Applying IFRS

Accounting considerations for the coronavirus outbreak

Updated April 2020

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Contents

1. Background

As the outbreak continues to evolve, it is difficult, at this juncture, to estimate the full extent and duration of the business and economic impact. Consequently, these circumstances have presented entities with greater challenges when preparing their interim and annual IFRS financial statements.

The threats posed by the coronavirus outbreak are not stopping. More countries have imposed travel bans on millions of people and more people in more locations are placed with quarantine measures. Businesses are dealing with lost revenue and disrupted supply chains. The disruption to global supply chains due to factory shutdowns has already exposed the vulnerabilities of many organisations. The outbreak has also resulted in significant volatility in the financial and commodities markets worldwide. There are already signs that the virus has significantly impacted the world economy. Various governments have announced measures to provide both financial and non-financial assistance to the disrupted industry sectors and the affected business organisations.

In February, we first issued *Applying IFRS accounting considerations of Coronavirus outbreak*, which focuses on addressing the financial effects when preparing IFRS financial statements for the year ended 31 December 2019. The new circumstances described above have presented entities with greater challenges in preparing their IFRS financial statements.

This publication has since been updated to provide a reminder of the existing accounting requirements that should be considered when addressing the financial effects of the coronavirus outbreak in the preparation of IFRS financial statements for the annual or interim reporting periods ending in 2020. Disclosure considerations for interim financial reporting are also covered in this publication. The issues discussed are by no means exhaustive and their applicability depends on the facts and circumstances of each entity. The financial reporting issues, reminders and considerations highlighted in this publication are the following:

- Going concern
- Financial instruments (
- Assets impairment
- Government grants
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- Leases
- Insurance recoveries
- Onerous contract provisions
- Fair value measurement
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2. Going concern

IAS 1 *Presentation of Financial Statements* requires management, when preparing financial statements, to make an assessment of an entity's ability to continue as a going concern, and whether the going concern assumption is appropriate. Furthermore, disclosures are required when the going concern basis is not used or when management is aware, in making their assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern. Disclosure of significant judgement is also required where the assessment of the existence of a material uncertainty is a significant judgement.

The going concern assessment needs to be performed up to the date on which the financial statements are issued.

In assessing whether the going concern assumption is appropriate, the standard requires that all available information about the future, which is at least, but not limited to, twelve months from the end of the reporting period, should be taken into account. This assessment needs to be performed up to the date on which the financial statements are issued. Refer to section 3 for further discussion on the current vulnerability entities are facing due to concentration and liquidity risks.

Measurement

Management is required to assess the entity's ability to continue as a going concern. When making that assessment, where relevant, management takes into consideration the existing and anticipated effects of the outbreak on the entity's activities in its assessment of the appropriateness of the use of the going concern basis. For example, when an entity has a history of profitable operations and relies on external financing resources, but because of the outbreak, its operations have been suspended before or after the reporting date, management would need to consider a wide range of factors relating to the current adverse situation including, expected impact on liquidity and profitability before it can satisfy itself that the going concern basis is appropriate. Management should consider all available information about the future which was obtained after the reporting date including measures taken by governments and banks to provide relief to affected entities in their assessment of going concern.

Disclosure

Given the unpredictability of the potential impact of the outbreak, there may be material uncertainties that cast significant doubt on the entity's ability to operate under the going-concern basis. If the entity, nevertheless, prepares the financial statements under the going-concern assumption, it is required to disclose these material uncertainties in the financial statements in order to make clear to readers that the going-concern assumption used by management is subject to such material uncertainties.

How we see it

The degree of consideration required, the conclusion reached, and the required level of disclosure will depend on the facts and circumstances in each case, because not all entities will be affected in the same manner and to the same extent. Significant judgement and continual updates to the assessments up to the date of issuance of the financial statements may be required given the evolving nature of the outbreak and the uncertainties involved.

3. Financial instruments (IFRS 9)

The coronavirus outbreak and the related government measures may have a direct impact on the accounting for financial instruments. IFRS 9 *Financial Instruments* and IFRS 7 *Financial instruments: Disclosures* deal with the accounting for financial instruments and the related disclosures. Entities should exercise careful consideration in their accounting for financial instruments. Additional accounting considerations for banks, are also included in this section.

