

Preparation of Financial Statements under the COVID-19 Circumstances

From the Desk of Technical Services

April 2020

Foreword

We are witnessing unexpected and unprecedented changes in 2020.

The Coronavirus (COVID-19) health crisis is impacting all of us, having wide ranging economic and financial implications for global as well as Pakistan economy.

While still evolving, the uncertainty and economic hardship is affecting companies of all sectors and sizes. A significant number of companies have either completely or partially closed their operations. These events and conditions have wide-spread financial reporting implications, and companies would face a challenging financial reporting period ahead.

In these challenging times, shareholders, investors, regulators and other stakeholders need high-quality financial reporting more than ever.

Therefore, the board of directors, audit committees and management need to focus on understanding the implications of COVID-19 on financial accounting and reporting and respond to the challenges associated with the accounting issues while preparing annual and interim financial statements.

About this publication

To facilitate you in identifying key accounting matters and responding to those matters in accordance with the International Financial Reporting Standards (IFRS), the Institute's Technical Services team has prepared this publication '**Preparation of Financial Statements under the COVID-19 Circumstances**'. This publication has been prepared on the advice of the Accounting Standards Board.

In addition to responses to various accounting issues, you will also find a snapshot of industry specific key accounting considerations and a summary of regulatory reliefs granted by the Securities and Exchange Commission of Pakistan (SECP) and State Bank of Pakistan (SBP).

While this document has been prepared to facilitate you in understanding and responding to COVID-19 financial reporting implications, however appropriate responses to the issues will depend on each company's unique facts and circumstances. The guidance provided in this publication should be used in combination with a thorough analysis of the relevant facts and circumstances, review of the IFRS and other accounting literature, and appropriate professional and technical advice. In this publication, the terms 'balance sheet date' and 'reporting date' are used interchangeably.

The matters and examples included in this document are not all-inclusive, and this publication could be updated with additional and modified information. Further, in case of any specific or additional enquiry you may approach the Technical Services team.

We hope that mix of guidance in question and answer form and analysis of industry-specific considerations helps you in preparing financial statements under the COVID-19 circumstances.

Farrukh Rehman
Chairman Accounting Standards Board

Sohail Malik
Director Technical Services



Contents

	Page #
Introduction	1
Financial Reporting Implications – <i>Your questions answered</i> *	
General issues	
Going concern	3
Events after the reporting date	11
Statement of financial position	
Property, plant and equipment	18
Inventories	20
Provisions and liabilities	22
Leases	28
Financial instruments	30
Assets held for sale	34
Statement of profit or loss	
Revenue	35
Employee benefits	38
Borrowing costs	40
Income taxes	41
Government grant	43
Presentation and disclosures	44
Interim financial reporting	45
Industry Specific Considerations	46
Regulatory Reliefs	52

* Questions (Q) on the Financial Reporting Implications, listed on the next pages.

Financial Reporting Implications – *Your questions answered*

Page

Going concern

Q 1	In the COVID-19 impacted environment, why assessment about company's ability to continue as a going concern would be a key focus area for the preparers of financial statements?	3
Q 2	What is the explanation of terms 'liquidation' and 'cease trading'?	4
Q 3	In present environment, what would be the key considerations for management while assessing company's ability to continue as a going concern?	4
Q 4	For the going concern assessment, whether the events after the balance sheet date would be adjusting events or non-adjusting events?	6
Q 5	How management's assessment of going concern could impact company's financial statements?	6
Q 6	Management may determine that company would not be able continue its operations for next 12 months. In such a case, how financial statements on a non-going concern basis would be prepared?	8
Q 7	Due to the adverse impacts of COVID-19, management may decide to make the company dormant. How financial statements of a dormant company would be prepared?	10
Q 8	How the non-going concern assessment of a subsidiary could impact its separate financial statements and group's consolidated financial statements?	10

Events after the reporting date

Q 9	COVID-19 related events and conditions are expected to continuously develop and evolve. How a company would evaluate whether COVID-19 related events are adjusting events or non-adjusting events?	11
Q 10	A company with December 31, 2019 reporting date (or earlier periods) might not have issued its financial statements. In such a case, how COVID-19 related events would be considered for the determination of subsequent events?	12
Q 11	What would be the impact of COVID-19 related events on companies with March 31, 2020 (or later) year end?	13
Q 12	Company might be having difficulty in meeting the terms of the long-term debt agreement. If refinancing, waiver or amendment to a long-term financing arrangement is agreed after the balance date sheet, how company would consider it for the financial statements prepared for the balance sheet date?	14
Q 13	The board of directors approve the financial statements. Subsequent to their approval the shareholders approve the financial statements. For the identification of subsequent events, whether date of board of directors approval of financial statements or shareholders approval of financial statements should be taken as the 'date on which the financial statements were authorised for issue'?	14
Q 14	In recent months global stock markets as well as Pakistan stock market has shown significant volatility. More specifically in March 2020 all leading markets declined significantly. Would the decline in the market value of a share, subsequent to the balance sheet date, result in the adjustment of the financial statements?	15
Q 15	How companies are disclosing COVID-19 related events (as subsequent events) in the financial statements?	15

Financial Reporting Implications – *Your questions answered*

	Page #
Property, plant and equipment	
Q 16 As a result of COVID-19 related events and conditions, what would be the considerations of a company for assessing recoverability of carrying values of property, plant and equipment?	18
Q 17 COVID-19 related events and conditions (such as travel restrictions, closure of borders) have adversely impacted the economic activity. Companies might have completely closed or partially closed their operations and production facilities. In this scenario should a company cease to depreciate the plant/production facility and other assets?	19
Inventories	
Q 18 Considering the adverse impacts of COVID-19 related events on businesses, what should be the key considerations of a company while estimating net realizable value (NRV) of the inventory?	20
Q 19 As a result of lockdown measures, a company might not been able to deliver/ship the inventory items to its customers by March 31, 2020. What could be the implications of this scenario on March 31, 2020 financial statements?	20
Q 20 COVID-19 might adversely impact company's sales volume. Sales could be significantly reduced or suspended for an extended period subsequent to the balance sheet date. How this sale decline could impact measurement of inventory at the balance sheet date?	21
Q 21 Due to closure/curtailment of operations, the production of inventory might decrease significantly. This could result in a prolonged shut-down or idle capacity of the production facility. How prolonged shut-down or idle capacity could impact the inventory costing?	21
Provisions and liabilities	
Q 22 The lockdown measures might result in complete or partial closure of operations of a company. These circumstances could also impact company's contractual arrangements. While preparing its financial statements, how implications of these circumstances should be considered?	22
Q 23 A company could be required to account for an un-avoidable liability or a loss making contract? How a loss making contract (i.e. an onerous contract) is identified and accounted for under IAS 37?	23
Q 24 The company has obtained office space on a five year lease term, ending in 2022. Lease agreement includes monthly lease payments and early termination penalties. Due to COVID-19, company may consider terminating the lease agreement in 2020. How this arrangement would be accounted for under IAS 37?	24
Q 25 A company might exercise its termination right, under the contract. Further, there is no penalty for exercising the termination right. In terms of IAS 37, whether there would be financial obligation(s) on the company if it exercises its termination right?	25
Q 26 Due to COVID-19 related events and circumstances, a company might plan or start a restructuring plan. What would be the key considerations for accounting and disclosure of the restructuring provisions?	25
Q 27 A company might announce its restructuring plans after the reporting date. In this scenario what would be the major considerations for financial reporting at the reporting date?	27

Financial Reporting Implications – *Your questions answered*

	Page #
Provisions and liabilities	
Q 28 A company through an announcement may decide to redesign its existing plant or transfer a plant from one location to another. Would this lead to a restructuring provision?	27
Q 29 A company might expect to receive reimbursements from third parties (e.g. insurance claim reimbursement) against the provision. What is the IFRS guidance for reimbursements?	27
Q 30 Should a company in anticipation of future operating losses, record these in current reporting period?	27
Leases	
Q 31 Due to financial constraints and reduced business activity, a company (as lessees) might be granted lease rental concession under an existing lease agreement. How lease concessions should be accounted for under IFRS 16?	28
Q 32 Would the company need to consider the recoverability of a leased (i.e. right of use asset)?	28
Q 33 How lease term could be impacted due to changes in lease assessment or exercise of termination right options?	29
Q 34 Recently the discount rate has been decreased. What could be the implications of this decrease on the measurement of its lease liabilities under IFRS 16?	29
Financial instruments	
Q 35 What should companies consider in developing their estimate of expected credit losses?	30
Q 36 In current environment, companies may renegotiate the terms of their existing financing arrangements. How restructuring or amendment of a loan agreement would be accounted for under IFRS 9?	30
Q 37 Should a company adjust or disregard the quoted price in a period of significant market volatility when determining the fair value of traded equity investment?	31
Q 38 The company under bank overdraft facility might have a overdrawn balance at the reporting date. How this overdrawn balance would be reflected in the financial statements?	31
Q 39 How should a company account for the interest free loans / below-market interest loans obtained from the parent company, directors or sponsors?	32
Q 40 A company might have breached loan covenant(s). How breaches of loan covenants could impact the classification as current and non-current?	33
Assets held for sale	
Q 41 Company might plan to dispose of items of property, plant and equipment within next 12 months. How these assets would be disclosed in the financial statements?	34
Q 42 What are the specific financial statements presentation requirements for discontinued operations?	34

Financial Reporting Implications – *Your questions answered*

	Page #
Revenue	
Q 43 What is the enforceability criteria of a revenue contract and why it would require special consideration in COVID-19 impacted business environment?	35
Q 44 Due to COVID-19 related events, a customer might face difficulty in paying for goods or services. What could be the impact on company's revenue recognition due to customer's inability to make payments for goods or services?	35
Q 45 As a result of lockdown measures a company might not be able to deliver/ship goods to its customers. In such a case how revenue recognition could be impacted?	36
Q 46 In current business environment, a company might offer incentives to its customers. What would be the affect of changes in a revenue contract relating to future concessions (such as reducing the price or decreasing quantities of goods or services to be delivered (or minimum purchase commitments)?	37
Q 47 Due to financial difficulty, a company might allow extended payment terms to customers. How the extended payment terms could result in significant financing component under IFRS 15?	37
Employee benefits	
Q 48 COVID-19 related events might significantly impact company's workforce and operations. Resultantly, it may decide to lay-off employees or negotiate salary reductions. How the company would account for these changes?	38
Q 49 What would be the accounting requirements of a termination scheme that is expected to be settled in more than 12 months after the reporting date?	39
Q 50 How should a company account for the recent decrease in the discount rate, while measuring its employee benefit liabilities under IAS 19?	39
Borrowing costs	
Q 51 Company might stop its operations and activities, owing to lockdown measures or liquidity crunch. How closure of operations and activities could impact the capitalisation of borrowing costs?	40
Income taxes	
Q 52 COVID-19 might adversely impact future profitability of companies. How these adverse conditions may impact recognition and realisability of deferred tax assets?	41
Q 53 How should a company account for deferred tax assets in the financial statements for the year ended December 2019, where events after COVID-19 outbreak indicate that the deferred tax is no longer considered to be recoverable?	41
Q 54 Government may provide relief from COVID-19 through changes in tax legislation. How a company would account for the impact of changes in tax legislation, if legislation is enacted after the balance sheet date?	42
Government grants	
Q 55 How different forms of government assistance should be recorded?	43

Financial Reporting Implications – *Your questions answered*

Page

Presentation and disclosures

- | | | |
|------|---|----|
| Q 56 | Due to COVID-19, company may have recorded expenses or provisions of material amounts, impacting current year's profitability. In view of the materiality and non-recurring nature of these expenses/provisions, can a company present these amounts, separately as extraordinary items in the statement of profit or loss? | 44 |
| Q 57 | Companies could be required to make or update significant estimates based on the new and evolving information and circumstances. What could be the impact of these changes on the financial statement disclosures? | 44 |

Interim financial reporting

- | | | |
|------|--|----|
| Q 58 | What are key considerations for interim financial reporting? | 45 |
|------|--|----|

The background of the entire page is a blue-tinted photograph of stadium seating. The seats are arranged in rows, and the perspective is from a low angle, looking up towards the back of the stadium. The lighting is soft, and the overall color palette is a monochromatic blue.

Introduction

Introduction

First reported at the close of 2019, in less than four months the COVID-19 pandemic has spread to 190 countries.

Many countries have responded to this health crisis by taking drastic measures, ranging from border closures, domestic and international travel restrictions, ending mass gatherings, closing public spaces and schools, while in some places curfew has been imposed with people ordered to stay indoors.

Besides noticeable social effects of COVID-19, the economic and financial costs are also significant. Businesses are either partially or completely closed, resultantly the earnings are declining and unemployment levels are increasing. The global financial markets are exhibiting uncertainty and volatility (Most notably, in March 2020 all global stock markets, including Pakistan stock market showed significant decline) and the prices of oil and other commodities have dropped dramatically 2020.

The economic impact of the COVID-19 is likely to continue for some time, however, at present, the magnitude and extent of the fallout is uncertain.

The governments, central banks and corporate regulators are responding to the adverse economic impacts through various interventions and initiatives, ranging from financial stimulus packages, policy adjustments and regulatory reliefs.

In Pakistan, the lockdown measures of Federal and Provincial Governments to stop the spread of COVID-19 have impacted all segments of the society. Companies from all sectors and scales are adversely impacted, though the magnitude and complexity of this impact would vary mainly due to nature of operations, diversification and geography of customers and suppliers, effectiveness of COVID-19 mitigating measures and duration and extent of the lockdown measures.

The COVID-19 related conditions, in general, are expected to cause cashflows problems, financing constraints, supply chain disruptions, consumer demand decline, investment deteriorations, under-utilization of assets, legal and contractual non-compliances and unavailability of human resources. In certain cases, the adverse conditions would trigger existential concerns for companies.

Further, the uncertainties and risks associated with pandemic are demanding a reconsideration of earlier planned activities and policies, such as, expansion plans, investment portfolios and dividend payout policies.

In 2020 (and onwards) a key consideration of companies for surviving and sailing through the difficult times would be generation and conservation of liquidity.

The pervasive and disruptive impact of this health crisis, therefore effects the operations, earnings, financial strength and cashflows of all businesses, while in certain cases it will raise questions about continued operations of companies.

COVID-19 will impact many areas of accounting and reporting for all industries, requiring specific accounting and disclosures in the financial statements. The preparers of financial statements, audit committees, board of directors, auditors and other stakeholders need not only focus on identifying, understanding and analyzing COVID-19 implications on financial reporting, but also need to respond to the challenging accounting issues while preparing annual and interim financial statements.

Some of the key accounting and reporting considerations while preparing financial statements in the COVID-19 circumstances include:

Whether company is a going concern (i.e. has sufficient liquidity and other resources to continue operations for next twelve months)

Whether the subsequent events require adjustment or disclosures in the financial statements

Whether the carrying values of property, plant and equipment are recoverable

Whether the deferred tax assets are realisable and income tax related changes are appropriately accounted

Whether revenue is correctly recognised in the reporting period, in line with the latest information and contract modifications

Whether accounting and classification of loans is in accordance with the financing arrangements and commercial terms

Whether provisions, employee benefits, lease obligations and other items are measured based on the latest information and contractual terms

The background of the slide is a close-up, blue-tinted photograph of a typewriter keyboard. The keys are visible in rows, with some showing signs of wear. The lighting is soft, creating a professional and slightly nostalgic feel.

Financial Reporting Implications - *Your questions answered*

Going concern

Question 1

In the COVID-19 impacted environment, why assessment about company's ability to continue as a going concern would be a key focus area for the preparers of financial statements?

Companies prepare their financial statements on going concern basis, presuming that their operations will continue for the foreseeable future.

Despite this presumption, an assessment of going concern is integral to the preparation of financial statements. IAS 1, *Presentation of Financial Statements*, specifically requires that appropriateness of the going concern basis of preparation is considered at each balance sheet date.

COVID-19 has brought in significant uncertainties, market volatility and business disruptions. In consideration of the prevailing economic conditions, some of the factors necessitating heightened focus of going concern assessment include considerations about:

- Adverse current liquidity position and possible difficulty in meeting obligations as they become due.
- Lenders' unwillingness to provide or extend support to the company, and the implications for company of the conditions imposed by lenders for the continuing support.
- Concerns about capacity and solvency of company's strategic suppliers and customers.
- Significant workforce disruptions and related implications on operations.
- Difficulty of making fair value estimates of the value of assets and liabilities when the market for those assets has evaporated.

Companies will need to consider the effects of the COVID-19 on their ability to continue after the balance sheet date.

For the financial reporting, IAS 1 addresses the requirement of preparation of financial statements on a going concern basis. However, IAS 1 (paragraph 25) also explains that departure from the going concern basis is required when specified circumstances exist.

In accordance with IAS 1, these circumstances may arise due to (either):

- Management's intention to liquidate the company.
- Management's intention to cease trading.
- No realistic alternative than to cease trading or liquidate, despite management's intention to carry on the business of company.

