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The impact of covid-19 on the going concern assumption in preparation of financial statements under IASs

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Abstract: This study aims to highlight the most significant economic effects of the (Covid-19) on the sector of economic institutions and its impact on its ability to continue as a going concern, which is a fundamental principle that underlies the preparation of the financial statements under international accounting standards. Where the study reached several conclusions, the most important of which is the need to carefully consider the uncertainty considerations surrounding the institution's activity when assessing the appropriateness of the going concern assumption for preparing its financial statements**.**

Keywords: going concern; Uncertainty; accounting; institution; Covid-19.

JEL classifications codes: M41

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I- Introduction:

The World Health Organization declared Corona Virus (COVID-19) to be a public health emergency on January 30, 2020. As at March 31, 2020, almost the whole of world is in some state of lock down. The governments have implemented various measures to contain the spread of the COVID - 19, including restricting the flight operations at the airports, curtailing intercity movements through buses and trains, temporary closing of businesses, schools etc. Impacts such as business and production disruptions, supply-chain interruptions, volatility in the equity and debt markets, reduced revenue and cash flows and other economic consequences also have accounting and financial implications. This includes, but is not limited to, Impairment under IAS 36 “Impairment of Assets”, Financial Instruments, Classification of assets, Revenue Recognition, Leases, Associates and Joint Ventures, Inventory, Property Plant and Equipment, Government Assistance, Provisions under IAS 37, Onerous Contracts, Contingent Assets, Employee Benefits and Share Based Plans, Income Taxes, Events After Reporting Period, Liabilities from Insurance Contracts, Financial and non-financial statement disclosures, Interim Financial Statement. In addition to their responsibilities in respect of above, management and directors have an obligation in relation to going concern that arises under the Corporations Act, which requires companies to comply with accounting standards. Accounting standards require management to make an assessment of an entity’s ability to continue as a going concern and prepare financial statements on a going concern basis, unless management either intends to liquidate the entity, to cease trading or has no realistic alternative but to do so. In the face of continuing uncertainty around the progress of COVID-19 and what a recovery may look like, directors of many organisations are concerned about how their companies, registered schemes or disclosing entities (“the entity” or “entities”) will be affected in the short and medium term and what their obligations are under legal in relation to going concern. So, how the entity does consider the impact of coronavirus (‘COVID-19’) on assessment and disclosures relating to going concern and in financial statements?

The importance of the study:

- The COVID-19 crisis has increased the complexity surrounding organisations' accountability and governance. The wicked nature of the problems faced by society during the outbreak, their changing nature and their temporality have generated an increasing demand for more material (or even new) practices of account-giving to reflect the unprecedented magnitude of the outcomes;

- The financial reporting impacts of COVID-19 are as varied as the businesses that face them and have given rise to a number of significant economic challenges for entities operating in many industries and sectors. These impacts are likely to have a pervasive impact on the financial reports including going concern, requiring preparers and auditors to challenge underlying assumptions, judgements and disclosures that may not have been considered in detail in the recent past;

- Financial reports are prepared based on a number of fundamental principles and using a variety of assumptions. COVID-19 may impact the application of these fundamental principles and assumptions in ways that may never have been considered by the entity in the past;

- Financial statements are generally prepared under the assumption that the entity will remain a going concern;

- In these unprecedented times, understanding whether an entity is a going concern is a key concern for management, investors and auditors. Stakeholders want to understand how viable and resilient an entity is to current and future stresses;

- Going concern is one of some of the more common challenges that preparers may face when producing the financial report during the COVID-19 pandemic;

- True and fair accounts can help investors to assess the viability and resilience of a business – and thus make their own judgements about its prospects – based on sound information;

- The rigour that both preparers and auditors apply to making these tough judgements and detailed assessments will be crucial for businesses and economies at such a volatile time;
- While accounting research has developed and become more sophisticated, the challenges posed by the COVID-19 pandemic provides both a challenge and need for research in this area to become more impactful.