Current vulnerability due to concentration and liquidity risks

Entities with concentrations of risk may face greater risk of loss than other entities. Paragraph 34(c) of IFRS 7 requires that concentration of risk should be disclosed if not otherwise apparent from other risk disclosures provided. Therefore, entities should consider including the following information:

- A description of how management determines concentrations of risk
- A description of the shared characteristic that identifies each concentration. For instance, the shared characteristic may refer to geographical distribution of counterparties by groups of countries, individual countries or regions within countries and/or by industry
- The amount of the risk exposure associated with all financial instruments sharing that characteristic

Entities that have identified concentrations of activities in areas or industries affected by the outbreak not previously disclosed should now reconsider making such a disclosure.

Entities that have identified concentrations of activities in areas or industries affected by the outbreak (e.g., the airline, hospitality and tourism industries) and have not previously disclosed the concentration because they did not believe that the entity was vulnerable to the risk of a near-term severe impact, should now reconsider making such a disclosure.

Similarly, liquidity risk in the current economic environment is increased. Therefore, it is expected that the disclosures required under IFRS 7 in this area will reflect any significant changes in the liquidity position as a result of the coronavirus outbreak. Entities should be mindful that this disclosure is consistent with their assessment of the going concern assumption.

For entities that will prepare interim financial statements under IAS 34 *Interim Financial Reporting*, if concentration and liquidity risks have significantly changed compared to their most recent annual financial report, they should disclose the above information in their interim financial statements.

Asset classification and business model assessment: impact of sales

A deterioration of the credit quality of the borrower or the issuer of a financial asset, as a result of the coronavirus outbreak, may result in entities deciding to dispose of investments classified as hold-to-collect under IFRS 9. If the sale is due to an increase in credit risk, this could still be consistent with the business model objective hold-to-collect, because the credit quality of financial assets is relevant to the entity’s ability to collect contractual cash flows. Selling a financial asset because it no longer meets the credit criteria specified in the entity’s documented investment policy is an example of a sale that would be consistent with the ‘hold-to-collect’ business model.

Additionally, an increase in the frequency and value of sales in a particular period is not necessarily inconsistent with the objective to hold financial assets in order to collect contractual cash flows, if an entity can explain the reasons for those sales and demonstrate why sales in the future will be lower in frequency or value. For example, if, due to a significant decrease in demand for the entity's products or services as a result of the coronavirus outbreak (e.g., airline tickets or hospitality events), the entity faces a temporary liquidity crisis, a sale of financial assets classified as held-to-collect may not be inconsistent with such business model.

Reclassifications triggered by a change in the business model for managing financial assets are expected to be very infrequent and will occur only when an entity either begins or ceases to perform an activity that is significant to its operations (for example, acquisition, disposal or termination of a business line). A change in intention related to particular financial assets (even in circumstances of significant changes in market conditions) is not a change in business model.

Contract modifications

Affected entities may experience cash flow challenges as a result of disruptions in their operations, higher operating costs or lost revenues. Such entities may need to obtain additional financing, amend the terms of existing debt agreements or obtain waivers if they no longer satisfy debt covenants. In such cases, they will need to consider the guidance provided in IFRS 9 to determine whether any changes to existing contractual arrangements represent a substantial modification or potentially a contract extinguishment, which would have accounting implications in each case.

For financial liabilities, an entity should derecognise the 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 on 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, commonly referred to as the '10% test'.

IFRS 9 provides guidance on 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 instrument is derecognised. However, other qualitative factors could lead to derecognition irrespective of the 10% test (e.g., if a debt is restructured to include an embedded equity instrument).