The implications of COVID-19 may result in the above specified circumstances, resultantly making the company a non-going concern. With regard to the financial reporting, such a company would be required to prepare financial statements on a non-going concern basis.

Even if company's liquidation or ceasing of trading is not imminent, there may be conditions or events that raise material uncertainties about company's ability to continue as a going concern.

In prevailing environment of economic uncertainty along-with increased pressure on liquidity, pricing and asset valuations, more companies and their management will find that the amount of time required to make the going concern assessment will significantly increase. Management would be required to consider all available information for updating the previously prepared business plans, forecast and projections to account for the consequences of COVID-19 on company's operations and finances.

Question 2
What is the explanation of terms ‘liquidation’ and ‘cease trading’?

IFRS explains non-going concern in terms of liquidation of company or ceasing of trading.

Liquidation is not defined in IFRS. In the US GAAP liquidation is explained as the process by which a company converts its assets to cash or other assets and settles its obligations with creditors in anticipation of the company ceasing all activities. Upon cessation of the company’s activities, any remaining cash or other assets are distributed to the company’s investors or other claimants (albeit sometimes indirectly). It also explains that liquidation may be compulsory or voluntary. Dissolution of a company as a result of that company being acquired by another company or merged into another company in its entirety and with the expectation of continuing its business does not qualify as liquidation.

IAS 1 (paragraph 25) and IAS 10 (paragraph 14) use the phrase ‘cease trading’. This phrase is used in the sense of a company which is no longer involved in the activity of buying and selling goods and services. It should not be confused with a situation where a company which is listed on a stock exchange has its shares suspended from trading.

Question 3
In present environment, what would be the key considerations for management while assessing company’s ability to continue as a going concern?

IAS 1 requires that management must make an assessment of a company’s ability to continue as a going concern at each annual and interim balance sheet date. For this assessment management evaluates whether there are conditions or events, considered in the aggregate, that create uncertainty about company’s ability to continue as a going concern.

The key points for management consideration are:

Frequency of assessment	In context of statutory financial statements company’s management should evaluate whether there are material uncertainties in connection with preparing financial statements for each annual and interim reporting period.
Period of assessment	<p>The assessment period is at least one year from the financial statement date (balance sheet date) with no upper time limit. Therefore, a March 2020 year end company should atleast assess its going concern ability till March 2021.</p> <p>It also implies that company is not obligated to assess its ability to meet obligations as they become due beyond one year of the balance sheet date. However, the company is not prohibited from considering and providing disclosure about the potential effect of known conditions and events that may occur beyond one year.</p>
Information subject to assessment	Management’s evaluation should be based on all available information about the future that is known and reasonably knowable at the date that the financial statements are issued. Reasonably knowable implies that management should make a reasonable effort to identify conditions and events that it may not readily know, but would be able to identify without undue cost and effort.
Subsequent events	<p>The events after the balance sheet date may provide information about company’s ability or inability to continue as a going concern. IAS 10 (paragraph 14) states that a company shall not prepare its financial statements on a going concern basis if management determines after the reporting period date, either that it intends to liquidate the company or to cease trading, or that it has no realistic alternative but to do so.</p> <p>Due to prevailing uncertainty and the fast evolving nature of the COVID-19 situation, the consideration of subsequent period information requires careful consideration.</p>

Detail of management's assessment	<p>Management's evaluation may vary depending on company's specific facts and circumstances. For example, a detailed analysis may not be necessary if company has a history of profitable operations, ready access to financial resources, and no significant near-term obligations in excess of its available liquid funds.</p> <p>However, consequences of COVID-19 would now warrant companies to consider all events or conditions, potentially negative consequences for their ability to continue as a going concern.</p> <p>The initial assessment (before consideration of management's plans) will require company to consider, among other things:</p> <ul style="list-style-type: none"> ▪ The extent of operational disruption; ▪ Potential diminished demand for products or services; ▪ Contractual obligations due or anticipated within one year; ▪ Potential liquidity and working capital shortfalls; and ▪ Access to existing sources of capital (e.g., available line of credit).
Consideration of management plans	<p>The focus of management plans would vary from one company to another. In addition to planning to resume operations, management plans would mainly involve improving liquidity position by:</p> <ul style="list-style-type: none"> ▪ Renegotiating and refinancing of debt ▪ Arranging new funding ▪ Complying with lending covenants <p>The mitigating effect of management's plans shall be considered in evaluating whether the material uncertainties are alleviated only to the extent that information available at the date on which the financial statements are issued indicates both of the following:</p> <ul style="list-style-type: none"> ▪ It is probable that management's plans would be effectively implemented within one year after the balance sheet date; and ▪ It is probable that management's plans, when implemented, would mitigate the relevant conditions or events that create material uncertainties about company's ability to continue as a going concern within one year after the balance sheet date.
Alleviation of material uncertainties	<p>Where management identifies conditions or events that raise doubt about company's ability to continue as a going concern, management should consider whether its plans that are intended to mitigate those relevant conditions or events will alleviate the material uncertainties related to going concern.</p>

Question 4

For the going concern assessment, whether the events after the balance sheet would be adjusting events or non-adjusting events?

IAS 10, *Events after the Reporting Period*, defines adjusting and non-adjusting events. IAS 10 (paragraph 14) explains that for going concern assessment all events and conditions before as well as after the reporting date (till the issuance of financial statements) should be considered.

Management would be required to consider information available after the balance sheet date and include it for developing plans and assessing company's ability to continue as a going concern. The going concern assessment is for at least 12 months after the balance sheet date, therefore, all events and conditions that are reasonably known till the date of issue of financial statements are considered in making an appropriate assessment.

Question 5

How management's assessment of going concern could impact company's financial statements?

Management's evaluation of company's ability to continue as a going concern may result in the following scenarios:

- No material uncertainties related to going concern exist;
- No material uncertainties exist but 'close call' situation exists;
- Material uncertainties exist, however, these would be mitigated by management plans; or
- Material uncertainties exist, and management plans would not be able to mitigate those uncertainties.

The impact on these scenarios on the accounting and disclosures of the financial statements would be as under:

Assessment about company's ability	Basis of preparation and disclosure/s	How going concern assessment would impact the financial statements
No material uncertainties exist	Going concern basis <i>Financial statements would be prepared under the going concern basis of accounting</i>	IFRS do not outline a specific disclosure about going concern assessment and basis of preparation.
No material uncertainties exist but 'close call' situation exists	Going concern basis with disclosures about significant judgments <ul style="list-style-type: none"> ▪ <i>Financial statements would be prepared under the going concern basis of accounting</i> ▪ <i>Disclosure of judgments made by management in context of 'close call' situation provided in the notes to the financial statements</i> 	The 'close call' situations could arise when there are significant doubts on company's ability to continue as a going concern but, based on the management plans and judgment there are no material uncertainties. IAS 1 (paragraph 122) requires disclosures of areas involving significant management judgments. The close call situations would involve significant judgment requiring disclosures in the financial statements.

Assessment about company's ability	Basis of preparation and disclosure/s	How going concern assessment would impact the financial statements
Material uncertainties exist, however, these would be mitigated by management plans	<p>Going concern basis with additional disclosure</p> <ul style="list-style-type: none"> ▪ <i>Financial statements should continue to be prepared under the going concern basis of accounting</i> ▪ <i>Disclosure of uncertainties that are casting doubt on company's ability to continue as going concern</i> 	<p>Under IAS 1 (paragraph 25), If conditions or events raise doubt about a company's ability to continue as a going concern, but the material uncertainties are alleviated as a result of consideration of management's plans, the company should disclose information that enables users of the financial statements to understand all of the following:</p> <ul style="list-style-type: none"> ▪ Principal conditions or events that raised substantial doubt about the company's ability to continue as a going concern (before consideration of management's plans); ▪ Management's evaluation of the significance of those conditions or events in relation to the company's ability to meet its obligations; and ▪ Management's plans that alleviated substantial doubt about the company's ability to continue as a going concern. <p>This should give financial statement users the opportunity to evaluate the likely success of those plans in mitigating the conditions or events that raised substantial doubt about going concern basis.</p>
Material uncertainties exist, and management plans would not be able to mitigate those uncertainties	<p>Other than going concern basis of accounting (i.e. Non-going concern basis) with additional disclosure</p> <p>Financial statements should not be prepared under the going concern basis of accounting</p> <p>Disclosure of basis of preparation and uncertainties that resulted in company's inability to continue as going concern.</p>	<p>IAS 1 (paragraph 25) suggests that departure from the going concern basis is required, when conditions or events create such material uncertainties that management has no other option than to liquidate the company or cease trading.</p> <p>IAS 1 requires that when a company does not prepare its financial statements on a going concern basis.</p> <ul style="list-style-type: none"> ▪ Disclose the fact that the financial statements have not been prepared on going concern basis; ▪ Disclose the basis of preparation used; and ▪ Reasons why company is not considered as a going concern (Principal conditions or events that raise substantial doubt about the company's ability to continue as a going concern and management's evaluation of the significance of those conditions or events in relation to the company's ability). <p>Regarding other basis of preparing financial statements, neither IAS 1 nor IAS 10 provide any details however, of any alternative basis and how it might differ from the going concern basis.</p>

Question 6

Management may determine that company would not be able continue its operations for next 12 months. In such a case, how financial statements on a non-going concern basis would be prepared?

Under the Companies Act, 2017, companies are required to prepare financial statements in accordance with accounting and reporting standards as applicable in Pakistan. These standards include:

- IFRS issued by IASB / IFRS notified by SECP
- IFRS for Small and Medium-sized Entities (IFRS for SMEs)
- Revised Accounting and Financial Reporting Standard for Small-sized Entities (AFRS for SSEs)

However, these standards do not outline specific explanation about recognition and measurement of assets, liabilities, equity, income and expense of a non-going concern company.

As explained above, IAS 1 requires companies to prepare financial statements with non-going concern basis. However, IFRS do not provide specific guidance for preparing financial statements on a non-going concern basis.

The Institute, through Circular 3 of 2017 (dated February 07, 2017) has issued ***Guideline on the basis of Preparation of Financial Statements of Companies that are not Considered Going Concern.***

The objective of issuing this Accounting Guideline was to assist preparers and other stakeholders in preparing the statutory financial statements of the companies that are not regarded as going concern. This Accounting Guideline sets out the principle of recognition and measurement of the elements of financial statements, provides guidance on the preparation of the financial statements of dormant companies, and outlines minimum disclosure and presentation requirements.

The guidance for preparing financial statements of a non-going concern company is as under

Basis of preparation

Financial statements should be prepared on the IFRS basis. Accordingly, the recognition, measurement and disclosure requirements of IFRS shall be followed.

Statement of compliance

In the financial statements, give an explicit statement of compliance with approved accounting and reporting standards as applicable in Pakistan.

Accounting policies

The accounting policies of prior year should be considered, incorporating necessary revisions to explain application of measurement and recognition of reporting date amounts.

Using IFRS framework, the assets, liabilities, income and expenses shall be re-measured to reflect the fact that the 'going concern' assumption is not appropriate.

This will generally involve writing assets down to their recoverable amount based on conditions existing at the end of the reporting period and providing for contractual commitments which may have become onerous as a consequence of the decision to liquidate the company or to cease trading.

Revision of accounting estimates

The estimates relating to recoverability and reliability may require revision. For example, the recoverability of property, plant and equipment would be assessed under IAS 36, *Impairment of Assets*. Potentially resulting in the recognition of impairment to the carrying value of property, plant and equipment.

Similarly the application of other IFRS for measurement of assets and liabilities would provide accounting information in consideration of company's inability to continue in next 12 months.

Under previous accounting policies, the assets may be revalued (such as property, plant and equipment) or remeasured at fair value (such as equity investments).

Upward adjustments

Upward adjustments for writing-up the carrying value of assets shall not be made. A number of IFRS would not permit such a write-up as their requirements restrict the amount to be recognised for an asset to the lower of cost or depreciated cost and net realisable value/fair value less costs to sell. These include IAS 2, *Inventories*, the cost model under IAS 16, *Property, Plant and Equipment* and IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*.

Non-recognition previously un-recognised assets

A company may have items that it plans to sell, that the company may not have previously recognized, such as trademarks or patents. A company applying the non-going concern basis of accounting should not recognize those items in the financial statements. However, such a company is required to disclose those items at the amount of expected sale proceeds.

Anticipated/ expected profit

The expected profit on the intended disposal of assets should not be recognised, either as a reduction in the impairment loss or provisions or as uplifts in the carrying value of the relevant assets.

A loss on disposal in the subsequent period reflects the decision to hold them rather than to sell them at the end of the reporting period. For similar reasons, it would not be appropriate to make provision for future losses or liabilities for which there was no commitment at the end of the reporting period.

Inventory sale

Gain on sale of inventory or other items should not be recognised until actual sale.

Provisions

Certain contracts may be regarded as onerous, requiring a provision. Contractual commitments may become onerous because of a decision to cease trading or to liquidate a business.

Provisions should not be made in respect of executory contracts (unless onerous) or restructuring costs that do not qualify as obligations under IFRS e.g. IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* (or other applicable approved accounting standard at the balance sheet date).

In accordance with IAS 37, it would generally not be appropriate to make a provision for future losses or liabilities for which a commitment did not exist at the end of the reporting period.

Cumulative adjustment

A company reporting on the non-going concern basis of accounting as of the effective date should record a cumulative-effect adjustment as of the date of adoption to account for any differences between the company's recognized assets and the measurements of its assets and liabilities (including measurement changes resulting from changes in assumptions).

Remeasurement

Subsequently, at each reporting date the company should re-measure its assets and liabilities to reflect change in value since the previous reporting date.

Classification of current and non-current

Under the principles of IAS 1 assets classified as non-current should not be reclassified as current assets unless and until they meet the 'held for sale' criteria of IFRS 5.

Long term liabilities should be reclassified as current liabilities if they meet the requirements of IAS 1, to be presented as current liabilities. For example a long-term debt may become current at the reporting date, due to breach of loan covenants. The breach should exist at the end of the reporting period (subsequent to the reporting date breaches are non-adjusting event) unless and until they meet the 'held for sale' criteria in IFRS 5. However, noncurrent liabilities may have to be reclassified as current liabilities because of breaches of borrowing covenants and similar factors which existed at the end of the reporting period.

Disclosure

In some situations, the effect on the statement of financial position of ceasing to regard the business as a going concern may be negligible. Nevertheless, accounting standards as applicable in Pakistan require the financial statements to disclose that the company is no longer regarded as a going concern.

Unless there is a statement to the contrary, these standards allow a reader to presume that a company is carrying on business as a going concern. Consequently, where necessary, the company should state that it has prepared its financial statements on a non-going concern basis, even if the effect of doing so has not been significant.

IAS 1 requires that when a company does not prepare its financial statements on a going concern basis.

At a minimum, a company should disclose all of the following when it prepares financial statements using the non-going concern basis of accounting:

- That the financial statements are prepared using the non-going concern basis of accounting, including the facts and circumstances surrounding the adoption of the non-going concern basis of accounting.
- The basis of preparation used, including methods and significant assumptions used to measure assets and liabilities, including any subsequent changes to those methods and assumptions.
- Should present an analysis of any upside not recognised in the profit or loss on assets during the period.
- Should also present an analysis of any items (such as trademark) that are not recognised in balance sheet during the period using a classification based on either their nature or their function within the company, whichever provides information that is reliable and more relevant.

Question 7

Due to the adverse impacts of COVID-19, management may decide to make the company dormant. How financial statements of a dormant company would be prepared?

There may be situation where a company ceases to trade during the year but which management intends to keep in existence as a dormant company.

To provide clarity to users of the financial statements, and to avoid the risk of giving a misleading impression regarding the trading status of the company, the financial statements should be prepared on a basis other than of a going concern as explained above, until such time as the only amounts reported in the current and prior year profit and loss account and financial position relate to the company's ongoing existence (i.e. any effects of ceasing to trade have been 'washed through'). Thereafter, the financial statements will no longer include any items relating to the trade that has ceased and, therefore, references to such cessation will be confusing. Instead the financial statements should be prepared on a going concern basis.

Question 8

How the non-going concern assessment of a subsidiary could impact its separate financial statements and group's consolidated financial statements?

The determination of going concern should be made for each reporting company. In many cases, a going concern basis may not be considered appropriate for an individual subsidiary, while the going concern basis may remain appropriate for the subsidiary's parent and for the group as a whole. Irrespective of the basis of accounting applied by a subsidiary, the going concern principles of approved accounting standards are applied in the group's consolidated financial statements if the group itself is a going concern. This might result in recognition and measurement differences between the consolidated financial statements and the subsidiary's individual financial statements.

Events after the reporting date

Question 9

COVID-19 related events and conditions are expected to continuously develop and evolve. How company would evaluate whether COVID-19 related events are adjusting events or non-adjusting events?

IAS 10 requires companies to identify events that happen after the reporting date till the date of issuance of financial statements. These events termed as subsequent events may require adjustment or disclosure in the reporting period financial statements.

The adjustment to the financial statement amounts is required for adjusting events. Those events that provide evidence of conditions that existed at the reporting date. While non-adjusting events indicate conditions that arose after the reporting date. Financial statement amounts are not adjusted for non-adjusting events.