The Objectif of the study:

- Presentation of management responsibilities relative to the assessment of an entity's ability to continue as a going concern;
- Discuss the key aspects relating to going concern assessment;
- addressing the assessments that an entity should consider in connection with going concern;
- Provide some requirement of evaluating and disclosing going concern to help navigate this new environment;
- To help preparers of financial reports and auditors navigate the key considerations of going concern assessment. It seeks to be applicable for economic entities.

Methodology:

This topic was studied by following the descriptive approach to clarify the various concepts as well as the analytical approach in order to facilitate the full understanding of the topic by highlighting all its parts.

II-Indicators and risk to be considered in assessing going concern under covid-19

When assessing whether an entity is a going concern, directors can consider the indicators and risks set out (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24) in below:

1. The indicators

Companies, whose financial year end corresponds to December 31, must take into account the following aspects for the purpose of evaluating the correct treatment of COVID-19 in the financial statements in accordance with the financial reporting framework applicable: (Partner, 2020, p. 2)

- Management and those responsible for governance must evaluate the impact that COVID-19 is having on the business, considering certain factors such as liquidity plans, the breakdown of the supply chain or supply problems.

- Companies should also assess whether the impact of the Coronavirus may create material uncertainty about the operations of the society and the continuity of the society. When it affects the application of the going concern principle, the company must carry out an assessment of the factors that generate doubts regarding the application of the going concern principle and the mitigating factors.

Companies should consider the possible implications of COVID-19 and the measures taken to minimize such risks when assessing their ability to continue as a going concern. (Partner, 2020, p. 4)

Directors and managers will need to consider how COVID-19 has impacted their entities when preparing annual reports. Of course, many of these impacts may still be unresolved both at year-end date and date of publication of that report and may continue to impact the entity in the future. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 8)

The following is a list of questions to consider when assessing the impact of COVID-19. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 31)

This list is not intended to be exhaustive. It is based on a publication released by the U.S. Securities and Exchange Commission in March 2020. (The Australian Institute of Company Directors (AICD), Chartered

Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 31)

- In light of changing trends and the overall economic outlook, how do you expect COVID-19 to impact your future operating results and near-and-long-term financial results?

- Do you expect that COVID-19 will impact future operations differently than how it affected the current period?

- How has COVID-19 impacted your capital and financial resources, including your overall liquidity position and outlook?

- Does COVID-19 increase the risk of you breaching any debt covenants? What is the likelihood of that occurring? Have you undertaken any discussions with your lender about what would occur in those circumstances?

- How do you expect COVID-19 to affect assets on your balance sheet?

- What assumptions have you built into your assessment of impairment, in particular of non-current assets, intangibles, and goodwill? Will there be significant changes in judgements in determining the fair value of assets?

- Have there been increases in allowances for credit losses, restructuring charges, other expenses, or changes in accounting judgements that have had or are reasonably likely to have a material impact on your financial statements?

- Have COVID-19-related circumstances such as remote work arrangements adversely affected your ability to maintain operations? What if they were to recur or last for a lengthy period?

- Have you experienced challenges in implementing your business continuity plans or do you foresee requiring material expenditures to do so? Do you face any material resource constraints in implementing these plans?

- Do you expect COVID-19 to materially affect the demand for your products or services?

- Do you anticipate a material adverse impact of COVID-19 on your supply chain or the methods used to distribute your products or services? Do you expect the anticipated impact of COVID-19 to materially change the relationship between costs and revenues?

- Will your operations be materially impacted by any constraints or other impacts on your human capital resources and productivity?

- Are travel restrictions and border closures expected to have a material impact on your ability to operate and achieve your business goals? Is your entity exposed to material effect of COVID-19 in an overseas jurisdiction where you operate a business?

- Has COVID-19 had a significant material effect on a related business entity (e.g. a parent, subsidiary, joint venture) and what will the effect be on your entity's financial and operational circumstances?

- Have you considered the possibility of contract modifications from customers and its effects on revenue?

- How reliant are you on continuing government support for your operation e.g. Jobkeeper? How vulnerable are you to sudden changes in government policy such as withdrawing that support?

- Have you undertaken any scenario analysis for different possibilities facing your business? What does this tell you about your assumptions around going concern?

