MOORE

CORONAVIRUS OUTBREAK – THE POTENTIAL FINANCIAL REPORTING IMPLICATIONS FOR THE YEAR ENDED 31 DECEMBER 2019

March 2020

BACKGROUND

The recent outbreak and spread of the coronavirus has now disrupted many businesses globally and has had a significant impact on financial markets. This publication focuses on the potential accounting and financial reporting implications of coronavirus that management should take into consideration when preparing the financial statements for the year ended 31 December 2019. Different considerations will apply for later accounting periods e.g. for financial statements for periods ending 31 March 2020 or other accounting periods with a reporting date subsequent to the outbreak taking place.

EVENTS AFTER THE REPORTING PERIOD

RELEVANT STANDARD

IAS 10 **Events after the Reporting Period** are events that occur between the end of the reporting period and the date the financial statements are authorized for issue. IAS 10 defines adjusting events as those events that provide evidence of conditions that existed at the end of the reporting period, whilst non-adjusting events are those that are indicative of conditions that arose after the reporting period.

Under IAS 10 an adjusting event requires adjustment to the financial statements, whereas a non-adjusting event requires only disclosures, assuming the event, and the relevant disclosures, are material to the users' understanding of the financial statements. The exception to this is where the non-adjusting event impacts the appropriateness of the going concern basis of preparation of the financial statements.

CONSIDERATION

The situation in Wuhan which developed into the coronavirus outbreak was first reported to the World Health Authority ("WHO") on 31 December 2019 although the virus was not identified as coronavirus until 7 January 2020. The WHO officially declared the coronavirus outbreak as a public health emergency of international concern on 30 January 2020. Subsequently on 11 March 2020, the coronavirus outbreak has been classified by WHO as a global pandemic.

As the outbreak was not declared as an emergency until January 2020, the subsequent spread of the virus and the various control measures taken do not provide additional evidence about the situation that existed at 31 December 2019 (as at 31 December there was no explicit evidence of human-to-human transmission). As a result, these events are therefore likely to be non-adjusting in nature and the key issue for preparers of 31 December 2019 financial statements is whether any disclosure is required, and how extensive it needs to be.

DISCLOSURE REQUIREMENTS

If management considers that the impact on the business of the coronavirus outbreak and/or the control measures put in place is material to the understanding of the users of the financial statements, they should make transparent and specific disclosures about the impact in the December 2019 financial statements. IAS 10 requires that such disclosure should include the nature of the event and an estimate of its financial effect. If it is not possible to make such an estimate, a statement that such an estimate cannot be made is required.

GOING CONCERN

RELEVANT STANDARDS

IAS 10 **Events after the Reporting Period** requires that an entity should not prepare its financial statements on a going concern basis if events after the reporting period indicate that the going concern assumption is no longer appropriate.

IAS 1 **Presentation of Financial Statements** specifies required disclosures if the financial statements are not prepared on a going concern basis; or 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.

IAS 1 requires management to take into account all available information about the foreseeable future, which is at least, but not limited to, twelve months from the end of the reporting period, in order to assess whether the going concern assumption remains appropriate. In some jurisdictions a longer period of assessment is required, for instance in the United Kingdom the foreseeable future is considered to be twelve months from the date of approval of the financial statements.

CONSIDERATION

Many businesses have been adversely impacted by the coronavirus outbreak, operationally and financially, and other entities may well be affected in due course depending on how the outbreak and the measures taken to mitigate it develop. The consequence is, or could be, a negative impact on both profitability and cash flows.

Management is required to assess the business' ability to continue as a going concern. In doing so the standard requires that all available information about the future is taken into account. Management will need to consider the current impacts to business, as well as the anticipated future effects that the coronavirus outbreak could have on their business. Examples of considerations include the impact of: staff shortages, supply chain breakdown, reduced stock levels, unavailability of debt finance or alternative finance, the impact of loan covenants, the impact of transport/travel suspension, fluctuating interest rates and foreign exchange rates, contract WIP contract clauses, and recoverability of accounts receivables.

Given the unpredictability of the potential impact on business, management should consider carefully whether there are material uncertainties arising from the outbreak of coronavirus and/or its knock-on events that may cast significant doubt upon the entity's ability to continue as a going concern. If significant doubt exists, management should further consider whether the going concern basis of preparation of the financial statements is still appropriate. Generally, the going concern basis of preparation will still be used unless management either intend to liquidate the business or cease trading, or have no realistic alternative but to do so.

As the coronavirus situation unfolds and evolves, these considerations will require to be continuously assessed right up to the point of the date of issuance of the financial statements.