However, in accordance with IAS 10 (paragraph 14), a condition that arose after the reporting date may indicate that company is not a going concern. This would require preparation of financial statements on a non-going concern basis with necessary adjustments to the financial statement amounts to reflect that company is not a going concern.

With regard to COVID-19 and its implications, companies would need to evaluate whether the events related to COVID-19 represent subsequent events. This evaluation may require companies to:

- Adjust the amounts recognised in their financial statements to reflect any adjusting events that occur during the subsequent events period.
- Adjust the financial statements to reflect that company is not a going concern due to the material uncertainties.
- Provide disclosure in their financial statements to reflect any non-adjusting events that occur during the subsequent events period.

The impact of COVID-19 related events would vary for different reporting periods.

Financial statements for the year/period ended December 31, 2019 (or prior)

It is widely accepted that on December 31, 2019 a limited number of cases of an unknown virus had been reported to the World Health Organization. There was no explicit evidence of human-to-human transmission at that date. The subsequent spread of the virus and its identification as a new coronavirus does not provide additional evidence about the situation at December 31, 2019 and generally would be a non-adjusting event.

Financial statements for the year/period ended March 31, 2020

For March 31, 2020 year/period ended financial statements, any accounting impact of the COVID-19 would likely be recognized. The amounts would be recognised as:

- Reporting period adjustments: If relate to transactions or events before March 31, 2020.
- Subsequent period adjustments: If relate to adjusting events after March 31, 2020.

Financial statements for the year/period ending June 30, 2020

For June 30, 2020 and later year/period ending financial statements any accounting impact of the COVID-19 would likely be recognized.

Question 10

A company with December 31, 2019 reporting date (or earlier periods) might not have issued its financial statements. In such a case, how COVID-19 related events would be considered for the determination of subsequent events?

As noted above, the spread of the COVID-19 does not provide additional evidence about the situation at December 31, 2019. The WHO declaration of COVID-19 as a pandemic in March 2020, and actions taken by governments and the private sector to respond to the outbreak also followed after December 31, 2019.

Generally, the consequences of COVID-19 would be non-adjusting event(s) for December 31, 2019 year ended companies. Therefore, based on information about the outbreak that was reasonably available as at December 31, 2019, it is likely that market participants would have made either no adjustments to their assumptions, or only inconsequential changes, based on their assessments of the available information and associated risks as at that date.

Impact on financial statements

Companies whose financial statements have been authorised for issue before March 11, 2020, the COVID-19 related events would require no further consideration.

Companies whose financial statements for current or prior years are yet to be issued may require adjustment or disclosure of COVID-19 related events. Generally, the financial reporting impacts would likely be limited to disclosures of non-adjusting events in the financial statements. For example, companies may experience losses due to supply chain issues or volatility in commodities markets that should be disclosed.

Companies may need to make additional disclosures to describe the impacts of the outbreak in the subsequent event period. Generally, disclosure should be made of those events during the subsequent events period that do not relate to conditions that existed at the date of the financial statements but cause significant changes to assets or liabilities in the subsequent period and either will, or may, have a significant effect on the future operations of the company.

In accordance with IAS 10 (paragraph 21) for material non-adjusting events, a company must disclose:

- (a) a description of the nature of the event; and
- (b) an estimate of the financial effect, or a statement that such an estimate cannot be made.

Examples of non-adjusting events that would generally result in disclosure include:

- Management's plans to deal with the effects of the COVID-19 outbreak and whether there is material uncertainty over the company's ability to continue as a going concern;
- Breaches of covenants, waivers or modifications of contractual terms in lending arrangements;
- Supply chain disruptions;
- The assessment of certain purchase or sale agreements as onerous contracts;
- Announcing a plan to discontinue an operation;
- Announcing, or commencing the implementation of, a major restructuring or downsizing (temporarily or permanently);
- Declines in the fair value of investments held after the reporting period (e.g., pension plan investments);
- Abnormally large changes in asset prices or foreign exchange rates; and
- Entering into significant commitments or contingencies, such as issuing significant guarantees to related parties.

Furthermore, in accordance with IAS 10 (paragraph 14) company should be taking into account assessment of going concern and adjust the financial statements as appropriate.

While non-adjusting, the COVID-19 related events may have financial statements implications for companies whose December 31, 2019 financial statements have not yet been issued.

For those companies though impacts of COVID-19 are non-adjusting event, however, the events and conditions after the reporting date sometimes provide additional information about the uncertainties that existed at the reporting date and they may impact financial reporting issues including:

- Going concern
- Fair value measurement
- Expected credit loss assessment
- Assets impairment
- Other financial statement disclosure requirements
- Other accounting estimates

For example: A company with December 31, 2019 year end has not issued its financial statements. The COVID-19 related events including restrictions on mobility and closure of operations in the months of March and April, may indicate that company is not a going concern. Financial statements for December 31, 2019 would be prepared on non-going concern basis.

Adjusting events

While for December 31, 2019 year ended financials statements, mostly COVID-19 related events would be non-adjusting. However, there may be conditions existing before December 31 that are further impacted by the outbreak, such that recognition in the financial statements for the year ended December 31, 2019 may be required.

For example, a customer's bankruptcy after the reporting date is often the culmination of a sequence of events that started before that date. In this scenario, receipt of information about the bankruptcy may be a recognized subsequent event.

Question 11

What would be the impact of COVID-19 related events on companies with March 31, 2020 (or later) year end?

The WHO declared the outbreak COVID-19 as a pandemic on March 11, 2020. International governments as well as government of Pakistan took measures to contain spread of COVID-19. These measures have generally affected companies workforce, customers, investors and business operations. Further, COVID-19 at macro level has had an adverse impact on the Pakistan and global economy.

In these circumstances for companies with March 31, 2020 balance sheet date, events and conditions may provide information about losses, liquidity and solvency concerns and breaches of contracts.

For reporting periods after December 31, 2019, more information about COVID-19 would be available to management and users of financial statements. The substantial part of this information would relate to events and conditions after March 11, 2020. Therefore, it is likely to be a current-period event that will require ongoing evaluation to determine the extent to which developments after the respective reporting date should be recognised in that reporting period.

Management would need to use their judgement to determine the impact of COVID-19 on their company. Management evaluation would involve impact of COVID-19 on the company:

- Prior to the end of the balance sheet date - Reporting period adjustments
- After the reporting date - Subsequent events (Adjustments or disclosures)

The evaluation of events till the reporting period may require recognition and/or remeasurement of assets and liabilities. Where this judgement has a significant impact on the amounts in the financial statements, it should be disclosed in accordance with IAS 1.

However, companies may not be required to necessarily make adjustments or provide disclosures in the financial statements, as the scale and severity of impact would vary from one company to another.

Companies also need to carefully assess specific facts and circumstances to identify events that generally represent the culmination of a series of conditions that existed at or before the reporting date. When it is determined that COVID-19 was an event that existed and caused an impact to operations at or before the reporting date, events subsequent to the reporting date should be accounted for as adjusting events.

For example, a customer may not pay the due amounts in March 2020. Subsequent, bankruptcy of such a customer could indicate that it is an adjusting event. Similarly, company's inability to supply goods or services due to lockdown may result in a breach of contract with a customer. Subsequent events may provide further information about the consequences of the breach, may require adjustment (i.e. recording of penalties) in the financial statements.

Where non-adjusting events are identified, companies are required to disclose the nature of the event and an estimate of its financial effect, or a statement that an estimate cannot be made.

Question 12

Company might be having difficulty in meeting the terms of the long-term debt agreement. If refinancing, waiver or amendment to a long-term financing arrangement is agreed after the balance date sheet, how company would consider it for the financial statements prepared for the balance sheet date?

The classification of a long-term debt as current or non-current reflects circumstances at the reporting date. Fundamentally, the classification is based on the contractual arrangements enforceable at the balance sheet date.

The granting of a waiver or a period of grace changes the terms of the loan agreement.

In accordance with IAS 1, the restructuring, waivers, amendments to the long-term debt that are agreed after the reporting date are not considered in determining the classification of the debt. The changed loan terms owing to restructuring, waivers, amendments are entered into and enforceable after the balance sheet date. Further, refinancing/rescheduling a liability after balance sheet date does not impact company's solvency and liquidity at the balance sheet date. It is a non-adjusting event in accordance with IAS 10.

On the other hand, in accordance with IAS 1, if company expects, or has the discretion, at the reporting date to reschedule the payments on a long-term basis, then the long-term debt is classified as non-current.

Question 13

The board of directors approve the financial statements. Subsequent to their approval the shareholders approve the financial statements. For the identification of subsequent events, whether date of board of directors approval of financial statements or shareholders approval of financial statements should be taken as the 'date on which the financial statements were authorised for issue'?

Under the Companies Act, 2017, the board of directors approve the financial statements. Further, the members of the company approve these financial statements in the annual general meeting.

IAS 10 (paragraphs 5 and 6) explain that date on which the financial statements were authorised for issue mean the date on which management (i.e. Board of Directors under the Companies Act, 2017) authorise the issue of financial statements to the members of the company. The shareholders are required to approve the financial statements, however, the date on which the financial statements were authorised for issue is the approval date of board of directors.

Accordingly, subsequent events till the date of director's approval of financial statements are considered for disclosure and/or adjustment in the financial statements.

Question 14

In recent months global stock markets as well as Pakistan stock market has shown significant volatility. More specifically in March 2020 all leading markets declined significantly. Would the decline in the market value of a share, subsequent to the balance sheet date, result in the adjustment of the financial statements?

In accordance with IAS 10, company shall recognize in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements.

Further, IAS 10 outlines that company should not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date but before financial statements are issued.

IAS 10 (paragraph 22) provides examples of non-adjusting subsequent events, including changes in the fair value of assets or liabilities (financial or non-financial) after the balance sheet date but before financial statements are issued. In general, the movement in the share price, subsequent to the balance sheet date is a non-adjusting event.

Question 15

How companies are disclosing COVID-19 related events (as subsequent events) in the financial statements ?

Companies may need to evaluate whether the consequences of COVID-19 represent subsequent events. For year-end 2019 financial statements, any COVID-19 related subsequent events identified are likely to be non-adjusting subsequent events.

A review of some of the annual reports (including financial statements) filed by companies in United States (with Securities and Exchange Commission (SEC), US) indicates that companies are discussing the impact of COVID-19 in their annual reports and also providing disclosures about COVID-19 as a subsequent event.

Few examples, extracted from the annual and quarterly financial statements filed by companies with the SEC during the periods from March 15, 2020 to April 14, 2020 are provided below:

Chico FAS, Inc.**Financial statements for the year ended February 01, 2020**

(Form 10-K filed with SEC on March 16, 2020)

“Subsequent event

In recent days, the COVID-19 outbreak in the United States has resulted in reduced customer traffic and the temporary reduction of operating hours for our stores as well as temporary store closures where government mandated. These recent developments are expected to result in lower sales and gross margin than provided in our previous outlook.”

Performance Shipping Inc.**Financial statements for the year ended December 31, 2019**

(Form 10-K filed with SEC on March 31, 2020)

“Subsequent events

Covid-19 Outbreak: On March 11, 2020, the World Health Organization declared the 2019 Novel Coronavirus (the “Covid-19”) outbreak a pandemic. In response to the outbreak, many countries, ports and organizations, including those where the Company conducts a large part of its operations, have implemented measures to combat the outbreak, such as quarantines and travel restrictions. The Company’s financial and operating performance may be adversely affected by the recent coronavirus outbreak. Any prolonged restrictive measures in order to control the spread of Covid-19, or other adverse public health developments in Asia or in other geographies in which the Company’s vessels operate may significantly impact the demand for the Company’s vessels. The extent to which Covid-19 will impact the Company’s results of operations and financial condition will depend on future developments, which are highly uncertain and cannot be predicted, and accordingly, an estimate of the impact cannot be made at this time.”

Abercrombie Fitch & Co
Financial year ended February 01, 2020
 (Form 10-K filed with SEC on March 31, 2020)

“Subsequent events

COVID-19 has caused business disruption beginning in January 2020, with the closure of stores in China and the surrounding area, modified operating hours in certain stores that remained open, and a decline in traffic. In late February 2020, the situation escalated as the scope of COVID-19 worsened beyond the Asia-Pacific region, with Europe and the United States experiencing significant outbreaks. In March 2020, the COVID-19 outbreak was declared to be a global pandemic by the World Health Organization and the Company temporarily closed its Company-operated stores across brands in North America and Europe, effective beginning March 15, 2020 and March 16, 2020, respectively, and expects these stores to remain closed until further notice. The majority of the Company's stores in the Asia-Pacific region have reopened, although many with temporarily reduced operating hours. The Company plans to follow the guidance of local governments and health organizations to determine when it can reopen these stores and to evaluate whether further store closures in the Asia-Pacific region will be necessary. As the situation continues to evolve rapidly, the Company is not currently able to predict the timing of store reopenings, which may occur on a location-by-location basis. The Company's robust digital operations across brands remain open to serve the Company's customers during this unprecedented period of temporary store closures.

The Company has seen, and expects to continue to see material reductions in sales across brands and regions as a result of COVID-19. The Company could experience other material impacts as a result of COVID-19, including, but not limited to, charges from potential adjustments of the carrying amount of inventory, asset impairment charges, deferred tax valuation allowances and changes in the effectiveness of the Company's hedging instruments. The current circumstances are dynamic and the impacts of COVID-19 on the Company's business operations, including the duration and impact on overall customer demand, cannot be reasonably estimated at this time, although the Company anticipates COVID-19 will have a material adverse impact on its business, results of operations, financial condition and cash flows in Fiscal 2020. ”

Buenaventura Mining Company Inc.
Financial statements for year ended December 31, 2019
 (Form 20-F filed with SEC on April 10, 2020)

“Subsequent events

COVID-19 (Corona Virus Disease 2019)

Our operations are subject to risks related to outbreaks of infectious diseases. For example, the recent outbreak of coronavirus COVID-19, a virus causing potentially deadly respiratory tract infections originating in China, has already and will continue to negatively cause further volatility in prices of precious metals. Additionally, a severe market disruption will likely entail decreased demand for our products and otherwise impact our operations and the operations of our customers, suppliers and other stakeholders. The Peruvian Government has issued a series of executive decrees declaring a national emergency and significantly restricting general circulation throughout the country.

In accordance with these restrictions and within the framework of the Company's pandemic response plan, we have limited our operations to those which are strictly necessary to ensure that our mine pumping systems, water treatment plants, energy supply, hydroelectric substations, health services and overall minimum safety conditions remain in place. Other than in respect of these minimum back-up operations, as of the date of this annual report, our mining processing facilities are completely halted. The company intends to immediately resume operations once it receives notice from the authorities that restrictions have been lifted. The ultimate severity of the Coronavirus outbreak is uncertain at this time and therefore we cannot predict the impact it may have on the world, the Peruvian economy, international financial markets, or ultimately on our financial condition, results of operations, production, sales, margins and cash flow from operations, our access to debt markets, covenants compliance, asset impairments, among others.”

Harvest Oil & Gas Corp.
Financial statements for year ended December 31, 2020
 (Form 10-K filed with SEC on April 14, 2020)

“Subsequent events

Harvest evaluated subsequent events for appropriate accounting and disclosure through the date these consolidated financial statements were issued.

On March 11, 2020, the World Health Organization recognized the novel strain of coronavirus ("COVID-19") as a global pandemic. This recent outbreak has adversely impacted global commercial activity, including the energy industry, and the industries in which several of the Company's customers operate. The impacts of the global emergence on the Company's business are currently unknown. In an effort to contain COVID-19 or slow its spread, governments around the world have also enacted various measures, including orders to close all businesses not deemed "essential," isolate residents to their homes or places of residence, and practice social distancing when engaging in essential activities.

The Company anticipates that these actions and the global health crisis caused by COVID-19 will negatively impact business activity across the globe. It is not clear what the potential effects any such alterations or modifications may have on the Company's business, including the effects on interactions with governmental agencies, customers, vendors and employees.

Due to the rapidly evolving developments regarding the pandemic, the Company's future results of operations, financial condition and cash flows may be impacted. However, the Company cannot reasonably estimate the ultimate impact of COVID-19."

National Rural Utilities Cooperative Finance Corporation
Financial statements for three months ended February 29, 2020
 (Form 10-Q filed with SEC on April 10, 2020)

“Subsequent events
COVID-19

On March 11, 2020, the World Health Organization declared COVID-19 a global pandemic and recommended containment and mitigation measures worldwide. On March 13, 2020, the United States declared a national emergency with respect to COVID-19. The effects of COVID-19 and the response to the virus have negatively impacted financial markets and overall economic conditions. We have been monitoring developments closely, and although our operations have not been materially affected by the COVID-19 outbreak to date, we are unable at this time to estimate the future impact of COVID-19 on our operations. The extent of the impact of COVID-19 on our operational and financial performance will depend on certain developments, including, among others, the duration and severity of the COVID-19 pandemic, the ultimate impact on our members, potential further disruption and deterioration in the corporate debt markets and additional, or extended, federal, state and local government orders and regulations that might be imposed in response to the pandemic, all of which are uncertain."