The degree of consideration by the entity in its going concern assessment will depend on its own facts and circumstances. (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)

Accounting standards do not set out indicators or circumstances where a detailed review of the going concern assumption may be necessary. It is up to the entity to determine where these might exist. In the current environment, management might need to consider a wide range of factors before it can conclude that the going concern basis is appropriate. Practically, possible indicators that may lead to an entity assessing the appropriateness of the going concern assumption in more detail might include (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11): (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 9)

- temporary shut-down of operations (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)
- the extent of operational disruption; (deloitte, 2020, p. 2)
- potential diminished demand for products or services; (deloitte, 2020, p. 2)
- contractual obligations due or anticipated within one year; (deloitte, 2020, p. 2)
- potential liquidity and working capital shortfalls; (deloitte, 2020, p. 2)
- Access to existing sources of capital (e.g. available line of credit, government aid) ; (deloitte, 2020, p. 2)
- Liquidity and how liquidity risk was managed;
- Reasons for reduced (or increased) demand for goods and services (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 9), In other words, reduced demand for goods and service or other income streams, caused by: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)
- restrictions and shutdowns imposed by governments, or reduction in discretionary spending by customers;
- expectations of future restrictions that might affect future demand;

- uncertainty surrounding the length of current or future restrictions;

- expected changes to the 'status quo' following the pandemic – for example, possibilities of increased working from home or financial conservatism;

- unavailability of resources necessary to continue operations, including inventory and employees; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)

- inability to repay borrowings, creditors, lease payments or other debts which become due during the pandemic; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)

- reliance on obtaining financing or credit from another company that is suffering financial difficulty due to the pandemic, or has made restrictions on lending due to the pandemic; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)

- breaching loan covenants; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)

- likelihood of financial guarantees being called upon; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 11)

- failure of other companies with similar structures and comparable operations in the same industry; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 12)

- financial difficulty or failure of debtors; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 12)

- negative equity as a result of asset impairments and/or reduced trading volumes; (AUDITING AND ASSURANCE STANDARDS BOARD (AUASB), Australian Accounting Standards Board (AASB), 2020, p. 12)

- fair value losses on assets, particularly where such assets were expected to be realised in the short-term and are relied on for short-term cash management purposes; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 12)

- reliance on intercompany funding or expected support from an overseas parent or subsidiary that may no longer be available; (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 12)

- Changes to previously announced plans, projects or initiatives and whether targets, aims or goals were missed;

- Changes in terms of trade or contract modifications with suppliers or customers that significantly affected or may affect cash flow such as customer payment defaults/bad debts;

- Breaches, or the potential for breaches, of debt covenants;

- Support provided to customers, employees or other stakeholders Changes to remuneration including bonus and incentive arrangements, and share-based payment arrangements;

- Sale or disposal of assets that would otherwise not have occurred;

- Impacts on financial position including reserves;

- Interruptions to supply chains;

- Operation of business continuity plans and effect of remote work arrangements on ability to maintain operations and controls, including cyber-security risk;

- Effects on a related company such as a parent, subsidiary, associate or joint venture including whether any support or performance guarantees have been given;

- Impact of travel restrictions and border closures;

- Significant impairment of assets, for example goodwill, Property, Plant and Equipment (PPE) or intangible assets;

- For listed entities, whether it has affected ability to pay a dividend including where an entity has previously declared an interim dividend but not yet paid it.

Some further examples of possible events and conditions given above that may be relevant to the assessment of going concern include the following: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, pp. 26, 27)

Obtaining external finance: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 26)

- Company has experienced difficulties in the past in obtaining external finance facilities and/or in complying with the related terms and covenants;

- Borrowing agreements or executory contracts include clauses relating to debt covenants at call terms or subjective clauses (for example, a “material adverse change clause” or share price declines below a certain dollar value) that triggers full or partial repayment of the amount borrowed;

- Company has breached some of the terms or covenants of the borrowing agreements giving rise to the risk that the facilities may be withdrawn or not renewed;

- Finance facility is secured on assets (for example, properties) that have decreased in value below the amount of the facility;

- Finance facilities are due for renewal in the next year;

- Management have no plans for alternative arrangements should current facilities not be extended;

- Company is dependent upon funding from a related or third party that is experiencing financial difficulties;

- Financing is provided by a syndicate of banks and other financial institutions and there are concerns about the viability of one or more of the members of the syndicate.

