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Where and how should COVID-19 impacts be presented in the income statement and related notes?

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What's the issue?

The COVID-19 coronavirus pandemic has affected and continues to affect the financial performance of many companies. Companies may intend to highlight and explain these impacts – i.e. by including quantitative and qualitative information about them either inside or outside the financial statements.

We focus here primarily on how companies might present these impacts on financial performance in the income statement. We highlight specific matters that, in our view, companies should consider when determining how to present and disclose them in their income statement and related notes.

How a company reflects the impacts of COVID-19 in the income statement will depend on its specific facts and circumstances, including the nature and extent of those impacts on the company and the company's ability to determine the impacts on a non-arbitrary basis – i.e. to quantify them reliably.

Getting into more detail

Determining where to present COVID-19 impacts in the financial statements

Under IAS 1 *Presentation of Financial Statements*, when items of income or expense are material, a company discloses their nature and amount separately, either on the face of the income statement or in the notes. *[IAS 1.97]*

Whether a company presents its COVID-19 impacts on the face of the income statement or discloses them in the notes will depend on:

– the pervasiveness of those impacts on the company; and

– its ability to determine them on a non-arbitrary basis.

Determining the impacts of COVID-19 on a non-arbitrary basis may be challenging because distinguishing between income and expenses that are part of normal operations and those that relate to the pandemic may involve significant subjectivity. Companies need to assess carefully whether they are able to determine COVID-19 impacts on a non-arbitrary basis, in order to provide relevant and reliable information to users of their financial statements.

In some cases, the company may be able to determine the impacts of COVID-19 but finds that they are pervasive – e.g. it affects nearly all line items. In these cases, it may be less meaningful to present the impacts separately in the income statement. Instead, it may be appropriate to disclose them in the notes.

In other cases, the impacts of COVID-19 may be so pervasive that the company is unable to determine the overall impacts of COVID-19 on a non-arbitrary basis. In these circumstances, we believe that the company should not present them in

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the income statement. Instead, it should consider disclosing them in the notes, providing quantitative (when possible) and qualitative information and stating whether it has identified only some or all of the impacts.

A company needs to ensure that its chosen presentation is not misleading and is relevant to the users' understanding of its financial statements. For example, it would be inappropriate to present or disclose only the expenses relating to COVID-19 – and omit the related income – if both income and expenses are affected. *[Insights 4.1.20.40]*

Companies should also consider any relevant regulatory guidance on the presentation and disclosure of COVID-19 impacts in the financial statements. For example, in a **public statement** the European regulator, ESMA[1], called for caution regarding any separate presentation of the impacts in the income statement because of their pervasiveness. It encouraged issuers to provide quantitative information on the impacts in the notes.

Determining COVID-19-related income and expenses

When determining the impacts of COVID-19, we believe that a company should consider as COVID-19-related only the income and expenses that are **incremental and directly attributable** to COVID-19. These are income and expenses that would not have been earned or incurred if the COVID-19 pandemic had not occurred and are not expected to recur once the effects have largely receded.

Recurring income and expenses that would be earned or incurred regardless of COVID-19 are not incremental. Therefore, we believe that these are not considered as income or expenses relating to COVID-19 and should not be described as such in the income statement. For example:

– payroll for idle employees;

– depreciation of plant facilities when production is suspended; and

– rent and utility costs incurred during temporary closures.

However, companies may disclose additional information in the notes about COVID-19's impacts on their financial performance provided that the information is useful to users' understanding and not misleading. See below for a discussion on labelling COVID-19-related income and expenses as 'unusual' or 'exceptional'.

Determining the amounts of incremental income and expenses directly attributable to COVID-19 will require judgement, the level of which will depend on the specific facts and circumstances and disclosure to this effect may be necessary.

Certain types of income and expenses can be more easily determinable as relating to COVID-19. For example:

– additional cleaning and sanitation costs incurred as part of infection control or prevention;

– temporary hazard pay to employees;

– penalties for delays or non-performance of contracts due to closure of production facilities; and

– **rent concessions** from lessors that occur as a direct consequence of COVID-19.

For other types, it may be challenging to determine whether and to what extent they were driven by COVID-19 or other factors – e.g. expected credit losses, impairment loss on non-financial assets and fair value loss on equity investments. Overall, the key is whether a company can determine the incremental income and expense on a non-arbitrary basis. If this is not possible, then the company considers disclosing additional information in the notes.

1 European Securities and Markets Authority

Labelling COVID-19-related income and expenses as 'unusual' or 'exceptional'

IFRS® Standards do not prohibit companies from presenting unusual or exceptional items. However, companies are not allowed to describe such items as 'extraordinary'. *[IAS 1.87, Insights 4.1.100.10]*

The terms 'unusual' and 'exceptional' are not defined in the Standards. In our view, if the description 'unusual' or 'exceptional' is used, then its use should be infrequent and reserved for items that justify a prominence greater than that achieved by separate presentation or disclosure. *[Insights 4.1.100.30]*

We believe that it may be appropriate to label COVID-19-related income and expenses as 'unusual' or 'exceptional'. Consistent with the approach of identifying COVID-19 related income and expenses, we believe that only incremental income and expenses directly attributable to COVID-19 could be labelled this way.

However, as companies adapt their businesses to the realities of COVID-19, what may have been assessed as unusual in 2020 may now be viewed as the new normal. As such, it may be more difficult to identify on a non-arbitrary basis items that warrant separate presentation or disclosure and can be labelled as unusual.

