ICAEW KNOW-HOW
FINANCIAL REPORTING FACULTY

THE FINANCIAL REPORTING IMPLICATIONS OF CORONAVIRUS UNDER UK GAAP

GUIDE

9 March 2020

As coronavirus continues to spread and more information comes to light about the nature of the virus and its impact, companies with 2019 and early 2020 year-ends need to consider how it affects their business and how the effects should be reported in the accounts. This guide is primarily aimed at those entities preparing accounts in accordance with FRS 102.

GOING CONCERN

An entity that has close ties with areas severely affected by the COVID-19 virus, or is in other ways adversely affected (for example, the impact on businesses involved in tourism), may need to consider additional disclosures of any material uncertainties which cast significant doubt over its ability to continue as a going concern. In some circumstances it may be necessary to consider whether it is appropriate to prepare the accounts on a going concern basis (FRS 102.3.8-9).

When assessing whether the going concern assumption is appropriate, management must take into account all available information about the future, which is at least, but not limited to, 12 months from the date that the financial statements are authorised for issue.

REFLECTING CONDITIONS WHICH EXISTED AT THE BALANCE SHEET DATE

The general requirement is that the balance sheet reflects the position at the end of the reporting period (FRS 102.4.1).

As at 31 December 2019 China had alerted the World Health Organisation (WHO) of several cases of an unusual form of pneumonia in Wuhan. However, substantive information about what has now been identified as coronavirus (or COVID-19) only came to light in early 2020. Therefore for companies with a 31 December 2019 year-end, the emergence of coronavirus is a non-adjusting event.

Companies with 2020 year ends will need to consider the timelines more carefully to assess the conditions which existed at the relevant balance sheet date.

NON-ADJUSTING POST BALANCE SHEET EVENTS

Given the emergence and spread of the COVID-19 virus is not considered to provide more information about conditions that existed at the balance sheet date, the measurement of assets and liabilities in the accounts should not be adjusted for its potential impact (unless the impact is so far reaching that the entity is no longer considered to be a going concern). Although estimating future cash flows is often relevant when, for example, testing stocks, debtors and other assets for impairment, such estimates should nonetheless be based on what could have reasonably been known at the balance sheet date.

The nature of any material non-adjusting event and an estimate of its financial effect must be disclosed by way of note (FRS 102.32.10, FRS 102.1AC.39). Therefore, directors will need to consider the impact of the COVID-19 virus on the business, which will vary according to the specific circumstances in which it operates. This assessment may involve considering the impact of the virus in the countries in which it operates, on the supply chain and the broader impact on the global economy, for example customer confidence, future buying intentions and their ability to pay.

THE DIRECTORS' REPORT AND/OR STRATEGIC REPORT

In its Advice to companies and auditors on Coronavirus risk disclosures the FRC recommends companies consider whether to refer to the possible impact of coronavirus in their reporting of principal risks and uncertainties. When mitigating actions can be taken, these should also be reported alongside the description of the risk itself.

Small companies are exempt from the requirement to prepare a strategic report and, therefore, the requirement to report on principal risks and uncertainties. Small companies are also exempt from the requirement in the directors' report to provide particulars of important events affecting the company which have occurred since the end of the financial year and an indication of likely future developments in the business of the company. However, the directors' report represents an opportunity for the directors to communicate how the board is taking account of any challenges it faces.

In some circumstances it may be useful to provide information above the minimum required by law which may be of interest to other stakeholders such as customers, lenders or suppliers.

2020 YEAR-ENDS

As we progress through 2020, more information is coming to light on the scale and impact of coronavirus. There may be a greater degree of judgement required when identifying the conditions at the balance sheet date, and therefore assessing whether the developments are adjusting or non-adjusting.

A business that has been – or is likely to be – adversely affected by the COVID-19 virus will need to review all areas of the accounts that are subject to judgement and estimation uncertainty.

In a typical business, most assets are measured at cost or amortised cost. However, when the income or benefits the asset is expected to generate (ie, its recoverable amount) are lower than its carrying value, the asset is impaired and must be written down. FRS 102 has specific requirements which address how and when to test for impairment (see FRS 102.11.21 for financial instruments such as debtors, and Section 27 *Impairment of Assets* for stock and fixed assets, including goodwill and other intangibles). Fair value measurements of, for example, investment property, will need to be reviewed to ensure the values reflect the conditions at the balance sheet date. When reviewing whether it is probable that a deferred tax asset will be recoverable, the entity will need to consider the implications of any downturn in profitability.

Future operating losses are not recognised but it may be that some contracts have become onerous, for example operating lease contracts for assets associated with tourism or major events. In such circumstances FRS 102 requires a provision for the present obligation under the contract (FRS 102.21.1A and Example 2 of the appendix to Section 21).

Other areas of the accounts that are dependent on valuations and estimates include, but are not limited to, share-based payments, pension obligations and tax.

With the exception of small entities reporting under Section 1A of FRS 102, an entity must disclose key assumptions about the future and other key sources of estimation uncertainty at the balance sheet date that have a significant risk of causing material adjustments to the carrying amounts of assets and liabilities in the next financial year.

POST BALANCE SHEET REVIEW PERIOD

Events after the end of the reporting period include all events up to the date when the financial statements are authorised for issue (FRS 10.32.3). It is important to incorporate a comprehensive post balance sheet review in the year-end reporting plan, particularly as information about the scale and the impact of the virus changes frequently. The WHO issues regular updates on the virus.

CONSIDERATIONS FOR MICRO-ENTITIES

The recognition and measurement requirements for those entities applying FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* are broadly similar to those outlined above. However, FRS 105 requires only very limited notes to the accounts and does not require disclosure, for example, of non-adjusting post balance sheet events or key sources of estimation uncertainty. When a micro-entity includes information additional to the 'minimum accounting items' it must have regard to the requirements of FRS 102 Section 1A *Small Entities* that relate to that information (FRS 105.1.3).

ICAEW's Financial Reporting Faculty and Technical Enquiry Service will be monitoring events and the need for further guidance.

The Audit and Assurance Faculty has issued guidance designed for UK group auditors with component auditors based in China or other jurisdictions impacted by Coronavirus (COVID-19) Coronavirus (COVID-19): Considerations for Group Auditors.

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