DISCLOSURE REQUIREMENTS

If it is determined that the going concern basis is still appropriate, but there are material uncertainties over the impacts of the coronavirus outbreak that may cast significant doubt upon the entity's ability to continue as a going concern, IAS 10 requires disclosure of these material uncertainties in the financial statements.

If management consider that the going concern basis is no longer appropriate and determined not to prepare the financial statements on a going concern basis, IAS 1 requires disclosure of this fact, together with the basis on which management have prepared the financial statements and the reason why the entity is not regarded as a going concern.

FAIR VALUE MEASUREMENT

RELEVANT STANDARD

IFRS 13 **Fair Value Measurement** specifies that when measuring fair value an entity shall take into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

CONSIDERATION

If an asset or a liability is measured through the use of unobservable inputs (i.e. Level 3 inputs), management should develop unobservable inputs by using the best information available at the measurement date, taking into account all information about the assumptions that market participants would use when pricing such asset or liability under current market conditions.

Entities should consider what information about the outbreak was known and knowable to the market participants at the reporting date in order to determine the fair value at that date.

Information on the development of coronavirus and/or the knock-on effects of the outbreak available subsequent to the year-end should not be therefore taken into account when measuring the fair value of an asset of a liability as of 31 December 2019, unless such information provides additional evidence of conditions that could have been reasonably known by market participants under a usual and customary due diligence performed at the measurement date, i.e. 31 December 2019.

DISCLOSURE REQUIREMENTS

In addition to the disclosure requirements specified in IFRS 13, management should also consider the relevant disclosure requirements as set out in IAS 10 **Events after the Reporting Period** if events or circumstances after the reporting date (i.e. the outbreak or control measures taken) trigger a decline in fair value of an asset or a liability and the impact is considered as material to the users of the financial statements.

IMPAIRMENT OF NON-FINANCIAL ASSETS

RELEVANT STANDARD

IAS 36 **Impairment of Assets** requires an entity to assess at the end of each reporting period whether there is any indication that a non-financial asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset.

CONSIDERATION

When assessing events after the reporting period and information received after the reporting period, in considering whether there is any indication of impairment, management should only consider the information which provides additional evidence over those conditions or events that already existed at the end of the reporting period.

For an impairment assessment where value in use is adopted in determining the recoverable amount, management should not apply hindsight when preparing the cash flow forecast or making projections. The assumptions have to be reasonable and supportable which will be based on the conditions that existed at 31 December 2019 and built on the best estimate of the economic conditions that will exist over the remaining useful life of the asset.

Management should consider IAS 10 to assess whether the events that occur or new information, available after the reporting date, that might affect the cash flow forecast are adjusting or non-adjusting events. For example, the panic buying consumption pattern which happened after the control measures were taken could not have been foreseen at the reporting date and therefore should not be included in the revenue projections.

DISCLOSURE REQUIREMENTS

Given the uncertainty brought about by the Coronavirus, management should consider providing detailed disclosures of the assumptions and sensitivities used.

EXPECTED CREDIT LOSSES

RELEVANT STANDARD

IFRS 9 **Financial Instruments** requires an entity to assess whether the credit risk on a financial instrument has increased significantly since initial recognition. It further specifies that if reasonable and supportable forward-looking information is available without undue cost or effort, an entity cannot rely solely on past due information when determining whether credit risk has increased significantly since initial recognition.

CONSIDERATION

Given the measurement of expected credit losses (ECL) is a probability weighted amount that is determined by evaluating a range of possible outcomes, there is significant debate as to whether it is appropriate to include the impact of the coronavirus outbreak in the ECL measurement for the year ended 31 December 2019.

Our current consideration of this is as follows:

Similar to impairment of non-financial assets as discussed above, management should avoid the use of hindsight in forming the accounting estimates and preparing the forecasts and only reasonable and supportable information existing or reflecting the conditions at the end of the reporting date should be considered in measuring the expected credit losses.

In other words, the subsequent events and conditions attributable to the development of coronavirus after the year-end should not be applied into the assessment of expected credit losses as future economic conditions, as they did not exist at the reporting date.

However, if the events after the reporting date provide additional information about the uncertainties that existed at the reporting date then these should be reflected in calculations. For example, the bankruptcy of a customer post year end could confirm that the debt was already credit-impaired at the end of the reporting date, and the bankruptcy was not purely due to the spread of the coronavirus, and may need to be taken into account in calculations.