Management plans to overcome financing difficulties include disposal of assets or possible rights issues: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 26)

- Plans developed prior to the onset of challenging or uncertain economic conditions have not been updated;
- Lack of evidence that management can realise the assets to be disposed of at the expected values;
- Shareholders' support uncertain in relation to a planned rights issue
- Possible "lukewarm" reception of prospective investors to share issuance due to the company's poor financial performance.

Company provides significant loans or guarantees to related parties or third parties: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 26)

- Guarantees that may be called in;
- Borrowers who/which may be unable to make payments.

Company dependent upon guarantees or financial support provided by a third party: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 27)

- Guarantor no longer able/prepared to provide the guarantee;
- Financial support withdrawn or in doubt.

Future cash flows: (AUDITING AND ASSURANCE STANDARDS BOARD (AUASB), Australian Accounting Standards Board (AASB), 2020, p. 27)

- Reduction in cash flows resulting from unfavourable economic conditions;

- Major customers taking longer or unable to pay;

- Market for product or services has contracted significantly;

- Terms or covenants of renewed financing are changed and become more difficult to comply with (for example, increased interest rates or charges);

- Company is subject to margin calls as a result of a decrease in fair market value of financial instruments that it holds;

- Company has issued loans (or received borrowings) having an introductory period during which favourable terms are in force which revert to normal market rates in the forthcoming year;

Company heavily dependent upon particular counterparties: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 27)

- Suppliers facing financial difficulties provide essential goods/services;

- Company unable to find alternative suppliers;

- Major suppliers tightening their credit terms;

- Key customers experiencing financial difficulties;

- Substantial reduction of orders from key customers;

- Financial instrument counterparties are in default or experiencing difficulty to comply with terms due to cash flow problems.

2. The risks

A non-exhaustive list of business risks that an entity may wish to consider are set out below: (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 18)

- Ongoing or intermittent government-imposed shutdowns of sectors of the economy, (such as hospitality, leisure and tourism) impacting demand for goods or services;
- COVID-19-related reduction in demand for goods and services;
- Travel restrictions and border closures by either domestic or foreign governments in relevant jurisdictions impacting supply chains, exports or customers;
- Increases in the rate of COVID-19 infection within the country and/ or other relevant jurisdictions;
- Financial impacts resulting from breaches of bank covenants, withdrawal of funding or inability to increase borrowings or raise capital;
- Lack of internal controls in remote working environment including potentially increased exposure to cyber security risks;
- Pandemic outbreak among employees, in particular key management personnel
- The withdrawal of government support;
- Political instability in other countries;
- Foreign exchange fluctuations.

III- COVID-19 Going Concern Considerations

1. COVID-19 implications on going concern assessments

Going Concern means that an entity is a going concern unless the directors intend to liquidate the entity or to cease trading, or have no realistic alternative but to do so. An entity will be a going concern where the directors intend to continue its operation for the foreseeable future which is at least, but is not limited to, twelve months from the end of the reporting period. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 6)

The going concern assumption is a fundamental principle that underlies the preparation of the financial statements (AUDITING AND ASSURANCE STANDARDS BOARD (AUASB), Australian Accounting Standards Board (AASB), 2020, p. 7). Financial statements are required to be prepared on a going concern basis, unless management intends that the entity will be liquidated, cease trading or have no realistic alternative other than these courses of action. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 23)

The preparation of the financial statements on a going concern basis is appropriate whenever the directors conclude that the entity is a going concern, even if there is material uncertainty related to this assessment, as long as there is adequate disclosure of this fact. Disclosure of judgements made may be required even when the entity has concluded there is no material uncertainty around going concern. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24)

A result of COVID-19 and its associated effects, entities need to consider whether, in their specific circumstances, they have the ability to continue as a going concern (deloitte, 2020, p. 2)

Management's going concern assessment may be significantly affected by the current circumstances.