Schmitt Industries, Inc.
Financial statements for three months ended February 29, 2020
 (Form 10-Q filed with SEC on April 14, 2020)

“Subsequent events

In December 2019, a novel coronavirus disease ("COVID-19") was reported and in January 2020, the World Health Organization ("WHO") declared it a Public Health Emergency of International Concern. On February 28, 2020, the WHO raised its assessment of the COVID-19 threat from high to very high at a global level due to the continued increase in the number of cases and affected countries, and on March 11, 2020, the WHO characterized COVID-19 as a pandemic.

The broader implications of COVID-19 on our results of operations and overall financial performance remain uncertain. We may experience constrained supply or slowed customer demand that could materially adversely impact our business, results of operations and overall financial performance in future periods. See Risk Factors for further discussion of the possible impact of the COVID-19 pandemic on our business."

Property, plant and equipment

Question 16

As a result of COVID-19 related events and conditions, what would be the considerations of a company for assessing recoverability of carrying values of property, plant and equipment?

Recoverability of non-financial assets (such as property, plant and equipment, goodwill, intangibles) is checked to ensure that these assets are not carried in the financial statements at more than the highest amount to be recovered through their use or sale. Generally, recoverability of property, plant and equipment is based on use rather than sale.

IAS 36, *Impairment of Assets*, deals with the recoverability assessments (i.e. impairment testing) of the non-financial assets, including property, plant and equipment. In accordance with IAS 36, property, plant and equipment are tested for impairment when there are indicators of impairment (triggering events). IAS 36 (paragraph 12) lists the external and internal indicators of impairment. These indicators include:

- Macroeconomic conditions, such as a deterioration in general economic conditions.
- Industry and market considerations, such as a deterioration in the environment in which a company operates.
- A significant or unexpected decline in market value.
- Adverse changes in technology, markets, economy, or laws.
- Increases in market interest rates.
- Net assets of the company higher than market capitalization.
- Obsolescence or physical damage.
- Asset is idle, part of a restructuring or held for disposal.
- Worse economic performance than expected.

In case there are triggering events, company would perform an impairment testing involving:

- Calculation of asset's recoverable amount.
- Comparison of recoverable amount to carrying amount.
- Recording a write-down (i.e. impairment loss), if carrying amount exceeds recoverable amount.

Generally, in times of recession, there is an increased likelihood of triggering events, which are indications that an asset may be impaired. Therefore, previously, companies in the absence of triggering events might not have performed impairment testing.

In context of the COVID-19 related events, including the lockdowns have adversely affected operations and finances of companies, leading to decreased demand for product, supply chain disruptions and/or liquidity pressures. Companies would be impacted with varying degrees, most significantly those that:

- Have been hit by a fall in demand for their products or services, or by restrictions imposed by the state;
- Are dependent on supply chains or have production facilities in countries significantly affected by COVID-19; and/or
- Trade with countries significantly affected by COVID-19.

Temporarily ceasing operations or suffering an immediate decline in demand or prices and profitability are clearly events that might indicate impairment. However, the impact of reduced economic activity and lower revenues are likely to affect almost any company and might also indicate impairment.

For the financial reporting of post COVID-19 pandemic period ended/ing in 2020, it is likely that a triggering event has occurred for a significant number of companies. Therefore requiring an impairment test to determine the recoverability of property, plant and equipment.

Question 17

COVID-19 related events and conditions (such as travel restrictions, closure of borders) have adversely impacted the economic activity. Companies might have completely closed or partially closed their operations and production facilities. In this scenario should a company cease to depreciate the plant/production facility and other assets?

In accordance with IAS 16 (paragraph 55), depreciation of an asset begins when it is available for use and depreciation of an asset ceases at the earlier of when the asset is classified as held for sale or is when the asset is derecognized. Depreciation does not cease when the asset becomes idle, or is retired from active use, unless the asset is fully-depreciated.

Therefore, plants and production facilities that are temporarily shutdown or idle due to current lockdown and market conditions, should continue to be depreciated. However, where company applies a usage-based depreciation method, for example unit-of-production, then under such method no depreciation arises during a shut-down period because no units would be produced.

Further, company should also consider that if an asset or component of an asset remains idle for a significant period of time, it may indicate potential impairment or demonstrate the need to reassess the asset's useful life.

Inventories

Question 18

Considering the adverse impacts of COVID-19 related events on businesses, what should be the key considerations of a company while estimating net realizable value (NRV) of the inventory?

IAS 2, *Inventories*, requires that inventory items should be measured at the lower of their cost and net realizable value (NRV). NRV is the estimated selling price in the ordinary course of business less the estimated costs of completion and sale. NRV involves estimated selling price, which would be based on the intended use of inventory.

In accordance with IAS 2 (paragraph 34) any write down of inventories to NRV is recognised as an expense in the period in which the write-down occurs.

The consequences of COVID-19 might adversely affect the recoverability of inventories. The adverse consequences could include disruption in transportation arrangements and suppressed customer demand. The recoverability of inventory items from normal sale could be an issue, specially for companies holding perishable items or large quantities of inventories. Due to lockdown and uncertainty about the market conditions, company's inventory may require a write-down based on the NRV.

However, another implication of disruption of business due to COVID-19, may affect in estimating NRV, such as:

- Fluctuation in estimated selling prices due to changes in customer demand mainly for perishable goods or goods with short shelf lives.
- Change in estimated costs to complete due to increase in the cost of material or labour.
- Sales and purchase contracts may not be fulfilled resulting in excess inventory, in turn affecting NRV.

NRV write downs would generally be determined on an individual item basis. However, in certain cases it may be appropriate to evaluate similar products or groups. This could be the case for items of inventory for the same product line that have similar purpose or end use, are produced and marketed in similar geographical area and cannot be evaluated separately from other items in that product line.

Company in current scenario would be required to use judgment in estimating the net realisable value for inventory. This should reflect the latest expectations of selling prices and projected costs to complete after taking into account the impact of COVID-19. Further, the estimation of NRV should also take into consideration fluctuations in selling price or costs to sell, based on the evaluation of subsequent events.

Question 19

As a result of lockdown measures, a company might not been able to deliver/ship the inventory items to its customers by March 31, 2020. What could be the implications of this scenario on March 31, 2020 financial statements?

IAS 2 requires that inventory be measured at lower of cost or NRV, and the decline to be recognized as a charge in the period in which it occurs.

Companies would be required to consider all available information to consider and determine inventory write down. Company may have information within the reporting period or the information would become available after reporting date.

The situation may lead to multiple scenarios, and a careful consideration of facts and circumstances is important to adequately assess the range of potential impacts.

Where inventory as at March 31, 2020 is for the customer's committed orders, a delay in the delivery of orders or customers unwillingness to obtain the delivery after March 31, 2020, may not require write down of the inventory. This would be when company by the reporting date has no information about customer's unwillingness or inability to obtain the ordered inventory. Hence it is a non-adjusting event.

In another scenario, while inventory of finished goods as at March 31, 2020 is for committed orders, however, company before March 31, 2020 has reasonable information about customer's unwillingness or inability to obtain ordered inventory. The customer may have finally communicated about cancellation of order after March 31, 2020, but company has reasonable knowledge of this event at the reporting date. The conditions subsequent to reporting date provide further evidence of event that existed at the reporting date, hence would be an adjusting event. The inventory write-down may be required based on its net realisability.

Therefore, a careful evaluation of facts and circumstances of different scenarios and judgment would be required to determine the accounting implication on the reporting period financial statements.

Question 20

COVID-19 might adversely impact company's sales volume. Sales could be significantly reduced or suspended for an extended period subsequent to the balance sheet date. How this sale decline could impact measurement of inventory at the balance sheet date?

An assessment would be made as to whether the events that contributed in significant reduction of sales or suspension of business also affect the net realisable value of inventory at the reporting date or not.

In accordance with IAS 2 (paragraph 30) events after the reporting date may provide evidence about the conditions that existed at the reporting date. In context, of inventory such subsequent events may require write-down of inventory at the reporting date.

Company's decline in sales volume could be due to COVID-19 related events that existed before the reporting date, such as customers reduced demands, travel restrictions in March 2020.

In case company determines that such events existed at the reporting date, an adjustment for inventory write-down may be required based on the difference between cost and NRV.

In addition to COVID-19 related events and conditions, company is also required to consider other unrelated factors that resulted in slowdown in the inventory turnover.

Question 21

Due to closure/curtailment of operations, the production of inventory might decrease significantly. This could result in a prolonged shut-down or idle capacity of the production facility. How prolonged shut-down or idle capacity could impact the inventory costing?

In accordance with IAS 2, cost of inventories comprises of:

- Cost of purchase
- Costs of conversion
- Other cost incurred in bringing the inventories to their present location and condition.

The production or conversion costs include all direct costs such as labour, raw materials and direct overheads along with allocated fixed and variable costs.

As a consequence of COVID-19 related restrictions, companies might have reduced the production levels. The significantly low production levels could be due to factors such as reduced demand, labour and material shortages, and unplanned facility or equipment downtime.

Even company has significantly low production levels however costs would still be incurred (i.e. fixed cost). The impact of allocation of fixed overheads to produced inventory would result in a significant increase in cost of produced inventory items. As a consequence of such low production or idle plant the amount of fixed overhead allocated to each unit of production will not be increased instead unallocated overheads are recognized as an expense in the period in which they are incurred.

Further, in accordance with IAS 2 abnormal amounts of wasted material, labour and other production cost are recognised as an expense and are not allocated to the cost of inventory.

Provisions and liabilities

Question 22

The lockdown measures might result in complete or partial closure of operations of a company. These circumstances could also impact company's contractual arrangements. While preparing its financial statements, how implications of these circumstances should be considered?

Due to lockdown measures, companies may have closed the operations or instructed staff to work from home. In certain cases companies may face difficulty in resuming the operations. On the other hand companies may have enforceable obligations under the contractual arrangements.

For example, the impact of lockdown measures may be in the form of:

- Closure of operations or decrease in demand with no corresponding decrease in obligations to receive deliveries from the suppliers
- Closure of offices or operations with no corresponding decrease in lease obligations
- Disruption in supply chain (raw material supplier not been able to provide supplies) leading to slow down in production
- Cancellation of orders due to travel restrictions (airline ticket or shipping cancellations etc)
- Cancellation of events (marriage ceremonies, office conferences, entertainment events etc)

These circumstances warrant evaluation of all contractual arrangements for determination of remedial measures and appropriate accounting in the current-period financial statements.

Company for determining the implications for the financial reporting should consider:

Applicability of contractual terms

Even though international government as well as Pakistan government have taken lockdown measures including travel restrictions, however, in principle, these measures do not exempt a company from complying with its contractual obligations.

In present circumstances, the contractual terms between the company and counterparties would determine the obligations of the company, including its financial obligations. Therefore, unless the contracts are mutually amended or a legal instrument of government provides relief from the contractual terms, there would be no exemption.

Impact on company's obligations

Whether the COVID-19 related events have resulted in a temporary or permanent impediment in fulfilling the obligations. In case of temporary impediment company may start execution of the contract as soon as the restrictive measures are lifted, it is thus of high importance to monitor how the situation evolves.

Remedial measures

Renegotiating the terms of the agreement with the contractual parties on the grounds of the unforeseen change of circumstances at the time of the conclusion of the contract.

In contractual matters, parties can always mutually decide to amend the terms of their agreements. Generally speaking, no specific formal requirement is imposed on renegotiation. However, it is advisable to formalise it through a written amendment to the contract. In addition, the contract may include specific provisions governing the contractual renegotiation.

Legal aspects of the agreements

Legal provisions such as force majeure, early termination, and penalties etc to determine the course of action.

In accordance with IAS 37 (paragraph 68) consider the lower of the present value of

- Cost of fulfilling the contract; and
- Costs of terminating the contract.

(Please also see next question for the determination of unavoidable costs in a lease arrangement)

In accordance with IAS 37 (paragraph 67) if a contract can be terminated without incurring a penalty, then it is not onerous. This is because company can exit the contract without completing the contract and incurring any cost.

Implication of contractual terms on financial reporting

Whether the non-fulfillment of legally enforceable contract:

- Impacts going concern assessment of the company.
- Requires any adjustment to the financial statements (e.g. recognition of additional liabilities, provisions for onerous contracts, provisions for restructuring or impairment of assets due to decline in recoverable amounts or net realisability).
- Requires reclassification of assets and liabilities (e.g. classification of long-term debt as a current liability due to breach of loan covenant, classification of non-current assets as assets held for sale).
- Disclosure in the financial statements to draw users attention to significant uncertainties and risks.

Question 23

A company could be required to account for an un-avoidable liability or a loss making contract? How a loss making contract (i.e. an onerous contract) is identified and accounted for under IAS 37?

As a result of COVID-19 related events, including lockdown measures taken by the government, companies may have difficulties in meeting contractual obligations toward their counterparties.

Even though companies may have entered into renegotiations during the reporting period, however, at the reporting date companies may not be in a position to fully comply with the contractual terms. Further, the enforceable obligations under the contract might result in some existing purchase or sale contracts becoming loss making i.e. onerous.

IAS 37 provides accounting for such onerous contracts. IAS 37 (paragraph 10) defines an onerous contract as a contract in which the unavoidable costs of meeting the obligations exceed the economic benefits expected to be received under the contract.

Therefore, in assessing whether a contract is onerous, company should consider:

- The unavoidable costs of meeting the obligations of the contract.
- The unavoidable costs are the lower of the net costs of fulfilling the contract and the cost of terminating it.
- The economic benefits expected to be received.

Unavoidable costs

For the unavoidable costs of meeting the obligations, company should:

- Include costs that are directly variable with the contract and therefore incremental to the performance of the contract;
- Not include allocated or shared costs that will be incurred regardless of whether the company fulfills the contract; and
- Include costs that cannot be avoided by company's future actions.

The examples of costs that are not incremental or cannot be avoided include depreciation of property, plant and equipment, non-cancellable operating lease costs and cost of staff who would be retained. These costs are generally operating costs, and have to be incurred irrespective of the company's decision to complete or terminate the contract.

Determine the costs of terminating the contract. This would include unavoidable costs to be incurred before exercising the termination rights and termination related penalties. Determine the present value of unavoidable costs of completing the contract and costs of terminating the contract, based on the time period(s) under the contractual terms.

Expected economic benefits

Company is required to estimate the expected benefit under the contract. This would involve estimation of the future inflows related to the contract. This would require management judgment, possibly based on the past experience or expert advice.

Recognition of provision

In case the unavoidable costs exceed the expected benefits, a provision for the onerous contract would be recognised in the reporting period.

However, in accordance with IAS 10 (paragraph 69) before recognising a provision for an onerous contract, a company tests all assets dedicated to the contract for impairment as per requirement of IAS 36.

Question 24

The company has obtained office space on a five year lease term, ending in 2022. Lease agreement includes monthly lease payments and early termination penalties. Due to COVID-19, company may consider terminating the lease agreement in 2020. How this arrangement would be accounted for under IAS 37?

In accordance with IAS 37, company should consider whether contract is onerous or not. For determination of onerous contract company considers whether the unavoidable costs of completing or terminating the contract exceed the expected benefits.

The leases on unfavourable terms (e.g. where a company pays rentals which are more than normal market rentals) are not right away onerous contracts. This is because the expected benefits may exceed the unavoidable costs.

In the lease arrangement the determination of unavoidable costs and expected benefits requires consideration of following:

Costs - The costs of fulfilling the contract should be determined based on the enforceable contractual terms at the reporting date. This determination would involve comparison of:

- The present value of lease rentals for the remaining periods (i.e. 2020 to 2022); and
- The present value of cost of terminating the contract in 2020 (i.e. payment of penalty etc).

The lower of two should be considered, regardless of the company's intention.

Expected benefits - The expected benefits under the lease for office space would involve estimation of any inflows expected from the use of the office. Consideration should be given to any sub lease income that company can earn by sub-letting the office space. This should be considered even if company chooses not to sub-lease the office space or if a sub-lease requires the lessor's approval, provided that lessor would not allow sub-letting unreasonably. However, if a lease prohibits sub-letting, then the potential sub-lease income should not be considered.

Measuring the provision - In accordance with IAS 37 (paragraph 66), where costs exceed expected benefits (based on above calculations) company should recognise the excess as a provision for onerous lease in the financial statements

Impairment of right of use asset i.e. office space - Company should also consider whether the right of use asset is impaired or not.

Question 25

A company may exercise its termination rights, under the contract. Further, there is no penalty for exercising the termination right. In terms of IAS 37, whether there would be financial obligation(s) on the company if it exercises its termination right?

In principal, the timing of decision to terminate the contract would determine whether company has a legal or constructive obligation at the reporting date.

In accordance with IAS 37 (paragraph 67) if a contract can be terminated without incurring a penalty, then it is not onerous. This is because company can exit the contract without completing the contract and incurring any cost. Therefore, there would be no financial implications of such a contract.

