management on the temporarily occupied territories and in combat zone.

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8. The Ministry of Finance of Ukraine (2014). Letter of the Ministry of Finance of Ukraine «On reflection in accounting of assets, located on the temporarily occupied territories the following developments have been disclosed in the paper:


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