The uncertainties about the impact of the COVID-19 pandemic make the going concern assessment more difficult, owing to the extent and duration of social distancing measures in effect in many jurisdictions and the impact on the economy. Companies should consider the impact of these matters on the entity's specific circumstances. In particular, the current and potential cash resources, including access to existing and new financing facilities, and factoring and reverse factoring arrangements, need to be considered up to the date of the authorisation of the financial statements. (Sheerin, 2021)

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The going concern assessment should initially be made at balance date and take into account all available information about the future (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24)

In making its going concern assessment, IAS 10 *Events after the Reporting Period* requires an entity to consider events up to the date of authorisation of the financial statements. In certain jurisdictions, regulations may extend this period (e.g. until presentation of the financial statements at an annual shareholders' meeting). (deloitte, 2020, p. 2)

When assessing the uncertainties associated with a company's going concern assumption, management takes into account all available information for a period of at least 12 months from the date of the interim financial statements. For example, when a company with a calendar year end prepares its quarterly interim financial statements at 31 March 2020, it considers information for the period until, but not limited to, 31 March 2021 when assessing whether the going concern assumption is appropriate.

However, it should be updated so that all relevant information has been considered before the financial statements are signed off on a going concern basis (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24)

Management's assessment of the entity's ability to continue as a going concern involves making a judgement, at a particular point in time, about inherently uncertain future outcomes of events or conditions. (deloitte, 2020, p. 2)

When an entity identifies events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, it should consider all relevant information, including the feasibility and effectiveness of any planned mitigation. Just because an indicator exists does not necessarily mean that there is a material uncertainty over the entity's ability to continue as a going concern (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 13)

Directors and managers should review how they addressed or mitigated any negative effects on the entity. Obviously, users will be looking at steps taken by the entity to manage the impacts of COVID 19, which may also be indicative of how resilient the entity may be to ongoing uncertainties and any future shocks (such as new outbreaks of COVID-19 domestically or internationally). (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 10)

The following are examples of mitigating factors that entities may be considering in response to going concern pressures arising due to COVID-19 business interruptions: (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 14)

- government stimuli or other government incentives available to the entity to subsidise revenue or provide support otherwise;

- do management have a plan to sell liquid assets, is there a current market for these assets and are enough liquid assets available to meet debts and operational costs as they fall due;

- the entity's ability to defer the settlement of liabilities (such as repayment holidays on loans) or obtain new sources of financing, and its realistic ability to repay such sources of financing in the future;

- whether any financing has been guaranteed and the guarantor has the ability to assist (taking into account the terms of the guarantee and any repayment obligations to the guarantor) or whether borrowers have at least indicated a willingness to renegotiate terms and conditions and waive covenant breaches for a certain period;

- capability of entity in obtaining additional equity contributions;
- possibility of reducing overhead and administrative costs;
- possibility of liquidating surplus assets or other assets that are no longer essential;
- practical ability to alter strategies to access new revenue streams;

As well as, a non-exhaustive list of possible mitigating factors includes: (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 10)

- Details of any government subsidies received, such as JobKeeper, or benefits received from schemes, such as the Coronavirus SME Loan Guarantee Scheme or an industry support scheme;
- Any new financial arrangements that have been entered into with lenders, such as debt renegotiations or extension of credit lines;
- Reductions in operating costs, such as cancelling or deferring capital expenditure;
- Capital raisings and the purpose of that raising;
- Renegotiation of major contracts, such as rent relief;
- Reductions in remuneration (including for senior executives and the board) or staffing levels;
- Halting or winding back of production and running down of inventory.