For financial assets, there is no explicit guidance in IFRS 9 for when a modification should result in derecognition. Hence, entities apply their own accounting policies, which are often based on qualitative considerations and, in some cases, include the '10% test'. However, the IFRS Interpretations Committee has indicated that applying the '10% test' in isolation would not always be appropriate, because of potential inconsistencies with the impairment requirements in IFRS 9. Some preparers may apply different accounting policies depending on whether a modification is granted due to the financial difficulty of the borrower, with some concluding that such circumstance would rarely result in the derecognition of the financial asset. If a measure provides temporary relief to debtors and the net economic value of the loan is not significantly affected, the modification would be unlikely to be considered substantial. For example, if the payment terms of a receivable are extended from 90 days to 180 days, this would likely not be considered a substantial modification of the receivable.

If, following the guidance above, a modified financial asset or 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. For floating rate instruments, a change in the market rate of interest is accounted for prospectively. However, any other contractual change (e.g., the spread applied above the interest rate) would also result in a catch-up adjustment at the date of modification.

Hedge accounting

If an entity has designated a transaction such as the purchase or sale of goods or the expected issuance of debt, as a hedged forecasted transaction in a cash flow hedge, the entity will need to consider whether the transaction is still a 'highly probable forecasted transaction'.

Business transactions may be postponed or cancelled, or they may occur in significantly lower volumes than initially forecasted. If an entity has designated a transaction such as the purchase or sale of goods or the expected issuance of debt, as a hedged forecasted transaction in a cash flow hedge, the entity will need to consider whether the transaction is still a 'highly probable forecasted transaction'.

This includes whether the volume or amounts involved will be lower than forecasted, whether the timing of the hedged forecasted transaction has changed (for example, the acquisition of an item of property, plant or equipment (PP&E) is postponed by six months as a result of the disruption created by the outbreak) or whether it is now no longer probable that a forecasted transaction will occur. That is, if the coronavirus outbreak affects the probability of hedged forecasted transactions occurring and/or the time period designated at the inception of a hedge, an entity will need to determine whether it can continue to apply hedge accounting to the forecasted transaction or a proportion of it, and for continuing hedges whether any additional ineffectiveness has arisen:

- If an entity determines that a forecasted transaction is no longer highly probable, but still expected to occur, the entity must discontinue hedge accounting prospectively. In this case, the accumulated gain or loss on the hedging instrument that has been recognised in other comprehensive income will remain recognised separately in equity until the forecasted transaction occurs.
- If an entity determines that the timing of a forecasted transaction has changed, and the cash flows are now expected to occur at a different time than initially forecasted, the outcome would depend on the nature of the hedged item and how the hedge relationship was documented.
    - For example, if the hedged forecasted transaction was the acquisition of a specific item of PP&E and the expected timing of it has been delayed by six months compared to when initially forecasted, it may be argued that the hedged transaction is still highly probable. However, hedge effectiveness would have to be reassessed under the new terms, which could result in some ineffectiveness being recognised in profit or loss.
    - In other cases, judgement may be needed based on the specific facts and circumstance. For example, if the hedged forecasted transaction was the interest payments in a loan and those were postponed as

a result of a payment holiday, judgement will be needed, considering the terms of the moratorium (including whether interest continues to accrue and whether it results in derecognition of the original loan) and how the hedged risk was designated, in order to establish whether the hedged forecasted transaction (or a portion thereof) is still expected to occur or if any additional ineffectiveness arises as a result.

- If an entity determines that a forecasted transaction is no longer expected to occur, in addition to discontinuing hedge accounting prospectively, it must immediately reclassify to profit or loss any accumulated gain or loss on the hedging instrument that has been recognised in other comprehensive income.

Fair value hedges are not subject to the highly probable forecasted transaction assessment. However, if the timing of the hedged cash flows changes without a corresponding change in the hedging instrument, this will cause ineffectiveness. Consideration will also be required as to whether the qualifying effectiveness assessment (applicable under IAS 39 *Financial Instruments: Recognition and Measurement*) or the economic relationship criteria (applicable under IFRS 9) is still met as a result of the change in the hedged item.