Question 26

Due to COVID-19 related events and circumstances, a company might plan or start a restructuring plan. What would be the key considerations for accounting and disclosure of the restructuring provisions?

IAS 37 (paragraph 10) defines restructuring as a programme planned and controlled by management that materially changes the scope of business or the manner in which it is conducted.

Due to COVID-19 management may consider restructuring such as:

- Closure of business location;
- Change in management structure; or
- Fundamental reorganizations that have a material effect on the nature and focus of the company's operations.

The restructuring provision may result in a constructive obligation under IAS 37 (paragraph 72).

In the reporting period, company would be recognising the restructuring provision only when both of the following conditions are met:

- There is a detailed formal plan for the restructuring; and
- Company has raised a valid expectation in those affected that the plan will be implemented.

Company would be raising valid expectation in those affected that the plan will be implemented by:

- Announcing the main features of the plan to those affected; or
- Starting implementation of the plan.

Company's announcement should include information about the business or part of the business that is affected, estimated timing and functions and approximate number of employees affected. Therefore, the approval of the restructuring plan by the company's board is not by itself sufficient to recognise a restructuring provision, unless the main features have been announced to those affected by the plan or company has started to implement the plan.

The announcement of plan in sufficient detail would be enough for creating any valid expectation in the counter parties on their own (such as employee's expectation of redundancy payments). In terms of IFRS, it is not necessary to specify individual parties such as employees, suppliers.

A restructuring provision shall include only the direct expenditures arising from the restructuring and costs associated with ongoing activities are not included in restructuring provisions.

In measuring the provision, company should consider costs such as:

- Lease termination costs, such as lease termination penalties.
- Employer termination benefits that relate directly to restructuring (e.g. Golden handshake schemes, share based termination benefits).
- Legal and professional fees directly incurred for restructuring.
- Expected costs from when operations cease until final disposal.
- Onerous contract provisions.

The termination benefits for employees made redundant as part of the restructuring are recognised in accordance with the specific requirements of IAS 19, *Employee Benefits*.

Certain costs as outlined in IAS 37 (paragraph 81) are not allowed to be included in the restructuring provision. Accordingly, company should not recognise provision for:

- Expected costs till ceasing or expected operating losses.
- Impairment of assets;
- Gain or losses on expected disposal of assets;
- Costs of training or relocating the staff;
- Loyalty bonus and other staff costs for their retention and continuation;
- Costs of moving the assets or office;
- Investments in new systems;
- Administration or marketing costs;
- Allocation of corporate / head office overheads; and
- Secretarial costs such as cost of changing the name of company.

Therefore, in current circumstances for recognising a restructuring provision, company should ensure that the obligating event before the reporting date has created a provision.

Once the nature of the restructuring costs has been identified, the provision is measured at the best estimate of the anticipated costs. That amount is discounted using a pre-tax rate that reflects both the time value of money and risks specific to the liability, if the financing component is material.

Accordingly for the restricting plan, company is required to ensure that:

- A formal detailed restructuring plan is in place, and that those affected by the plan have a valid expectation that it will be carried out, before recognising a restructuring provision.
- Restructuring provision does not include costs associated with the company's ongoing activities, unless they relate to an onerous contract.
- Clear and transparent disclosures about the nature of the restructuring provision, the expected timing of any resulting outflows of economic benefits and related uncertainties.

Question 27

A company might announce its restructuring plans after the reporting date. In this scenario what would be the major considerations for financial reporting at the balance sheet date?

As explained above, the restructuring provision are recognised once these become legal or constructive obligations. If company announces restructuring plans after the reporting date, there would be no legal or constructive obligation at the reporting date. Therefore, no provision would be recognised for such future restructuring.

However, company should consider the disclosure requirements of IAS 37, where it has commenced the restructuring after the balance sheet date but before the approval for issue of financial statements.

Further, post balance sheet restructuring might provide evidence of impairment at the balance sheet date, which would be an adjusting event in accordance with IAS 10.

Question 28

A company through an announcement may decide to redesign its existing plant or transfer a plant from one location to another. Would this lead to a restructuring provision?

A company may decide to redesign the asset, or utilize the asset at another location. These costs are not restructuring provisions, rather costs of new equipment and improvement to existing equipment are capitalised when they are incurred in accordance with IAS 16.

Question 29

A company might expect to receive reimbursements from third parties (e.g. insurance claim reimbursement) against the provision. What is the IFRS guidance for reimbursements?

In accordance with IAS 37, where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised only when it is virtually certain that reimbursement will be received if the company settles the obligation.

Company would typically remain liable for the entire obligation. In the statement of financial position, reimbursements are therefore presented separately as assets.

Expenses relating to a provision can be presented net of the amount recognised for a reimbursement in the income statement. The amount of reimbursement recognised should not exceed the amount of the related provision.

Question 30

Should a company in anticipation of future operating losses, record these in current reporting period?

As a result of current market situation due to COVID-19 pandemic, most of the companies might be foreseeing the future operating losses. However, under IAS 37 (paragraph 63) a company is not permitted to recognise future operating losses or future business recovery of costs.

However, an expectation of future operating losses might be an indicator that certain assets in the companies operations may be impaired. IAS 37 (paragraph 65) explains that such assets shall be tested for impairment in accordance with IAS 36.

Leases

Question 31

Due to financial constraints and reduced business activity, a company (as lessees) might be granted lease rental concession under an existing lease agreement. How lease concessions should be accounted for under IFRS 16?

As a part of facilitative measures taken by companies due to COVID-19, contractual terms of lease arrangements might be renegotiated and lessees might be granted some sort of a concession in connection with lease payments.

To account for a such concession under IFRS 16, *Leases*, companies first need to determine the nature of the concession, whether such rent concession is:

- Lease modification i.e. a change in scope or consideration for a lease that was not part of the original terms and conditions of the lease; or
- Variable lease payment i.e. the original terms and conditions of the lease may include a clause for such concessions if certain events occur.

Where the rent concession is determined to be a lease modification, companies shall apply the detailed guidance in IFRS 16 on accounting for lease modifications. Whereas, when it is determined to be a variable lease payment, the company shall account income or expense in the period in which they arise.

In order to make the above assessments in the current circumstances, the companies need to consider following:

- Review existing lease contracts to identify whether they contain concession clauses that may be triggered in the current conditions;
- Identify and document key judgements made e.g. in assessing the nature of the concession and, where relevant, determining the revised discount rate; and
- Consider expanding disclosures on the accounting impact of concessions as a result of the outbreak.

Question 32

Whether the company is required to consider the recoverability of a leased (i.e. right of use asset)?

IAS 36, requires non-financial assets (including right-of-use assets) to be tested when there is an indication of possible impairment. The impact of reduced economic activity, lock downs and lower revenues are likely to affect many companies and might also indicate impairment in the right-of-use assets along with the other non-financial assets. Further, the circumstances giving rise to the rent concessions as a result of the COVID-19 pandemic are also likely to indicate that assets may be impaired, e.g. loss of earnings during the period covered by a rent concession may be an indicator of impairment of the related right-of-use asset.

Accordingly, a company shall apply IAS 36 to determine whether the right-of-use asset is impaired and to account for any impairment loss identified. A key consideration in the impairment testing of right-of-use assets is whether it can be performed at the individual asset level or not. Where the recoverable amount of the right-of-use asset cannot be determined individually, the impairment test moves to the level of the cash-generating unit ('CGU') to which the right-of-use asset belongs.

Typically, a right-of-use asset does not generate cash inflows that are largely independent from other assets, and it should be grouped within a CGU for an impairment test in these circumstances. One exception may be an asset that is subleased and therefore may generate cash inflows that are largely independent from other assets. Another common exception relates to leased investment properties, accounted for under IAS 40 *Investment Property*. In such a case, the leased investment property is a right-of-use asset that might have cash inflows (from tenants under a sublease) which are largely independent from other assets, and therefore this property could be considered for impairment at the individual asset level. However, a right-of-use asset classified as an investment property can be recorded at fair value under IAS 40 and, if it is carried at fair value, the property need not be assessed for impairment in accordance with IAS 36.

Question 33

How the lease term could be impacted due to changes in lease assessment or exercise of termination right options?

Under IFRS 16, lease term is non-cancellable period of lease together with both:

- Periods covered by a lessee's extension option if extension is reasonably certain; and
- Periods covered by a lessee's termination option if the lessee is reasonably certain not to terminate.

In assessing whether a lessee is reasonably certain to exercise an option to extend a lease, or not to exercise an option to terminate a lease, a company is required to consider all relevant facts and circumstances that create an economic incentive for the lessee to exercise the option to extend the lease, or not to exercise the option to terminate the lease.

A company is required to revise and reassess the lease term if there is a change in the non-cancellable period of a lease or when a significant event or a significant change in circumstances within its control changes any of its assessments about what is reasonably certain i.e. to exercise an extension option or not to exercise an option to terminate the lease early.

As in current market situation due to COVID-19 pandemic, most of the companies might make business decisions that affect their lease contracts. As a result, lease contracts containing renewal and termination clauses may need to be reassessed by considering effect of current economic incentive for the lessee to determine whether the lessee initial conclusion that exercise of the extension option and not to terminate lease option included in initial lease term determination was still reasonably certain or not. Because this will determine whether lease term needs to be revised or not.

Any changes in the lease term could have a significant impact on the carrying amount of lease assets and liabilities.

Question 34

Recently, SBP has decreased the discount rate. What could be the implications of this decrease on the measurement of its lease liabilities under IFRS 16?

SBP recently reduced its policy rate from 11 percent to 9 percent considering the current economic situation of the country as a result of COVID-19 pandemic. The change in discount rate along with the impending concessions and modifications in the lease contracts as a result of current market situation due to COVID-19 pandemic, might trigger the need for re-measurement of lease liabilities using revised discount rates under IFRS 16.

Under IFRS 16 (paragraphs 40-42), company is required to re-measure the lease liability by discounting the revised lease payments when there is a change in:

- the lease term;
- the assessment of an option to purchase the underlying asset;
- amount expected to be payable under a residual value guarantee; or
- future lease payments resulting from a change in index or a rate used to determine those payments.

In case of (a) and (b) above, the lessee shall use a revised discount rate as the interest rate implicit in the lease for the remainder of the lease term, if that rate can be readily determined, or the lessee's incremental borrowing rate at the date of reassessment, if the interest rate implicit in the lease cannot be readily determined. In case of (c) and (d) above, the lessee shall use an unchanged discount rate, unless the change in lease payments results from a change in floating interest rate. In that case, the lessee shall use a revised discount rate that reflects changes in the interest rate.

Further, under IFRS 16 (paragraph 45) when there is a modification in the terms and conditions of the lease contract which is not accounted for as a separate lease, a company is required to re-measure the lease liability by discounting the revised lease payments using a revised discount rate. The revised discount rate is determined as the interest rate implicit in the lease for the remainder of the lease term, if that rate can be readily determined, or the lessee's incremental borrowing rate at the effective date of the modification, if the interest rate implicit in the lease cannot be readily determined.

Financial instruments

Question 35

What should be the key considerations of companies, while developing the expected credit loss model?

IFRS 9 *Financial instruments* requires expected credit losses (ECLs) to be measured as an unbiased, probability-weighted amount, using reasonable and supportable information that is available without undue cost or effort at the reporting date. Evaluating ECLs requires companies to consider a range of possible outcomes and their respective probabilities, and to apply judgement when determining what constitutes reasonable and supportable forward-looking information [IFRS 9.5.5.17].

The adverse impacts of COVID-19 pandemic can impact the ability of borrowers, whether corporate or individuals, to meet their obligations under loan relationships. Individual and corporate borrowers may have a particular exposure to the economic impacts in their geographical location and industry sector. More broadly, reductions in forecasts in economic growth increase the probability of default across many borrowers and loss given default rates may increase due to the fall in value of collateral evident more generally by falls in prices of assets.

Following key considerations warrant specific attention in the wake of current economic situation as a result of COVID-19 pandemic:

Re-segmentation of loan portfolios or groups or receivables: For the purpose of measuring ECLs and for determining whether significant increase in credit risk (SICR) has occurred, a company should group financial instruments on the basis of shared credit risk characteristics and reasonable and supportable information available on a portfolio basis.

The occurrence of the COVID-19 outbreak might change the risk characteristics of certain loans or receivables, because the respective borrowers or customers might engage in businesses, or locate in areas, which have become affected, or are more prone to be affected, by the outbreak. Therefore, companies should consider re-segmenting the portfolios.

Individual and collective assessment of loans, receivables and contract assets: Due to the abnormal circumstances, it may take time for a company to detect actual changes in risk indicators for a specific counterparty. In order to accelerate the reflection of such changes in credit quality not yet detected at an individual level, it may be appropriate to adjust ratings and the probabilities of default (PD) on a collective basis, considering risk characteristics such as the industry or geographical location of the borrowers.

Extension of payment terms: If payment terms are extended in light of the current economic circumstances, the terms and conditions of the extension will have to be assessed to determine their impacts on the ECL estimate as well as any other accounting impacts.

Question 36

In current environment, companies might re-negotiate the terms of their existing financing arrangements. How restructuring or amendment of a loan agreement would be accounted for under IFRS 9?

Due to unstable trading conditions and decrease in cash flows, the capacity of the companies to fulfill their loan repayment commitments would be adversely impacted. As a result, companies would approach the financial institutions for rescheduling of the loan repayment terms.

Under IFRS 9 (paragraph 3.3.1-2), a company should derecognise a financial liability if the cash flows are extinguished (i.e., when the obligation specified in the contract is discharged, cancelled or expires) or if the terms of the instrument have substantially changed.

IFRS 9 provides guidance for determining if a modification of a financial liability is substantial, which includes a comparison of the cash flows before and after the modification, discounted at the original effective interest rate (EIR), commonly referred to as 'the 10% test'. If the difference between these discounted cash flows is more than 10%, the loan would be derecognized.

If, following the guidance above, a financial liability does not result in derecognition, the original EIR is retained and there is a catch-up adjustment to profit or loss for the changes in expected cash flows discounted at the original EIR.

Companies are required to assess the specific facts and circumstances of each rescheduling of financing arrangement, to determine if it is a modification or extinguishment.

Question 37

Should a company adjust or disregard the quoted price in a period of significant market volatility when determining the fair value of traded equity investment?

If The fair value of an asset or liability at the reporting date should be determined in accordance with the relevant requirements of IFRS 9 and IFRS 13 *Fair Value Measurement*. IFRS 13 defines fair value the price that would be received to sell an asset or paid to transfer a liability in an ordinary transaction between market participants at the measurement date.

Under IFRS 13, when fair value is based on an observable market price, the quoted price at the reporting date should be used [IFRS 13.76-77].

The volatility of prices on various markets has increased as a result of the spread of COVID-19. This affects the fair value measurement directly if fair value is determined based on market prices (for example, in case of shares or debt securities traded on an active market).

The above features may need adequate management consideration and professional judgment to determine whether the quoted prices are based on transactions in an orderly market. It may not be always appropriate to conclude that all transactions in such a market are not orderly. The concept of an orderly transaction is intended to distinguish a fair value measurement from the price in a distressed sale or forced liquidation. The intent is to convey the current value of the asset or liability at the measurement date, not its potential value at a future date.

Question 38

The company under bank overdraft facility might have a overdrawn balance at the reporting date. How this overdrawn balance would be reflected in the financial statements?

Bank overdraft is a financial liability. In accordance with IAS 7 *Statement of Cash Flows* (paragraph 8) bank borrowings are generally considered to be financing activities.

However, IAS 7 also explains that the overdrafts which are immediately repayable on demand and are integral part of a company's cash management are included as a component of cash and cash equivalents. The presentation of bank overdrafts as a part of cash and cash equivalents is for the purposes of statement of cash flows.

In the statement of financial position, presentation of 'cash and bank balances' net off the bank overdraft depends on fulfilling off-setting principle of financial instruments outlined in IAS 32 *Financial Instruments: Presentation* (paragraph 42). The bank overdraft and bank balance are off-set and presented net in the statement of financial position only when:

- Company has a legally enforceable right to set off bank overdraft and bank balance;
- Company intends to settle the overdraft with the bank balance.

If the off-set criteria is not met, the bank overdraft balance is a liability and should be reflected accordingly in the statement of financial position.

Question 39

How should a company account for the interest free loans / below-market interest loans obtained from the parent company, directors or sponsors?

The operational cash flows and overall liquidity position of companies could be severely impacted, as lockdown measures have resulted in complete or partial closure of business activities. In such cases companies might obtain financial support from parent companies, directors or sponsors, in the form of interest free or below market interest loans.

A company which receives interest free loans from a parent company, director or a sponsor should consider the requirements of IAS 32, IFRS 9 and TR 32 *Director's Loan* to determine proper classification and measurement of such loans.

IFRS 9 requires all financial instruments to be measured on initial recognition at fair value. Where loans are made on normal commercial terms, no specific accounting issues arise and the fair value at inception will usually equal the loan amount. The normal commercial terms include the market interest rate that an unrelated lender would demand in making an otherwise similar loan to the company. This interest rate would reflect the company's credit risk, taking into account the loan's ranking and any security, as well as the loan amount, currency duration and other factors that would affect its pricing.