The mere existence or possibility of mitigating factors alone may not be sufficient to conclude whether the going concern assumption is appropriate. Judgement is required by management to assess the feasibility and effectiveness of mitigating factors, so that they can satisfy themselves that there is a realistic alternative to avoid entering liquidation or ceasing trading (i.e. that the going concern assumption is appropriate) (AUDITING AND

ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 14)

The business impacts of COVID-19 will differ for each entity depending on specific circumstances and the level of disruption to the business. We expect that COVID-19 will result in the identification of more events or conditions that may cast significant doubt on the ability to continue as a going concern for many entities when compared to previous years. (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 13)

The degree of going concern considerations depends on the facts in each case. For example, if an entity concludes in making its assessment that it is unaffected by COVID-19, has a history of profitable operations and ready access to financial resources, it may reach a conclusion that the going concern basis of accounting is appropriate without detailed analysis. In that case, the entity should consider whether any disclosure may be necessary (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 12)

If the directors conclude that the entity is not a going concern, then the financial statements should not be prepared on a going concern basis (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24). The basis of accounting should be adjusted if management determines that the going concern basis is no longer appropriate, including if that is determined after the reporting period (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 4). Where this approach is taken, the financial statements will need to disclose this fact, and the reasons why the entity is not regarded as a going concern. It must also then disclose the alternative basis on which the financial statements have been prepared. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24)

The accounting standards do not prescribe an alternative basis in this situation. It is therefore important for entities to clearly explain how the alternative basis used has affected the accounting policies, recognition, measurement and presentation of the amounts in the financial statements. It would also be beneficial for the preparers and directors to discuss the basis of preparation with their auditors. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24)

2. Disclosure requirements

Disclosure is required when management concludes that there are no material uncertainties but reaching that conclusion involved significant judgement (a ‘close call’). (Kegalj, 2020, p. 2)

Given the current uncertainty and the variety of outcomes still possible related to the course of the pandemic and its adverse impact on economies all over the world, entities will need to consider a wide range of factors related to current and expected profitability, among other things. There may be cases when an entity concludes, after having considered all relevant information, including the feasibility and effectiveness of planned mitigation, that there are no material uncertainties that cast substantial doubt about its ability to continue as a going concern requiring disclosure under IAS 1. (deloitte, 2020, p. 4)

However, in this current climate, reaching that conclusion will often involve significant judgements around the range of outcomes to consider and the probabilities assigned to those outcomes. Furthermore, the range of possible outcomes and their impact on the entity’s future operations may be broad, meaning that assigning more or less weight to possible outcomes could make a difference in the entity’s conclusion regarding the existence of material uncertainties. (deloitte, 2020, p. 4)

The disclosure should be specific to the entity’s own situation, for example explaining how and when the uncertainty may crystallise and its impact on the entity’s resources, operations, liquidity and solvency. The assumptions used in determining whether an entity is a going concern should be consistent with the information used in other areas of the financial statements (e.g. liquidity risk management disclosure, impairment of non-financial assets, recognition of deferred tax assets, hedge accounting) (deloitte, 2020, p. 5). In other words. An entity must consider how its going concern assessment is reflected in the rest of its financial statements, and that any assumptions made in its going concern assessment are consistent with other recognition, measurement and disclosure in the financial statements. For example, entities should ensure that assumptions, such as cash flow projections or other estimates, used in impairment testing, fair value measurement and other estimations are consistent with the going concern assessment. Examples of COVID-19 related accounting consequences that link to going concern assessments may include (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 19): (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 19)

- impairments of assets, either financial or non-financial;
- fair value measurements;
- decreases in the net realisable value of inventory;
- recognition of provisions and onerous contracts; and
- write-off of deferred tax assets

IAS 1 requires disclosure of the judgements made that have the most significant impact on the amounts recognised in the financial statements. IAS 1 also requires disclosure of the significant judgements which the entity has made to reach the conclusion that no disclosure of material uncertainties is required under IAS 1, especially when other reasonable judgements may have resulted in a different conclusion. This is consistent with the conclusion reached by the IFRS Interpretations Committee in the July 2014 *IFRIC Update* that disclosure of significant judgements is required when an entity concludes there is no material uncertainty regarding its ability to continue as a going concern but reaching this conclusion involved significant judgement. Such disclosure is important to provide users of the financial statements with sufficient information to understand the pressures on liquidity, viability and solvency. (deloitte, 2020, p. 5)