If a company labels income and expenses that relate to COVID-19 as 'unusual' or 'exceptional', then it uses the term consistently and describes the term in the notes to provide clarity for the users of financial statements. *[Insights 4.1.100.60]*

If an item of expense is labelled as 'exceptional' or 'unusual', then in our view the description used by the company should include the nature of the item – e.g. exceptional cleaning costs due to COVID-19. We believe that describing an item simply as 'exceptional' or 'unusual' does not meet the requirement for amounts to be classified by their nature or function (see below). Similarly, we believe that merely describing an income or expense item as 'COVID-19-related' is insufficient: the nature of the item should also be provided – e.g. COVID-19-related cleaning costs. The notes to the financial statements should also include an additional explanation of the nature of the amount and its characterisation as 'exceptional' or 'unusual' or 'COVID-19-related'. *[Insights 4.1.100.40]*

Presentation of COVID-19-related expenses will depend on the current structure of income statement

If a company determines that presenting COVID-19 impacts in the income statement is appropriate, then it considers how this would fit into the current structure of the income statement – in particular, the classification of expenses.

Under IAS 1, expenses are classified according to either their function (e.g. cost of sales, distribution, administration) or their nature (e.g. staff costs, depreciation, amortisation). This analysis may be presented either in the income statement or in the notes. The chosen classification is generally applied consistently from one period to the next. *[IAS 1.99–105, Insights 4.1.20–40]*

When a company presents the analysis of expenses in the income statement rather than in the notes, in our view the amount of expenses described as 'COVID-19-related' should be classified by function or nature, in the same way as expenses that do not relate to COVID-19. *[Insights 4.1.100.50]*.

Consequently, we believe that it may be inappropriate to present a single line item for the total amount of expenses relating to COVID-19 in the income statement when it affects a company's expenses across different natures or functions.

Example – Presentation in the income statement when expenses are classified by nature

We illustrate below how a company that classifies expenses by nature might present its expenses relating to COVID-19 in the income statement – using parentheses and subtotals.

Approach 1 – Use of parentheses

Example income statement

	20XX
Revenue	1,000
Other income (including **insurance recoveries from COVID-19 related claims** of 40)	150
Changes in inventories of finished goods and work in progress	(120)
Raw material and consumables used	(160)
Employee benefit expense (including **temporary hazard pay to employees due to COVID-19** of 70)	(250)
Depreciation and amortisation expense	(100)
Other expenses (including **cleaning and sanitation costs incurred to prevent the spread of COVID-19** of 30)	(80)
Profit before income tax	440

Approach 2 – Use of subtotals

Example income statement

		20XX
Revenue		1,000
Other income		
Insurance recoveries from COVID-19 related claims	40	
Other	110	
		150
Changes in inventories of finished goods and work in progress		(120)
Raw material and consumables used		(160)
Employee benefit expense		
Temporary hazard pay to employees due to COVID-19	(70)	
Other employee benefit expense	(180)	
		(250)
Depreciation and amortisation expense		(100)
Other expenses		
Cleaning and sanitation costs incurred to prevent the spread of COVID-19	(30)	
Other	(50)	
		(80)
Profit before income tax		440

COVID-19-related income and expenses inside or outside operating profit subtotal

When a company presents an operating profit subtotal in its income statement, it will need to consider whether it presents income and expenses relating to COVID-19 as part of this subtotal.

The Standards do not define the terms 'operating' and 'non-operating' in the context of the income statement. If a company presents an operating profit subtotal as an additional subtotal, then it should present it consistently from period to period. *[IAS 1.85A, Insights 4.1.120]*

It would be inappropriate to exclude items that clearly relate to operations – e.g. inventory write-downs and restructuring and relocation expenses – because they occur irregularly or infrequently, or are unusual in amount. *[IAS 1.BC56]*

Therefore, companies should not present COVID-19-related income and expenses outside operating results solely because they may be non-recurring or unusual. Instead, companies should apply the definition of 'operating' consistently to income and expenses regardless of whether they relate to COVID-19. For example, cleaning costs are generally part of operating activities and are therefore presented within operating results. As such, incremental cleaning costs incurred to prevent the spread of COVID-19 are also presented within operating results.

Including 'as if' measures or notional numbers in the financial statements

Hypothetical, 'as if' measures or notional numbers – e.g. those that reflect originally budgeted or normalised amounts – do not represent historical financial information and are generally not included in the financial statements. Therefore, it is inappropriate to present these items (e.g. 'expected revenue had the COVID-19 outbreak not happened') in the income statement. Similarly, presentation of 'lost revenues' is also inappropriate.

Companies may need to refer to relevant regulatory guidance when considering whether to include hypothetical or 'as if' measures in the notes to the financial statements. For example, a **public statement** issued by IOSCO[2] states that it would not be appropriate to characterise hypothetical sales and/or profit measures as non-GAAP financial measures.

Other considerations

If companies include information about the impacts of COVID-19 outside the financial statements, then they should consider any relevant regulatory guidance. IOSCO's **public statement** also stated the importance of transparent and complete disclosures about COVID-19 impacts in the financial statements as well as management commentary. ESMA also published a **Q&A** that provides guidance on the use of alternative performance measures (APMs) in the context of COVID-19[3].

Actions for management

As companies continue to assess the impacts of COVID-19 on their financial performance, management should also consider the following.

- Evaluate whether the company can determine income and expenses that relate to COVID-19 on a non-arbitrary basis.
- Consider how the presentation of determinable COVID-19 impacts would fit into the current structure of the income statement.

2 International Organisation of Securities Commissions
3 See Question 18 in the **Q&A**

– Determine the nature and extent of information to be given inside and outside the financial statements to supplement the information about the company's financial performance in the income statement.

References to 'Insights' mean our publication **Insights into IFRS®**

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