On the other hand, if loan is not on normal commercial terms (e.g. carries below market rate interest), the below-market element of the transaction needs to be evaluated and separately accounted for.

The classification of an interest free loan from a parent company, director or sponsor as a financial liability or equity depends upon the repayment terms of such loan. Broad categories could be:

- A short-term interest free loan;
- An interest free loan repayable on demand;
- An interest free loan repayable at the discretion of borrower; or
- An interest free loan repayable on a specified date.

Repayment term of interest free loan	Classification	Accounting of interest free loan
Short-term loan	A short-term loan fulfills the criteria of financial instrument and is classified as financial liability.	The short-term loans that are expected to be repaid in the near future should generally be recorded at the loan amount, as loan amount is likely to be a sufficiently close approximation to fair value in most of the cases.
Loans repayable on-demand	Interest free loan repayable on demand fulfills the criteria of financial instrument and is classified as financial liability.	The interest free loans that are repayable on demand should generally be recorded at the loan amount.
Loan repayable at the discretion of borrower	Where the interest free loans are repayable at the discretion of the borrower, then such loans do not fulfill the classification criteria for a financial liability as there is no contractual obligation to deliver cash or another financial asset to the lender. These loans are considered as an equity contribution by the owners of company.	The loan proceeds of the interest free and below market-interest loan that is repayable at the discretion of borrower should be reflected in the statement of changes in equity.

Repayment term of interest free loan	Classification	Accounting of interest free loan
Loan repayable at a specified date	Interest free loan repayable as per a specified term fulfills the criteria of financial instrument and is classified as a financial liability.	<p>The loan proceeds of the interest free and below market-interest loan should be compared with its fair value.</p> <p>The fair value is calculated as present value of all future repayments discounted using the prevailing market rate of interest for a similar instrument (similar as to currency, term, type of interest rate and other factors) with a similar credit rating.</p> <p>Any difference between gross amount of loan proceeds and the fair value is recognised in equity, considered as a capital contribution from the parent company, director or sponsor.</p> <p>Subsequently, the loan should be measured at amortised cost, using the effective interest method. This involves "unwinding" the discount such that, at repayment, the carrying value of the loan equals the amount to be repaid.</p> <p>The unwinding of the discount should be reported as interest expense in the statement of profit or loss.</p>

In case a company obtains an interest free or below interest loan from an unrelated party, the difference between gross amount of loan proceeds and the fair value should be reported as interest income in the statement of profit or loss.

The subsequent unwinding of discount should be reported as interest expense in the statement of profit or loss.

Question 40

A company might have breached loan covenant(s). How breaches of loan covenants could impact the classification as current and non-current?

A breach of the long-term loan covenant(s) may make the loan immediately payable or payable on demand. The breach of loan covenant triggering repayment depends on the contractual terms and varies from one loan agreement to another.

If such a breach of loan covenant(s) is before the reporting date, the entire loan would be a current liability. This classification would be irrespective of the possibility, that lender after the reporting date and before authorisation of financial statements has agreed to refinance or has not demanded the payment. In accordance with IAS 1, the loan is a current liability because, at the balance sheet date, company does not have an unconditional right to defer the settlement for at least twelve (12) months after the balance sheet date.

On the other hand, if lender agreed before the balance sheet date to refinance (e.g. provide a grace period of more than twelve (12) months, ending after the balance sheet date), the loan is classified as non-current liability.

Assets held for sale

Question 41

A company might plan to dispose-off items of property, plant and equipment within next 12 months. How these assets would be disclosed in the financial statements?

The current interruption in the economic activity as a result of COVID-19 and economic uncertainty might force companies to consider implementing restructuring plans such as the sale or closure of a part of business or permanent downsizing of operations.

In such a situations, companies should consider the requirements of IFRS 5.

The non-current assets (e.g. property, plant and equipment, including capital stores) pertaining to part of business planned to be closed under a restructuring plan, should be classified as held for sale in line with IFRS 5, provided these are available for immediate sale in as-is condition, and it is probable that the sale shall be concluded within one year of reporting date [IFRS 5.6-8].

Question 42

What are the specific financial statement presentation requirements for discontinued operations?

The operating results of the part of business planned to be closed under a restructuring plan as a result of economic downturn from COVID-19 pandemic qualify to be presented as discontinued operations under IFRS 5.

Company shall present a single amount in the statement of comprehensive income comprising total of:

- the post-tax profit or loss of discontinued operations; and
- the post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation.

Further, in accordance with IFRS 5 (paragraph 33) the analysis of the single amount into revenue, expenses etc. shall be disclosed in the notes to the financial statements.

In accordance with IFRS 5 (paragraph 41) company is also required to provide additional disclosures in the notes such as description of non-current assets, description of facts and circumstances of sale or expected sale, expected manner and timing of disposal etc.

Revenue

Question 43

What is the enforceability criteria of a revenue contract and why it would require special consideration in COVID-19 impacted business environment?

The first step in the revenue recognition model of IFRS 15 *Revenue from Contracts with the Customers* is the identification of a contract with the customer. Some of the key conditions to evidence the existence of a contract include:

- Are the both parties to the contract committed to performing their respective obligations?
- Is it probable that consideration will be collected?
- Does the contract allow each party to terminate a wholly unperformed contract without compensating the other party?

A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by a company's customary business practices. The practices and processes for establishing contracts with customers vary across legal jurisdictions, industries and companies. In accordance with IFRS 15 (paragraph 10) a company shall consider those practices and processes in determining whether an agreement with a customer creates enforceable rights and obligations.

Determining whether rights and obligations are enforceable may require significant judgement and regular reassessment. As circumstances continue to change, companies should monitor the enforceability of their contract terms closely. The current economic situation due to COVID-19 pandemic may bring into question the enforceability and existence of contracts with the customers in terms of conditions outlined in IFRS 15 because:

- Customers may not be able to honor their commitments to perform their respective performance obligations.
- A company's right to payment for performance to date may not be enforceable due to existence of force majeure or similar clauses in contracts or government actions to restrict the companies from enforcing the performance obligations.
- The companies and their customers may seek to modify the terms of existing contracts in response to the impacts of COVID-19 pandemic.

Therefore, companies need to reassess whether the contract existence and enforceability criteria continue to be met for existing contracts.

Question 44

Due to COVID-19 related events, a customer might face difficulty in paying for goods or services. What could be the impact on company's revenue recognition due to customer's inability to make payments for goods or services?

Under IFRS 15 (paragraph 9(e)), one of the key conditions for existence of an enforceable contract with the customer is the collectivity of consideration due from the customer. Collectivity is that it is probable the company will collect substantially all of the consideration to which it expects to be entitled in exchange for the goods or services that will be transferred (the collectability criterion).

In the current economic situation due to COVID-19 pandemic, customer credit risk could increase significantly as the economic activity has almost come to a halt and underemployment/unemployment has risen manifold. This might indicate that the collectability criterion is no more met in some of the contracts with the customers.

If the collectability criterion is not met at the contract inception or on contract reassessment, the company cannot apply the revenue recognition model under IFRS 15. In such circumstances, a company recognises consideration received as revenue only when either of the following events has occurred:

- the company has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the consideration promised by the customer has been received by the company and is non-refundable; or
- the contract has been terminated and the consideration received from the customer is non-refundable.

IFRS 15 requires a company to first consider any potential price concessions that it expects to provide, which reduce the transaction price, before assessing collectability. Additionally, a company should consider as part of the collectability assessment whether it has the ability and intent to cease providing service if the customer fails to pay [IFRS 15.9(e), 52-54]. In many cases it may be challenging to conclude that collection for new sales is probable when the customer has been unable to pay existing receivables. This type of situation requires judgment and is dependent upon facts and circumstances.

In respect of contracts for which collectability criterion was satisfied at the contract inception and the company has satisfied its performance obligations, the company shall assess both the receivables and contract assets for impairment in accordance with IFRS 9.

Question 45

As a result of lockdown measures a company might not be able to deliver/ship goods to its customers. In such a case how revenue recognition could be impacted?

Under IFRS 15, a company shall recognise revenue when or as the company satisfies a performance obligation by transferring the promised goods to a customer. An asset is transferred when the customer obtains control of that asset.

In the context of current lock down situation to stop the spread of COVID-19, it is likely that companies might not have been able to deliver products to its customers. These hurdles could be due to various reasons, including travel and shipping restrictions or closure of customer's facility preventing physical delivery.

In such circumstances, a company needs to assess whether it has satisfied its performance obligation by transferring the promised good to the customer. IFRS 15 requires a company to determine at contract inception whether it satisfies the performance obligation over time or satisfies the performance obligation at a point in time. If a company does not satisfy a performance obligation over time, the performance obligation is satisfied at point in time.

In cases where the performance obligation is satisfied upon delivery of promised goods to the customers, i.e. point in time, a company shall not recognise revenue where it has not been able to deliver the promised goods to the customer in accordance with the terms of contract.

In some cases, revenue may be recognized over time such that all or most of the revenue is recognized prior to delivery. For example, revenue for customized products might be recognized over time as the products are manufactured if the company has the right to payment for performance to date. If revenue is recognized (i.e., control transfers) at a point in time, the guidance provides five indicators that help to identify the point at which control has transferred:

- (1) the company has present right to payment;
- (2) the customer has legal title to the asset;
- (3) the company has transferred physical possession of the asset;
- (4) the customer has the significant risks and rewards of ownership;
- (5) the customer has accepted the asset.

Accordingly, companies might need to make significant judgements considering all pertinent facts and circumstances to determine whether it has satisfied the performance obligation by transferring the promised goods to the customer.

Question 46

In current business environment, a company might offer incentives to its customers. What would be the affect of changes in a revenue contract relating to future concessions (such as reducing the price or decreasing quantities of goods or services to be delivered (or minimum purchase commitments)?

Because of current market conditions, it may be necessary for the companies to take facilitative measures such as modifying the contracts with the customers to provide future concessions such as reducing the price or decreasing the quantities.

Such modification would be accounted for as a separate contract only if distinct goods or services are added to the contract for a price equal to standalone selling price (adjusted for contract-specific circumstances). The accounting for a modification that is not a separate contract depends on whether the remaining goods or services are distinct from the goods or services transferred before the modification:

- If the remaining goods or services are not distinct (e.g., a single performance obligation is being modified), the modification is accounted for on a cumulative catch-up basis. Estimates of the transaction price and measure of progress are updated and cumulative revenue recognised is adjusted (increased or decreased) accordingly.
- If the remaining goods or services are distinct (including goods or services that are part of a series), the modification is accounted for prospectively as if it were a termination of the existing contract and the creation of a new contract. The sum of: (a) unrecognized consideration from the original contract and (b) additional consideration promised as part of the modification is allocated to the remaining goods or services to be provided based on relative standalone selling prices as of the modification date.

For modifications accounted for on a prospective basis, price concessions given due to current events (as opposed to concessions related to the company's past performance) will generally reduce the consideration allocated to the remaining goods or services and accordingly, reduce revenue recognised for future goods or services. Judgment may be required to determine whether a decision to give away free or highly discounted goods or services is a modification of an existing customer contract or a marketing offer that does not impact the accounting for existing contracts.

Question 47

Due to financial difficulty, a company might allow extended payment terms to customers. How the extended payment terms could result in significant financing component under IFRS 15?

As a result of current events, a company may decide to offer payment terms to customers that extend longer than typically offered. In accordance with IFRS 15 (paragraph 15.9(e), for a new contract, extended payment terms should be considered in the assessment of whether collection is probable and/or whether the company intends to provide a concession at contract inception.

Extended payment terms may also indicate that the arrangement includes a significant financing component. Importantly, the mere existence of extended payment terms is not determinative when assessing whether collection is probable (for purposes of establishing the existence of a contract) and all facts and circumstances should be evaluated.

Companies should also consider whether extended payment terms affect their assessment of the allowance for doubtful accounts or credit losses under IFRS 9. If a company modifies an existing contract to extend payment terms (potentially changing the transaction price), it should consider whether the contract modification guidance applies, particularly if the change is made in conjunction with other changes to the scope of the contract.

Employee benefits

Question 48

COVID-19 related events might significantly impact company's workforce and operations. Resultantly, it may decide to lay-off employees or negotiate salary reductions. How the company would account for these changes?

As a result of difficult economic conditions due to COVID-19, companies may have started or plan to reduce their workforce or offer lower salaries to existing employees.

Company that offers or is required to pay termination benefits to the affected employees, should consider how and when to account for the liability/expense in accordance with IAS 19.

Company may offer lump-sum termination benefits. Further, company's termination benefit might be in the form of monthly salary for a specified period (e.g. six months) and employee is not required to render service during this period. Another form of termination benefit could be where company increases the post-employment benefits (e.g. when employees last calculated pension amount or gratuity amount is increased). The enhanced amount would be a termination benefit as employee would not be offering any service against this benefit.

After determining the termination benefits, in accordance with IAS 19 (paragraph 165), company should recognise a liability and expense for termination benefits.

The timing of this would be the earlier of the following dates:

- When the company can no longer withdraw the offer of those benefits; and
- When the company recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of termination benefits.

The company after announcing the termination plan may withdraw from it. Accordingly, till this date company has no obligation of termination benefits.

However, incase employee has accepted the company's offer of termination benefits, the company cannot withdraw the offer of termination benefits at the earlier of:

- When the employee accepts the offer; and
- When a restriction (such as a legal, regulatory or contractual requirement) on the company's ability to withdraw the offer takes effect.

The termination obligation would be in most cases a short-term liability, expected to be settled within twelve (12) months of the reporting date. Nevertheless, it could be a long-term liability, based on its expected settlement timelines exceeding twelve (12) months of the reporting date.

IAS 10 does not require a specific disclosure about termination benefits. However, company would need to consider the requirements of IAS 24 (Paragraph 17) that requires disclosures about employee benefits for key management personnel.

Salary is a short-term employee benefit. In accordance with IAS 19 (paragraph 11) company shall recognise the expected amount of the reduced salary as an obligation (corresponding salary expense), when an employee has rendered the service. There would be no change in the accounting and presentation of reduced salary compared to earlier period's full salary.

Question 49

What would be the accounting requirements of a termination scheme that is expected to be settled in more than 12 months after the reporting date?

If employee termination scheme involves a longer than 12 months period, the amount expected to be settled after 12 months would require present value calculation. The discount rate of high-quality corporate bond rates with similar duration may be used for determining the present value. The difference between the undiscounted cashflows and their present value should be recognised in the statement of profit or loss over the period as the amount accretes.

Question 50

How should a company account for the recent decrease in the discount rate, while measuring its employee benefit liabilities under IAS 19?

SBP recently reduced its policy rate from 11 percent to 9 percent considering the current economic situation of the country as a result of COVID-19 pandemic.

IAS 19 requires the liability for long term and post-employment benefit obligations to be measured at the present value using discount rates which reflect yield on high quality corporate bonds where there is a deep market in such bonds. For currencies for which there is no deep market in such high quality corporate bonds, the market yields (at the end of the reporting period) on government bonds denominated in that currency shall be used.

The recent cut in policy rate by the SBP will affect the determination of the discount rate used in the re-measurement of liabilities for long term and post-employment benefit obligations in the financial statements for the periods ending on or after June 30, 2020. Therefore, the entities would be required to re-determine the discount rates being used for re-measurement of liabilities for long term and post-employment benefit obligations.

Borrowing costs

Question 51

Company might stop its operations and activities, owing to lockdown measures or liquidity crunch. How closure of operations and activities could impact the capitalisation of borrowing costs?

One of the key counter measures taken by the governments globally to limit the spread of COVID-19 pandemic involves complete or partial lockdowns at the city or state/province level. This might result in suspension of major construction activity on infrastructure development projects due to shortage or unavailability of labour and supplies.

IAS 23, *Borrowing Costs*, requires a company to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, i.e. an asset that necessarily takes a substantial period of time to get ready for its intended use or sale [IAS 23.1, 5]. If a company suspends active development of a qualifying asset for an extended period, then it also suspends capitalisation of the borrowing costs for that asset. [IAS 23.20]

The current economic turbulence resulting from the COVID-19 might warrant suspension of capitalisation of borrowing costs as a result of suspension of active development of on assets under development.

Income taxes

Question 52

COVID-19 might adversely impact future profitability of companies. How these adverse conditions may impact recognition and realisability of deferred tax assets?

Under IAS 12, *Income Taxes*, companies recognise deferred tax, mainly reflecting the origination and reversal of temporary differences and the benefits arising from unused tax losses, tax credits or temporary differences.

The recognition of deferred tax asset for unused tax losses and unused tax credits is based on the general principle that:

- It is probable that company will have future taxable profits; and
- Against those future taxable profits the unused tax losses and unused tax credits can be utilised.

IAS 12 also requires companies to reassess the realisability of the deferred tax assets at each balance sheet date. Accordingly, companies are to make a judgement based on the available information, for not only recognising deferred tax assets, but also for their realisability in coming periods.