Even if an entity concludes that there is no material uncertainty regarding its ability to continue as a going concern, information that may be relevant to users of the financial statements includes: (deloitte, 2020, p. 5)

- the different going concern scenarios that have been considered;
- inputs that have been subject to stress tests and an explanation of how these stress tests have affected the going concern conclusions;
- any mitigating actions management is able to take to improve liquidity;
- any post balance sheet changes to liquidity, specifically the arrangement of new lending facilities, the extension of existing facilities or the renegotiation of debt instruments or facilities or waiving of loan covenants;
- the level of drawn and undrawn finance facilities in place;
- the covenants in place and whether they are expected to be breached;
- The need for structural changes in order for the entity to continue to operate as a going concern.

Entities should also consider any additional expectations relating to disclosure of these matters that have been articulated by regulators in their jurisdictions.

The accounting standards do not prescribe an alternative basis in this situation and there are differing views on whether such financial statements would still need to comply with the broad principles of the Conceptual Framework for Financial Reporting where an entity must still prepare financial statements that comply with accounting standards as required. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 24) Where the going concern basis is no longer appropriate because the directors have no realistic alternative but to liquidate the entity and intend to appoint a liquidator or external administrator, the directors should consider whether and how this may affect the financial reporting obligations of the entity for the current reporting period. (AUDITING AND ASSURANCE STANDARDS BOARD(AUASB), Australian Accounting Standards Board (AASB), 2020, p. 20)

Conclusion:

The impact of COVID-19 has been an evolving situation since late 2019. Given the information available at 31 December 2019, COVID-19 would be unlikely to have had a material effect on the measurement of assets and liabilities at that date. Since then, both the impact of the virus and the information available about that impact have changed. The World Health Organisation declared a global health emergency in January 2020 and in March 2020, it declared the spread of COVID-19 as a global pandemic. Consequently, entities with a reporting date after 31 December 2019 should consider the impact of COVID-19 on the measurement of assets and liabilities, the recognition of gains and losses, the potential impact on going concern, and the related disclosures.

The coronavirus (COVID-19) pandemic has developed rapidly in 2020, with a significant number of cases globally. Measures taken to contain the virus have significantly affected economic activity, which in turn has implications for financial reporting. Entities should consider whether developments (including those events subsequent to the reporting date) have any implications for the going concern assumption. Ultimately, we can extract these outcomes:

- Going concern is one of the fundamental principles of accounting, on the basis of which financial statements are prepared. Under this principle, it is assumed that a business will continue to operate in the foreseeable future without the need or intention to liquidate or curtail its operational activities. Accordingly, the assets and liabilities are recorded on the basis that the entity will be able to realise its assets and discharge its liabilities in the normal course of business;

- It is the responsibility of the management of an entity to determine whether the going concern assumption is appropriate in the preparation of financial statements;

- Certain sectors may face financial distress, such as declining demand, falling sales and margin pressures and could be more exposed than others. In this scenario, the risk assessment procedures of going concern performed by management would be very different to that from previous years;

- Implementation of stringent measures to contain or delay the spread of COViD-19 has significantly disrupted business operations and economic activity. The unpredictability of the potential impact of the outbreak may result in material uncertainties that cast doubt on an entity's ability to operate as a going concern. It is therefore important for the management to understand and anticipate the effects of COVID -19 on their business while performing an assessment of going concern this year;

- Multiple scenarios might exist about the potential impact of COVID-19 on the entity such as: going concern with material uncertainties; going concern without material uncertainties; going concern without material uncertainties; non-going concern;

- An overall lower economic activity in the country has created an unprecedented level of uncertainty of consequent future earnings of entities, particularly in the near term. In this highly uncertain environment, management's going concern assessments would be more difficult to be made;

- We expect that most entities will disclose information about the impact of COVID-19 on going concern in the financial statements. The detail and location of such disclosure should depend on the extent to which the entity is affected;

- Auditors would evaluate and conclude on the appropriateness of management's use of the going concern basis of accounting in the preparation of financial statements, and would need to conclude whether a material uncertainty related to the entity’s ability to continue as a going concern exists.

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