Expected credit loss (ECL) assessment

The occurrence of large-scale business disruptions potentially gives rise to liquidity issues for certain entities. It might also have consequential impacts on the credit quality of entities along the supply chain. This will also have knock on effects on retail portfolios (consumer and mortgage loans) as many businesses will have to reduce staff numbers resulting in an increase in the number of unemployed workers. The deterioration in credit quality of loan portfolios, but also, e.g., of trade receivables, as a result of the outbreak will have a significant impact on the ECL measurement. In responding to these challenges, certain governments and central banks have introduced, or have directed or encouraged commercial banks to introduce, various types of relief measures.

The deterioration in credit quality of loan portfolios, but also, e.g., of trade receivables, as a result of the outbreak will have a significant impact on the ECL measurement.

A number of prudential and securities regulators, including the European Banking Authority (EBA), the European Central Bank (ECB), the European Securities and Market Authority (ESMA) and the Prudential Regulation Authority (PRA) in the United Kingdom (the regulators) have published guidance on the regulatory and accounting implications of the outbreak. Additionally, the International Accounting Standards Board (the IASB or Board) has recently published a document, for educational purposes, to help support the consistent application of accounting standards in the context of ECLs. The document is broadly consistent with the guidance from the regulators and emphasises that IFRS 9 does not set bright lines or a mechanistic approach to determining when there is a significant increase in credit risk (SICR), nor does it dictate the exact basis on which entities should determine forward looking scenarios to measure expected credit losses.

The measurement of ECL should be based on an unbiased, probability-weighted amount that is determined by evaluating a range of possible outcomes and reflecting time value of money.

The use of reasonable and supportable information

The measurement of ECL should be based on an unbiased, probability-weighted amount that is determined by evaluating a range of possible outcomes and reflecting time value of money. Entities should exercise judgement and their best efforts to consider all reasonable and supportable information available about past events, current conditions and forecasts of future economic conditions, as described further in this publication.

The IASB acknowledges that it is likely to be difficult at this time to incorporate the specific effects of the outbreak and government support measures on a reasonable and supportable basis. When it is not possible to reflect such information in models, the IASB expects post-model overlays or adjustments to be considered.

Given the unprecedented circumstances, it is critical that entities provide transparent disclosure of the critical assumptions and judgements used to measure the ECL.

Re-segmentation of loan portfolios or groups or receivables

For the purpose of measuring ECLs and for determining whether an SICR has occurred, an entity 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 coronavirus 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, entities should consider (re)segmenting (sub)portfolios.

Individual and collective assessment of loans, receivables and contract assets

Due to the abnormal circumstances, it may take time for an entity 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. Entities using a provision matrix approach to calculate ECLs for trade receivables will need to make appropriate adjustments to their historical loss rates and reflect the current economic environment as well as forward looking information. For example, a supplier of products or services to the airline industry would likely consider that the PD (or loss rates, if a provision matrix approach is used) of its customers has increased irrespective of specific events identified at the level of individual counterparties.

In estimating PD, loss rates and ECL, entities should consider the effect of any state aid plans to support customers through various measures (e.g., refinancing measures or other forms of financial support, including guarantees). Additionally, entities which are using multiple economic scenarios when estimating ECL should consider updating these scenarios to reflect the current change in circumstances (for further guidance, refer to the section 'Additional considerations on ECL for banks' below).

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.

Extension of payment terms

As indicated previously, 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. For example, if the payment terms of a receivable are extended from 90 days to 180 days, this would likely not be considered a substantial modification of the receivable. However, such an extension may result in an increase in PD, which would, in turn, affect the measurement of ECL. For entities which do not apply the simplified model, such extension may also result in moving the receivable to stage 2, depending on the extent and terms of the payment extension. However, if the same extension of payment terms is offered to an entire class of customers irrespective of individual circumstances, this should generally not result, by itself, in a stage movement.

Additional considerations on ECL for banks

Payment holidays and breaches of covenants

The accounting impact of relief measures on ECL depends on the details of the arrangements. For example, the extension of payment holidays or a waiver of a breach of covenant to all borrowers in particular classes of financial instruments should not automatically result in all those instruments suffering a SICR. This would be the case even if a moratorium results in a loss for the lender (e.g., if interest payments are reduced or waived), if it is provided irrespective of the borrowers' individual circumstances.