IAS 12 also notes that the existence of unused tax losses is a strong evidence that future taxable profit may not be available. As a result, the deferred tax asset recognition principle applies. While companies might have history of recent losses, the recognition of a deferred tax asset arising from unused tax losses or unused tax credits is only to the extent that the company has sufficient taxable temporary differences or there is convincing other evidence that sufficient taxable profit will be available against which the unused tax losses or unused tax credits can be utilised by the company.

While assessing the realisability of deferred tax assets, the company is also required to consider the events occurring subsequent to a company's balance sheet date, but before the financial statements are issued (that provide additional evidence regarding the likelihood of realisation of existing deferred tax assets).

As a consequence of current market situation due to COVID-19 pandemic, companies are expected to face decline in sales and lower profitability. Further, as noted, the existence of unused tax losses is a strong evidence that future taxable profit may not be available. The expected losses in early future years (Post COVID-19 year-ends) and uncertainties whose unfavourable resolution would adversely affect future results are also negative evidence to be considered

Therefore, companies would have to re-assess their assessment of the realisability of its deferred tax assets recognised in the latest financial statements. Accordingly, in the cases where companies do not foresee availability or future profits due to effects of COVID-19 related events, it would have to derecognise the deferred tax assets above the threshold of available taxable temporary differences.

Companies with December 2019 (and prior) years ends that have not yet issued the financial statements, also need to consider the implications of COVID-19 on their financial statements. The earlier assessments and related projections might differ significantly from the present and future outlook due to COVID-19.

Question 53

How should a company account for deferred tax assets in the financial statements for the year ended December 2019, where events after COVID-19 outbreak indicate that the deferred tax is no longer considered to be recoverable?

A company would consider the requirements of IAS 10, to determine whether the non-recoverability of deferred tax assets as at December 31, 2019 due to adverse economic impacts of COVID-19 is an adjusting event or a non-adjusting event.

IAS 10 explains that adjusting events are those that provide evidence of conditions that existed at the end of the reporting period. Whereas, non-adjusting events are those that are indicative of conditions that arose after the reporting period. Judgement is required in determining whether events that took place after the end of the reporting period are adjusting or non-adjusting events.

With respect to reporting periods ending on or before December 31, 2019, there is a general consensus that the effects of the COVID-19 outbreak are the result of events that arose after the reporting date (e.g., in the UK, the Financial Reporting Council has stated that COVID-19 in 2020 was a non-adjusting event for the vast majority of UK companies preparing financial statements for periods ended December 31, 2019).

Similarly, in case of Pakistan, we understand that the adjustments to reported balances of assets and liabilities due to adverse economic impacts of COVID-19 would not be adjusting events for financial statements for the years ends of December 31, 2019. This is because the first ever cases of COVID-19 in Pakistan emerged in late February 2020.

Accordingly, the non-recoverability of deferred tax assets reported in the financial statements for the year ended December 31, 2019 due to COVID-19 after effects should be considered as non-adjusting events. Therefore, the deferred tax assets reported in the financial statements for the year ended December 31, 2019 should not be written down/off due to these becoming irrecoverable as a result of adverse financial impacts of COVID-19.

However, where the management concludes that the impact of non-recoverability of deferred tax assets is material to the financial statements for the year ended December 31, 2019, it is required to disclose the nature of the event and an estimate of its financial effect under IAS 10. Such disclosures may include describing qualitatively and quantitatively, how the market volatility subsequent to year end has affected the recoverability of its deferred tax assets.

Question 54

Government may provide relief from COVID-19 through changes in tax legislation. How a company would account for the impact of changes in tax legislation, if legislation is enacted after the balance sheet date?

IAS 12 (paragraphs 46 and 47) requires current and deferred tax assets and liabilities to be measured using the tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. The substantive enactment has been explained in IAS 12 (paragraph 48), as the practice in some jurisdictions where the announcement of tax rates/tax laws by the government have the substantive effect of actual enactment, which may follow the announcement by a period of several months.

In the light of above guidance, companies would need to assess whether the changes in tax rates/laws introduced by the government as a part of relief measures against the COVID-19 pandemic, had been enacted or substantively enacted at the end of the reporting period. The measurement of current and deferred tax assets and liabilities as at the reporting date would be done using the tax laws/rates which have been substantively enacted through formal announcement even when the actual enactment occurs after the end of the reporting period.

For interim reporting, IAS 34 *Interim Financial Reporting* (paragraph 30) requires income tax expense for each interim period to be based on the best estimate of the weighted average annual income tax rate expected for full financial year. Accordingly, in the interim financial reports, the effect of new legislation is recognised in the interim period in which the legislation is enacted even if the change in the tax rates is retroactive. Companies cannot allocate the effects of retroactive rate changes to prior interim periods and restate the interim financial information for prior interim periods.

For the changes in tax laws/rates under COVID-19 relief measures, which have been substantively enacted after the reporting period, the company would consider the requirements of IAS 10. When there is a significant effect on current and deferred tax assets and liabilities, a company shall disclose an estimate of its financial effect, or a statement that such an estimate cannot be made.

Government grants

Question 55

How different forms of government assistance should be recorded?

Government is also responding to limit the adverse economic impacts of COVID-19 pandemic by providing various reliefs and assistance to the affected sectors of the economy. The accounting for government grants and assistance is covered under IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*.

The proper accounting for government grant under IAS 20 i.e. whether the grant income should be recognised as income immediately or should be deferred, depends on the type of the grant and the terms and conditions attached to it. Companies need to evaluate all the facts and circumstances of each type of government grant in the light of IAS 20 guidance to determine the appropriate accounting.

For other types of government assistance which cannot reasonably have a value placed upon them and hence do not fulfill the definition of a government grant, a company is required to disclose nature and extent of such assistance.

Presentation and disclosures

Question 56

Due to COVID-19, company may have recorded expenses or provisions of material amounts, impacting current year's profitability. In view of the materiality and non-recurring nature of these expenses/provisions, can a company present these amounts, separately as extraordinary items in the statement of profit or loss?

IAS 1 *Presentation of Financial Statements* (paragraph 87) states that any items of income or expense shall not be presented as extraordinary items, in the statement of profit or loss, statement of other comprehensive income or in the notes.

IFRS do not define the term extraordinary items. However, previously this concept was contained in IAS 8 *Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting*. That standard defined extraordinary items as income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and therefore are not expected to recur frequently or regularly.

In substance certain expenses/provisions as a consequence of COVID-19 may be non-recurring, distinct and significant. However, IAS 1 prohibits the presentation of items of income and expense as 'extraordinary items' in the statement of profit or loss, statement of other comprehensive income and the notes. Therefore, in accordance with IAS 1, no items of income and expense are to be presented as arising from outside the company's ordinary activities.

Question 57

Companies could be required to make or update significant estimates based on the new and evolving information and circumstances. What could be the impact of these changes on the financial statement disclosures?

The current economic situation and its impacts on businesses has drastically increased the uncertainty about future market scenario. Under IAS 1 (paragraph 125) a company is required to disclose information on the assumptions it makes about the future and other major sources of estimation uncertainty as at the reporting date.

Because of current market conditions, it may be necessary for the companies to make additional disclosures about significant accounting estimates and management judgments, especially those involving valuation and impairment. Estimates and judgments that are based on highly subjective assumptions (e.g., a valuation of financial instruments that is not based on observable market information, assumptions about future events and conditions) may be challenging to develop and also provides the opportunity for management override.

Companies should evaluate their disclosures to ensure that they accurately reflect the current uncertainty and meet the disclosure objective of IAS 1.

Interim financial reporting

Question 58

What are key considerations for interim financial reporting?

The financial impacts of COVID-19 pandemic might be first reported in the interim financial statements.

The interim-financial reporting would also require assessment of company's ability to continue as a going concern. As COVID-19 impacts started in first quarter of 2020, therefore, the going concern assessment would require greater impact analysis for the interim financial reporting of March 2020. The financial statements adjustments and disclosures may be required for material uncertainties.

In accordance with IAS 34, *Interim Financial Reporting*, there might be greater use of estimates in interim financial statements. In the context of current economic conditions, use of estimates is expected to become more significant in the interim financial statements.

The recognition and measurement implications of COVID-19 pandemic applicable in case of annual financial statements (covered in previous sections) are equally relevant to the interim financial statements.

Interim financial information usually updates the information in the annual financial statements. However, IAS 34 requires that a company shall include in its interim financial report an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the company since the end of the last annual reporting period. This implies that additional disclosure should be given to reflect the financial impact of the virus and the measures taken to contain it. This disclosure should be company specific and should reflect each company's circumstances.

Where significant, the disclosures required by paragraph 15B in IAS 34 should be included, together with:

- Significant events or transactions during the interim period;
- the impact on the results, balance sheet and cash flows of the virus and the steps taken to control the spread;
- significant judgements that were not required previously, for example in connection with expected credit losses;
- updates to the disclosures of significant estimates.

The image shows a vast number of empty blue stadium seats, arranged in neat rows that recede into the distance. The perspective is from a low angle, looking down the length of the seating area. The seats are a vibrant blue color. A thin white rectangular border is superimposed over the middle section of the image, framing the text.

**Industry specific
considerations**

Industry Specific Considerations

The disruptions caused by COVID-19 and measures taken to prevent its spread both in Pakistan and internationally have impacted every industry.

The economic effects of the pandemic and resulting societal changes are currently not predictable. Going forward, the COVID-19 could effect additional areas of business and the financial impacts could vary from this seen and anticipated today. There are a number of uncertainties that could impact the results of operations, cashflows and financial position. Some of the variables include the effectiveness of COVID-19 mitigating measures, the duration of the pandemic, global economic conditions, changes to consumer confidence, behaviors and spending, work from home trends, and the sustainability of supply chains.

This section discusses industry-specific key accounting and financial reporting points emanating from the impact of the COVID-19 on the following industries:

- Oil and Gas
- Banking sector
- Travel and Transportation
- Hospitality
- Retail
- Manufacturing

Oil and Gas	
The oil and gas industry has been hit particularly hard with the fallout from COVID-19 and price of oil and gas. The oil prices have declined significantly post December 2019, primarily due to oversupply and by the adverse economic impacts of COVID-19. The expected economic downturn will further put pressure on the industry.	
Key accounting considerations include:	
Impairment of oil and gas assets	<p>The up-stream oil and gas companies apply either successful efforts or full cost method for the recognition and measurement, including impairment of oil and gas assets.</p> <p>Companies that are using “successful efforts” accounting should consider if the decline in oil prices is an indicator of impairment.</p>
Impairment of property, plant and equipment	<p>The downstream and oil marketing companies due to COVID-19 have been adversely impacted due to decrease in the oil demand.</p> <p>These companies should consider how a reduction in upstream activity may affect their operations and associated accounting. For example, considerations may include the impairment of property, plant and equipment.</p>
Liquidity	<p>The oil industry is typically capital intensive by nature, that is, it demands great amount of resources in order to build its assets and have oil and gas fields in productive conditions.</p> <p>The reduction in oil prices along-with the circular debt situation may impact liquidity and financing arrangements. Further, due to financial constraints, companies would be forced to delay expansion plans and lower capital expenditures to preserve liquidity.</p>

Banking sector

Banking and finance industry will need to consider the impact of COVID-19 as they are most likely to be impacted by the downturn in the stock market and economic disruption. The decline in credit quality and unexpected drop in demand for financing along-with travel restrictions are posing operational and financial challenges for the banking sector.

Further, the announcements of government programs to stimulate the economy, including supporting the banks and other industries may also affect financial position and results of this sector.

Key accounting considerations include:

Impairment of credit portfolio (Non-performing advances)	<p>The forced shutdown and economic uncertainty will increase the credit risk of borrowers. Especially small and medium enterprises, are at risk due to the forced shutdown. The delays and defaults of loan portfolios are expected to increase the loan loss allowances. Further, the impaired portfolio will also negatively impact earnings (i.e. interest income).</p> <p>Further, greater number of loan arrangements are expected to be restructured.</p> <p>Banks and DFIs should consider the impact of these factors to determine the impairment of loan portfolio, under the Prudential Regulations,</p> <p>Further, for the implementation of IFRS 9, the SBP shared timelines and milestones also need consideration. In particular the current environment would make the application of forward-looking Expected Credit Loss (ECL) model (for Performa financial statements) more challenging. The application of ECL would require more resources to assess the impact of changing market conditions.</p> <p>The present adverse factors could also impact the transition to IFRS 9 on January 01, 2021.</p>
Valuation of investment portfolio	<p>Global as well as Pakistan stock market witnessed significant decline in the first quarter of 2020.</p> <p>The stock market volatility and declining share prices will adversely affect the valuation of the investment portfolio and profitability.</p> <p>Banks and DFIs should consider the implications of decreasing share prices on the investments as well the potential impairment of Available for Sale equity securities due to significant or prolonged decline.</p>
Debt restructuring and forbearance	<p>To help borrowers cope with the financial consequences of COVID-19, banks and governments may announce various types of relief programmes that involve payment holidays. These may include blanket moratoriums on debt payments for all borrowers in a certain class or case-by case basis relief.</p> <p>Banks shall consider the accounting implications of these restructurings and reliefs, such as their impact on interest income recognition and loan loss provisioning.</p>
Liquidity	<p>The liquidity position could be stressed as a ramification of delayed recoveries or defaults.</p> <p>Banks/DFIs should continuously monitor and reassess the liquidity position in light of the latest information and market conditions.</p>
Capital management	<p>The risk-weighted assets may be impacted by increased volatility levels and higher counterparty risks.</p> <p>Increase in loan loss provisions, along with a decline in revenue, will negatively impact the profitability, leading to a deterioration of capitalisation. The capital-adequacy could be impacted due to these factors.</p>

Travel and transportation

The implications of COVID-19 on the travel and transportation industry are unexpected and unprecedented. In this sector, airlines are most badly affected. The governmental and business travel restrictions and declining consumer and business demand for air travel has completely grounded the airlines. Passenger ground transportation businesses and shipping business are also affected by COVID-19.

The International Air Transport Association (IATA) released updated analysis shows that the COVID-19 crisis will see airline passenger revenues drop by \$314 billion in 2020, a 55% decline compared to 2019. While full-year passenger demand (domestic and international) is expected to be down 48% compared to 2019.

Key accounting considerations include:

Going concern and liquidity	<p>The loss of traffic due to travel restrictions, along-with uncertainty about easing of these restrictions by governments and expectedly significant lower demand could impact the ability of airlines to continue their operations. The liquidity crunch due to decreased revenue and possible breaches of contractual terms will also add to the going concern issue.</p> <p>Assessment of airlines and other transportation companies' ability to continue for the foreseeable future shall be carried out on the basis of available information and evolving conditions.</p>
Impairment of non-financial assets (including right-of use assets)	<p>Present market conditions and adverse future outlook may indicate challenges in recovering assets through normal use. Significant reductions in aircrafts utilization, idling of aircrafts, and profitability challenges along-with other external factors indicate a need to assess the recoverability of latest carrying amounts of the aircrafts, goodwill and other intangibles.</p> <p>These indicators trigger the requirement to test impairment of non-financial assets.</p>
Restructuring provisions	<p>In response to COVID-19 airlines may consider restructuring activities such as closure of business location or laying-off of employees. These shall be considered in accordance with the IAS 37 and IAS 19.</p>
Revenue recognition	<p>Airlines could be offering incentives such as waiver of cancellation charges, new customer loyalty programs etc. Airlines shall consider the impact of these changes on the revenue recognition. Further, enforceability of contractual arrangements due to currently enforced restrictions and collectability assessment of customer shall also be carried out.</p> <p>The shipping companies shall evaluate the timing of revenue recognition since product delays, crewing issues, or delays at ports may require re-evaluation of the voyage time (which affects revenue recognition).</p>

Hospitality

Hospitality is one of the hardest hit due to fears of community spread through travel and group environments. Hotels and restaurants are experiencing business challenges in the face of declining consumer demand and both mandatory and voluntary property closures. The declines in revenue and demand could be prolonged.

Key accounting considerations include:

Going concern and liquidity

Companies will be impacted by liquidity crunch and going-concern related uncertainties, resulting from declining revenues.

The hotel industry is facing significant decline in revenue due to lower occupancy and declining price. Restaurants are also either closed or operating with very low demand. While on cost side, hospitality sector is incurring additional costs due to COVID-19 (such as sanitization, screening), in addition to the expenditures related to cancellations of entertainment and convention events, and payroll and legal costs. These conditions pose significant challenges related to liquidity, covenant compliance and going-concern issues.

Assessment of companies ability to continue for the foreseeable future shall be carried out on the basis of available information and evolving conditions.

Impairment of hotel properties

Lower occupancy and significantly reduced customer demand indicate triggering events for impairment testing.

The hotels as well as restaurants shall assess the recoverability of long-lived assets.

Revenue recognition

Evaluation of revenue recognition related to changes in cancellation policies, stand-alone selling prices for complimentary rooms, and management company agreements that include incentive fees and the achievability of those targets.

Retail sector

The retail sector is impacted negatively due to early closing hours, along-with disruptions in the supply chain. Further, workforce availability is also a challenge. The larger retailers might be witnessing increased customer traffic, however, a significant number of retailers are adversely impacted by the lockdown measures.