DISCLOSURE REQUIREMENTS

In short, no matter what approach the entity chooses, the basis of the conclusions and considerations for the ECL estimate should be disclosed. Management should also consider the relevant disclosure requirements as set out in IAS 10 **Events after the Reporting Period** to provide adequate and appropriate disclosure that enables the users of the financial statements to understand:

- How the coronavirus outbreak and its associated events affect the entity;
- The estimated financial effect of the coronavirus outbreak

If management determined to take the coronavirus outbreak into account when measuring the ECL at the reporting date, given the ECL measurement involves high estimation uncertainty, disclosure should be provided to enable users of the financial statements to understand the impact of the coronavirus outbreak affecting the amounts, timing and uncertainty of an entity's future cash flows in assessing ECL.

OTHER IMPLICATIONS

OTHER ACCOUNTING ESTIMATES

There are a number of other areas of financial statements that may also be subject to estimation uncertainty. New information about the impact of coronavirus which became available subsequent to the reporting date does not provide additional evidence about the conditions that existed at 31 December 2019 and therefore should be disregarded by management when making the relevant assumptions or projections. IFRS standards involving accounting estimates include, but are not limited to:

- IAS 2 **Inventories** - Net realisable value of inventory
- IAS 12 **Income Taxes** - Recoverability of deferred tax assets and liabilities
- IAS 16 **Property, Plant and Equipment** - Remaining useful life and residual value of property, plant and equipment
- IAS 37 **Provisions, Contingent Liabilities and Contingent Assets** - Provision for liabilities

OTHER DISCLOSURE REQUIREMENTS

IAS 1 **Presentation of Financial Statements** requires an entity to disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Given the unpredictability of the development and spread of the coronavirus, it creates estimation uncertainty and elevates the risks that the carrying amounts of assets and liabilities may require a material adjustment in the subsequent financial year. Therefore, depending on the degree of risk, additional disclosures may be required in providing the relevant disclosures about management's significant estimates and judgements applied in relation to the coronavirus outbreak and its subsequent impact.

Depending on the nature of the assumptions and other circumstances, the disclosures include:

(a) the nature of the assumption or other estimation uncertainty;

(b) the sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity;

(c) the expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year in respect of the carrying amounts of the assets and liabilities affected; and

(d) an explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved.

REPORTING & ANNUAL SHAREHOLDER MEETINGS

Regulators and local authorities are taking different measures in response to practical difficulties brought by the coronavirus outbreak, below are some actions taken in certain jurisdictions:

- The US Securities and Exchange Commission ("SEC") announced on 4 March 2020 that, subject to certain conditions, it will give public companies affected by the coronavirus epidemic a 45-day extension to file certain financial disclosure reports that would otherwise have been due between 1 March and 30 April 30 2020.
- The Financial Conduct Authority ("FCA") in the UK is working in conjunction with the Bank of England and HM Treasury to closely engage with the financial services sector to ensure it is responding effectively to the coronavirus outbreak. FRA expects firms to ensure that they can meet their regulatory obligations, even if that involves operating remotely.
- The Securities and Futures Commission ("SFC") and The Stock Exchange of Hong Kong Limited ("HKEX") has issued a joint statement to provide guidance to listed companies and their auditors in relation to the disclosure of financial information in view of travel and other restrictions that have arisen in response to the coronavirus outbreak.
- On 7 February 2020, the Singapore Exchange Regulation ("SGX RegCo") decided to grant a conditional waiver to certain listed companies with large Chinese operations. The waiver provides the issuers an extension of up to two months to hold their Annual General Meetings to approve their 31 December 2019 financial results.

MORE READING ON

- SEC Public Statement on Continued Dialogue with Audit Firm Representatives on Audit Quality in China and Other Emerging Markets; Coronavirus — Reporting Considerations and Potential Relief
- ICAEW The Financial Reporting Implications of Coronavirus
- FCA Statement on Coronavirus
- SFC and HKEX Joint Statement in relation to Results Announcements in light of Travel Restrictions related to the Severe Respiratory Disease associated with a Novel Infections Agent
- SGX RegCo gives issuers up to 30 June 2020 to hold AGMs to approve FY Dec 2019 results amid 2019-nCoV situation
- FRC Advice to Companies and Auditors on Coronavirus Risk Disclosures

MOORE GLOBAL NETWORK

At Moore, our purpose is to help people thrive – our clients, our people and the communities they live and work in. We're a global accounting and advisory family of over 30,000 people across more than 260 independent firms and 110 countries, connecting and collaborating to take care of your needs – local, national and international.

When you work with Moore firms, you'll work with people who care deeply about your success and who have the drive and dedication to deliver results for you and your business. You'll have greater access to senior expertise than with many firms. We'll be here for you whenever you need us – to help you see through the maze of information, to guide you in your decisions and to make sure you take advantage of every opportunity. To help you thrive in a changing world.

CONTACT US

Find your nearest member firm at
www.moore-global.com

Or email:
marketing@moore-global.com

MOORE

www.moore-global.com