In other situations, if the relief measures are available only to those who meet certain criteria, entities need to carefully assess whether such criteria themselves might indicate a SICR for the affected borrowers. For instance, a SICR is more likely to have occurred if a borrower applies for a relief measure which is available only to corporates which have suspended operations or individuals who have lost employment. Another example is if the relief, such as a deferral of loan payments, is offered to all participants in certain industries. This circumstance may indicate that borrowers in that industry are exposed to a higher risk of business failure and, thus, a higher probability of default as a class. In combination with other reasonable and supportable information, this is more likely to result in the classification of the related loans and other exposures in this portfolio, or a portion of them, into stage 2. The assessment should be made irrespective of the fact that a concession is imposed by laws or regulations. Entities are also expected to exercise judgement, in light of all facts and circumstances, including the effect of government support, to determine if the respective loans are credit impaired and should therefore be classified as stage 3.

Regulators have stressed the need to differentiate a temporary liquidity need from a SICR and highlighted that there may be very limited information available to make this determination at an individual borrower level. This means that lenders should distinguish between obligors whose long-term credit risk is unlikely to be significantly affected by the outbreak from those who may be more permanently impacted. In light of the above, the 30 days past due backstop assumption may need to be rebutted in the current circumstances.

Entities whose models include such events as automatic SICR triggers may need to include overlays to unwind the effects if they determine that SICR trigger is not warranted in this situation.

Entities whose models include such events as automatic SICR triggers may need to include overlays to unwind the effects if they determine that SICR trigger is not warranted in this situation.

For retail loans, data will often not be available to determine whether a SICR has occurred for individual borrowers. For wholesale exposures, more information is generally available on individual obligors, although the SICR assessment will still be difficult. A lender may consider that borrowers in certain industries (e.g., airlines, tourism and hospitality) are exposed to a higher risk of business failure and, thus, an increased PD.

When it is not practical to determine SICR on an individual basis, a collective approach to staging should be considered. This will also be challenging. A possible method could be to transfer to stage 2 a portion of those customers who have been given a payment holiday or a waiver of a covenant breach, whose PD was already close to the level that would trigger an SICR. Any approach will require considerable judgement.

As indicated previously, if a measure provides temporary relief to debtors and the net economic value of the loan is not significantly affected, the modification would be unlikely to be considered substantial. It follows that the effect of any such waiver of interest or capital (measured using the original effective interest rate of the loan) must be recorded as an expense in profit or loss as soon as it is granted.

Individual and collective assessment, multiple macroeconomic scenarios and management overlays

Whether the impact of the outbreak is reflected in an individual ECL assessment (e.g., estimation of probability of default on an individual basis), factored into the scenario analysis of future macroeconomic conditions on a collective basis, or adjusted through management overlays, depends on the bank's systems and processes and the facts and circumstances. In practice, entities may probably consider a combination of these approaches. In estimating the impact of the coronavirus outbreak, entities should, however, avoid double-counting of the effects of various assumptions applied in individual assessment, macroeconomic scenarios and management overlays.

Due to the abnormal circumstances, it may take time before banks detect changes in risk indicators at a specific borrower level and are able to reassess the affected exposures. 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 on a collective basis, considering risk characteristics such as the industry or geographical location of the borrowers. However, many methods for performing collective assessments make use of historical information, which may not be relevant in the current circumstances.

Many financial institutions consider multiple macroeconomic scenarios in the assessment of ECL. The current situation is not likely to have been reflected in any of the scenarios used for the ECL estimates at the prior year end and, as such, will need to be updated. In addition to updating GDP expectations for the various scenarios, a challenge will be to estimate how the impact of the coronavirus outbreak and any related government programmes will affect specific sectors, regions and borrowers, especially as the details surrounding many government programmes are currently evolving.