Key accounting considerations include:

Valuation of inventory

Inventory obsolescence shall be considered, if retailer will not be able to sell merchandise.

Lease rentals

Retailers shall consider the impact of rent concessions (if provided in the lease agreement or allowed by the lessor).

Penalties

Penalties for any order cancellations, to the extent applicable.

Liquidity and financing

Liquidity and financing considerations related to servicing debt obligations and covenant compliance, including the assessment of going concern, if revenue declines are significant.

Manufacturing sector

Manufacturing sector is facing challenges of workforce availability, supply chain disruptions and decreased customer demand. Due to lockdown and travel restrictions the manufacturing activity contracted sharply as many manufacturers have temporarily closed their manufacturing plants.

Key accounting considerations include:

Going concern and liquidity	<p>The manufacturing industry, compared to other industries is more impacted by workforce shortages, as bulk of its workforce is required on-site for the production related activities. Further, uncertainty about easement of restrictions across the globe poses the risk of prolonged supply chain disruptions (The impact would be more profound for companies having business relationships with counter parties in Europe and America. While could be less in case of suppliers from China).</p> <p>Therefore, companies due to workforce shortages, unavailability of supplies and decline in customer demand and revenue, might face liquidity strain and going-concern related uncertainties.</p> <p>An assessment of ability to continue as a going concern should be performed in light of current economic conditions and changing circumstances.</p>
Impairment of non-financial assets (i.e. recoverability of property, plant and equipment)	<p>The consumer demand is low, resulting in decline in revenue and gross margin. Considering these factors along with possible decline in the stock prices, companies need to consider the impairment indicators and perform impairment testing accordingly.</p>
Inventory valuation	<p>The reduced business activity and less than normal customer demand, may require estimation of net realisable value of inventory. Further, the periods of significantly low production may impact inventory costing.</p>
Restructuring provisions and Discontinued operations	<p>Companies may plan restructuring activities such as closure of business location or termination of employees. A restructuring provision for restructuring activities is recognised only when the specified conditions are met as mentioned. The operating results of the part of business planned to be closed under a restructuring plan as a result of economic downturn from COVID-19 pandemic may qualify to be presented as discontinued operations.</p>
Revenue recognition	<p>The revenue recognition may involve variable consideration (rebates, discounts) allowed to customers based on the estimated activity levels. The changes in customers demand will require companies to consider their impact on revenue recognition. Further, the enforceability of revenue contracts as well as the customer ability to make payment against delivered goods shall also be considered. The significant extension in credit terms could result in significant financing component.</p> <p>Companies shall consider the impact of these factors along with the impact of order cancellations of revenue recognition.</p>
Penalties	<p>The unfulfilled orders may attract penalties and fines under the contractual terms. Appropriate accounting of these amounts shall be considered based on the enforceable contractual arrangements and mutual understanding.</p>



Regulatory Reliefs

Regulatory Reliefs

Governments and regulators are taking unprecedented measures so that the temporary lockdowns required to slow the spread of the virus does not disrupt the economy permanently.

In context of financial reporting and areas which may impact the financial statements, the SECP and SBP have provided guidance and offered companies regulatory reliefs. The significant financial reporting related reliefs are listed below:

Relief granted by SECP	Brief discussion of the relief
SECP provides relaxation from certain provisions of Companies Act, 2017	<p>SECP, through, Circular No.10 of 2020 (dated April 1, 2020) and Circular No. 06 of 2020 (dated March 22, 2020) provided the following regulatory reliefs for compliance with the requirement of the Act:</p> <p>General Relaxation in Holding AGM and filing deadline for first quarter financial statements General extension for a period of 30 days in holding the annual general meeting (AGM) has been granted. The companies can now hold their AGM for the year ended on December 31, 2019 on or before May 29, 2020. Further SECP shall also facilitate for grant of extension in filing first quarter financial statements on application sent to SECP via email.</p> <p>Relaxation in holding election of directors The companies, whose election of directors is due before or in the AGM for year ended December 31, 2019, may file impediment reports with the concerned registrar citing the reasons for delay in holding the election of directors.</p> <p>Relaxation in filing statutory returns Statutory return required to be filed on or after March 24, 2020 may be filed with the concerned registrar with the delay of 30 days of occurrence of any event without any additional filing fee as no penal action shall be taken for the late filing.</p> <p>Circulars can be accessed on following links https://www.secp.gov.pk/document/circular-no-6-of-2020-relaxation-from-certain-provisions-of-companies-act-2017-due-to-covid-19/?wpdmdl=38830&refresh=5e8c4a02230a11586252290 https://www.secp.gov.pk/document/circular-10-of-2020-regulatory-relief-for-corporate-sector-to-dilute-covid-19-impact/?wpdmdl=38897&refresh=5e93dea2cc5361586749090</p>
SECP defers the effective date of IFRS 9 for NBFCs	<p>SECP, through, S.R.O. 273 (I)/2020 (dated March 30, 2020) has deferred the effective date of IFRS 9 for NBFCs.</p> <p>NBFCs previously were required to apply IFRS-9 for reporting period/year ending on or after June 30, 2020. Now IFRS 9 for NBFCs shall be applicable for reporting period/year ending on or after June 30, 2021 (earlier application is permitted).</p> <p>S.R.O. can be accessed on following link https://www.secp.gov.pk/document/sro-273i-2020-change-in-the-effective-date-of-ifrs-9/?wpdmdl=38900&refresh=5e8aa6034e6a81586144771</p>

Relief granted by SECP	Brief discussion of the relief
<p>SECP grants relaxation from IFRS 9, for fair value remeasurement of equity instruments in the statement of profit or loss</p>	<p>SECP, through S.R.O. 278 (I)/2020 (dated April 1, 2020) has allowed all companies, relief from the requirements of recording fair value adjustments of equity instruments held as FVPL (Fair Value through Profit or Loss) in the statement of profit or loss, as at March 31, 2020 as contained in IFRS 9. Similar exemption would be available to the same instruments accounted for under IAS 39, IFRS for SMEs and AFRS for SSEs.</p> <p>Under this relaxation companies can opt to recognise:</p> <ul style="list-style-type: none"> ▪ Gain/loss due to fair value measurement of FVPL equity instruments, held as at March 31, 2020 in the Statement of Changes in Equity, as a separate component of equity; ▪ The amount taken to equity as per (i) above, including any adjustment/effect for price movements shall be taken to the Statement of Profit or Loss for the year/period ending June 30, 2020; and ▪ The amount of loss taken to equity as per (i) above, shall be treated as a charge to statement of profit or loss for the purposes of distribution as dividend, where applicable. <p>S.R.O. can be accessed on following link https://www.secp.gov.pk/document/s-r-o-278-i-2020-relief-from-requirements-contained-in-ifs-9/?wpdmdl=38929&refresh=5e8c1f537f3821586241363</p>
<p>SECP grants relaxation to Lending NBFC from Restructuring/ Rescheduling of facilities</p>	<p>SECP, through circular No. 9 of 2020 (dated March 31, 2020) in order to facilitate the lending non-bank finance sector owing to outbreak of COVID-19 allowed the following relaxations to all lending NBFCs including Non-Banking Micro Finance Companies (NBMFCs):</p> <ul style="list-style-type: none"> ▪ NBFC may defer the repayment of principal loan amount for one year on written request of borrower received before June 30, 2020 provided that markup will continue to be paid as per agreed terms and such deferment will not be reported as restructuring in ECIB; ▪ Where such borrower is unable to service markup amount or need deferment exceeding one year, facilities may be rescheduled/ restructured upon their request. If the rescheduling/ restructuring is done within 90 days of loans being overdue in case of microfinance and 180 days in any other finance facility. Such facilities will continue to be treated as regular and reported in the ECIB accordingly; and ▪ NBFC shall not classify the financing facilities of such borrower who have requested deferment or rescheduling/ restructuring as mentioned above. <p>Circular can be accessed on following link https://www.secp.gov.pk/document/circular-no-9-of-2020-relaxation-to-lending-nbfc-under-regulation-67a/?wpdmdl=38893&refresh=5e8c4a021f1231586252290</p>

Relief granted by SECP	Brief discussion of the relief
<p>SECP grants relaxation from certain provisions of NBFC Regulations, 2008</p>	<p>SECP, through, Circular No. 16 of 2020 (dated April 21, 2020), allowed following relaxations to asset management companies in relation to compliance with certain requirements of the <i>Non-Banking Finance Companies and Notified Entities (NBFC) Regulations, 2008</i>:</p> <ul style="list-style-type: none"> ▪ The time period for submission of quarterly financial statements of Open End Schemes and Closed End Schemes for the quarter ended on March 31, 2020 under Regulation 38(2)(f) of the NBFC Regulations is extended by 30 days i.e. till May 31, 2020; ▪ Time to ensure compliance with minimum fund size for Open End Schemes under Regulation 54(3b) of the NBFC Regulations, 2008 is increased to 180 days for Open End Schemes currently non-compliant with minimum fund size requirement and Open End Schemes that may become non-compliant within next 90 days of issuance of this circular. <p>The Circular can be accessed on following link https://www.secp.gov.pk/document/circular-no-16-of-2020-relaxations-from-certain-provisions-of-nbfc-regulations-2008/?wpdmdl=39123&refresh=5e9fe9a534bd91587538341</p>
<p>SECP directs preventative measures against COVID-19 in relation to inspection of companies documents and obtaining certified copies</p>	<p>SECP, through Circular No. 17 of 2020 (dated April 20, 2020), announced following measures in relation to inspection of companies documents and obtaining certified copies, for ease and facilitation of the public:</p> <ul style="list-style-type: none"> ▪ Inspection of documents/record of companies as provided in regulation 19 of the Company (Registration Offices) Regulations, 2018 has been allowed. However, prior appointment shall be obtained via email or phone call to the respective CRO providing name of the company and intended date of visit. CRO in charge shall allow inspection ensuring adequate health security measures. ▪ Certified copies of returns can be issued and collected from the respective CRO within two working days and in case not collected within the prescribed time, the same shall be sent via courier. <p>Circular can be accessed on following link https://www.secp.gov.pk/document/circular-17-of-2020-preventive-measures-against-covid-19/?wpdmdl=39124&refresh=5e9fe9a5371221587538341</p>

Relief granted by SBP	Brief discussion of the relief						
SBP grants relaxation by allowing phased recognition of impairment loss of Available for Sale (AFS) Investments	<p>SBP, through, BPRD Circular Letter No. 13 of 2020 (dated March 26, 2020), while providing various regulatory reliefs to Banks/DFIs, has also provided relaxation to banks and DFIs from recognising impairment loss of AFS in a phased manner.</p> <p>Under this relief Banks/DFIs may opt to recognise impairment loss if any, resulting from the remeasurement of listed equity shares held as AFS, equally in quarterly basis during calendar year ending December 31, 2020.</p> <p>Circular can be accessed on following link http://www.sbp.org.pk/bprd/2020/CL13.htm </p>						
SBP extends timeline related to International Financial Reporting Standard 9	<p>SBP, through, BPRD Circular No. 04 of 2019 had notified IFRS 9 to be applicable to the banks/DFIs effective from January 01, 2021. Under this circular, SBP also directed banks/DFIs to prepare pro forma financial statements for year 2019 and ensure parallel run of IFRS 9, as per specified timelines.</p> <p>In this regard SBP, through, BPRD Circular Letter No. 15 of 2020 (dated March 26, 2020) keeping in view of the COVID-19 pandemic situation has extended the timeline of the following milestones related to IFRS 9 implementation:</p> <table data-bbox="428 907 1308 1141"> <thead> <tr> <th>Particulars</th><th>Timelines</th></tr> </thead> <tbody> <tr> <td>Preparation of IFRS 9 compatible pro forma Financial Statements for year-ended 2019</td><td>Aug 31, 2020</td></tr> <tr> <td>Parallel Run of IFRS 9</td><td>Periods beginning July 1, 2020</td></tr> </tbody> </table> <p>Circular can be accessed on following link http://www.sbp.org.pk/bprd/2020/CL15.htm </p>	Particulars	Timelines	Preparation of IFRS 9 compatible pro forma Financial Statements for year-ended 2019	Aug 31, 2020	Parallel Run of IFRS 9	Periods beginning July 1, 2020
Particulars	Timelines						
Preparation of IFRS 9 compatible pro forma Financial Statements for year-ended 2019	Aug 31, 2020						
Parallel Run of IFRS 9	Periods beginning July 1, 2020						
SBP relaxes Capital Conservative Buffer and Retail Portfolio Limit	<p>SBP vide BPRD Circular Letter No. 12 of 2020 (dated March 26, 2020) to facilitate the banks/DFIs to continue providing financing facilities to their customers implemented the following relaxations from Basel Capital Adequacy measures with immediate effect:</p> <ul style="list-style-type: none"> ▪ The Capital Conservation Buffer has been reduced, for the time being, from its existing level of 2.50% to 1.50%, till further instructions. ▪ The existing regulatory retail portfolio limit of Rs. 125 million has been enhanced to Rs. 180 million. <p>Circular can be accessed on following link http://www.sbp.org.pk/bprd/2020/CL12.htm </p>						

Relief granted by SBP	Brief discussion of the relief
<p>SBP grants relief in the Prudential Regulations for SMEs Financing/ Corporate / Commercial Banking/ Consumer Financing</p>	<p>SBP, through, IH&SMEFD Circular Letter No. 3, 4 and 5 of 2020 and BPRD Circular Letter No. 13 and 14 of 2020 (dated March 26, 2020) provided following common relief to banks/ DFIs to dampen the adverse effects of COVID-19:</p> <p>(i) Relaxation from Restructuring/ Rescheduling of financing facilities to SMEs, Housing Sector, Corporate and Consumer</p> <p>Banks/ DFIs may defer the repayment of principal loan amount for one year on written request of borrower received before June 30, 2020 provided that markup will continue to be paid as per agreed terms and such deferment will not be reported as restructuring in ECIB;</p> <p>Where such borrower unable to service markup amount or need deferment exceeding one year, facilities may be rescheduled/ restructured upon their request. If the rescheduling/ restructuring is done up to 180 days, such facilities will continue to be treated as regular and reported in the ECIB accordingly; and</p> <p>Banks/ DFIs shall not classify the financing facilities of such borrower who have requested deferment or rescheduling/ restructuring as mentioned above.</p> <p>Financing under SBP refinance schemes along with their respective Shariah compliant alternative schemes are also allowed above relaxations from Restructuring/ Rescheduling.</p> <p>Further following other reliefs are also allowed from Prudential Regulations for Corporate / Commercial Banking:</p> <p>(ii) Relaxation under Margin Requirement regulation</p> <p>The margin requirement from 30 percent to 20 percent and margin calls from 30 percent to 10 percent for exposure against shares of listed companies;</p> <p>(iii) Relaxation under Impairment in Value of Securities regulation</p> <p>Impairment losses from valuation of listed equity securities classified as available for sale can be recognised in phased manner equally on quarterly basis during calendar year ending 31 Dec 2020;</p> <p>(iv) Relaxation under Financing against Shares / TFCs / Sukuk regulation</p> <p>Banks/DFIs are permitted to take exposure on any person against the shares issued by its group companies, provided the tenor of the financing facilities do not exceed one year; and</p> <p>(v) Relaxation under Classification of Loans and Advances regulation</p> <p>The criteria for classification of "Trade Bills" have been relaxed by six months. The Banks/DFIs shall classify the "Trade Bills" as "Loss" when the payment obligation is not repaid / adjusted within 365 days of the due date.</p> <p>Circular can be accessed on following link: http://www.sbp.org.pk/sme fd/circulars/2020/CL3.htm http://www.sbp.org.pk/sme fd/circulars/2020/CL4.htm http://www.sbp.org.pk/bprd/2020/CL13.htm http://www.sbp.org.pk/bprd/2020/CL14.htm http://www.sbp.org.pk/sme fd/circulars/2020/CL5.htm</p>

Relief granted by SBP	Brief discussion of the relief
SBP instructs all Banks, DFIs and MFBs to suspend the payment of dividends for March and June, 2020 quarters	<p>SBP through Letter No. BPRD/BA & CPD/006315/20 (dated April 22, 2020) has instructed all the banks, DFIs and Micro-Finance Banks (MFBs) to suspend distribution of profits by way of declaring dividends in any manner (cash or stock) for the quarter ended March 31, 2020 and half year ending June 30, 2020. However, this instruction will not be applicable on dividend declared for the year ended December 2019.</p> <p>The aim of this instruction is to conserve the capital and further enhance the lending and loss absorption capacity of banks, DFIs and MFBs.</p> <p>SBP has directed the board of directors of all banks, DFIs and MFBs have been directed to take note of this instruction. However, if board of directors considers it necessary to declare the dividend in wake of the institution’s specific circumstances, it may approach SBP with sound justification for consideration of request on merit. The SBP will review the above instructions on distribution of dividends after June 30, 2020, keeping in view the severity and impact of the COVID-19 and the economic dynamics on the safety and soundness of the banking system.</p>