

The Financial reporting implications of COVID-19

3 April 2020

By the KPMG Mantra editorial team

Like all other aspects of a company's operations, financial reporting for the period ended 31 March 2020 will be significantly impacted by the global fallout from the COVID-19 pandemic.

At a fundamental level, for certain companies, the current situation casts significant doubt on their ability to continue as a going concern, particularly if large debt repayments are due within the next 12 months. Management would need to prepare detailed assessments to support the going concern assumption. These assessments may be difficult to make given the high levels of uncertainty. In certain cases, this may require disclosure in the financial statements, and even in the auditor's report.

Another area involving significant judgment and estimates is the recognition of impairment, which is generally based on forecasted cash flows to be generated from the use of certain asset groups. Companies would need to critically evaluate and revise their previous cash flow estimates to determine any impairment losses to be recorded for plant & machinery, intangibles, strategic investments and goodwill from acquisitions. Similarly, given that realisable value of the company's inventory may have reduced, there may be a need to write-down inventory.

Issues may also arise in areas relating to revenues. At the basic level, companies would need to determine whether the conditions for revenue recognition have been met for goods that may have been dispatched, but not delivered to the customer. Companies would also need to determine whether they may have breached any obligations to deliver under their contractual arrangements, and whether any provisions need to be established for penalties. Further, companies are now required to record their provision for bad debts based on what is called the Expected Credit Losses (ECL) model. These models have been constructed based on the company's historical experience, which may not be representative of future expectations of bad debts. In such cases, the ECL model would need to be appropriately updated.

Even as companies deal with the above issues, they need to determine whether their period-end financial reporting processes are geared to operate in the current 'work from home' environment. This environment may severely impact the company's ability to prepare its financial statements and get them audited per original timelines. In several cases, companies may need to defer the dates of their Board meetings to consider the audited financial results. Acknowledging this, the Securities and Exchange Board of India has already deferred the timelines for year-end financial results of listed companies by 45 days to 30 June 2020. Additionally, the work from home environment may impact the efficacy of certain internal controls set up by the company, and thereby expose the company to risks of fraudulent financial reporting.

Given the uncertainties involved, it is important that 'C' level executives communicate regularly with all stakeholders, including the Audit Committees and the auditors. Companies should expect a greater level of challenge from these stakeholders. This challenge is essential to ensure that the financial statements

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. The KPMG name and logo are registered trademarks or trademarks of KPMG International.

accurately capture the impact of various risks and uncertainties involved. In certain cases, auditors may not be able to perform mandated audit procedures such as year-end inventory counts, which may result in qualifications in the auditor's report.

The impact of COVID-19 reporting is not restricted only to the audited financial statements. While preparing their annual reports and investor presentations, companies would need to ensure that their Management Discussion & Analysis, risk management disclosures and investor decks are also suitably updated.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. The KPMG name and logo are registered trademarks or trademarks of KPMG International.