The IASB noted how a number of the assumptions and linkages underlying the way ECLs have been implemented to date may no longer hold in the current environment. For example, the relationship between GDP and other macroeconomic variables, such as unemployment and interest rates, and sector-specific variables, such as oil prices, is very likely to be different from what has been experienced in the past and is currently used in economic forecasting models. The probability weightings assigned to macroeconomic scenarios may also need to be revisited. However, the IASB still expects changes in economic conditions to be reflected in the macroeconomic scenarios and in their weightings and, when the effects of the outbreak cannot be reflected in the models, post-model overlays or adjustments will need to be considered.

In estimating overlays, entities may consider historical experience, including, for instance, the impact of similar events such as the SARS outbreak in 2003. However, it appears clear that the widespread nature and severity of the consequences of the coronavirus outbreak is not directly comparable with any recent similar events. It may be appropriate for this purpose, to plot several possible scenarios of what might happen over the coming months and assign weightings to them, to ensure that any overlay reflects the inherent uncertainty and non-linearity of potential outcomes.

Impact of financial support and credit enhancements

The effect of any form of support provided by a government or a parent company depends firstly on whether its effect is to prevent a default by the borrower, or to compensate a lender for losses it suffers due to the borrower's default.

The effect of any form of support provided by a government or a parent company depends firstly on whether its effect is to prevent a default by the borrower, or to compensate a lender for losses it suffers due to the borrower's default. In some cases, a government or a parent company may provide direct financial support to a borrower. For example, the government may offer to compensate employees who have lost their job with a portion of their previous salary for a period of time. These forms of financial support prevent or reduce the extent to which a borrower would otherwise default on a loan. These forms of financial support are considered in a lender's assessment of SICR and ECL as it reduces the credit risk associated with the underlying loan.

In other cases, a guarantee may be issued to a lender to compensate it for losses it suffers due to default by a borrower. Such a guarantee does not prevent default by a borrower, but rather reduces the effect of any default. The accounting effect of such a guarantee depends on whether it is integral to the contractual terms of the guaranteed loan and whether it is required to be recognised separately by the lender. If it is integral to the loan and is not required to be recognised separately by a lender, the guarantee is taken into account in calculating the loss given default (LGD) of the guaranteed loan, however, it does not affect the SICR assessment. The impact of the outbreak on the value of the enhancement (e.g., shares or bond prices, real-estate values and the credit standing of any guarantor) also needs to be considered.

In December 2015, the IFRS 9 Transition Resource Group observed that credit enhancements included in the measurement of ECLs should not be limited to those that are explicitly part of the contractual terms. ESMA considered that a guarantee will be integral 'when a public guarantee is provided in conjunction with broadly applicable *ex-lege* moratoria or economic support and relief measures'. Whether a credit enhancement is integral depends on an assessment of individual facts and circumstances and is likely to require judgement. If the guarantee is issued at the same time as the loan and is inseparable from it, it would be generally considered to be integral to the loan and therefore included in the measurement of ECL. If the guarantee is issued on existing loans instead, it would generally not be considered integral to that loan if it was not anticipated when the loan was originally granted.

If a guarantee is not considered to be integral, it may still meet the criteria to be recognised as a reimbursement asset by analogy to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, which would have to be recognised separately in the statement of financial position and may result in an offsetting entry in profit or loss, depending on the accounting policy of the lender.

Where guarantees are issued by governments for a below market rate fee, both borrowers and lenders will have to assess whether this constitutes a government grant to be accounted for and disclosed in accordance with IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*.

Where guarantees are issued by governments for a below market rate fee, both borrowers and lenders will have to assess whether this constitutes a government grant to be accounted for and disclosed in accordance with IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. In performing such an assessment, entities will need to consider the level of the interest rate offered to the borrower on the guaranteed loan and whether the economics of the overall transaction are providing a benefit to the lender, the borrower or to both. For example, any benefit to a lender from a below market rate fee on a guarantee is required to be (partially) offset by a reduction in the interest earned on the loan to the borrower, in which case, the value of any government grant to the lender may be reduced or eliminated. In such a case, the value of the grant accrues mainly to the borrower in the form of a below market rate loan relative to the borrower's credit risk.

Where such guarantees are provided at below market rates by holding companies or other group entities, the initial benefit provided may need to be accounted for as an equity transaction between group entities.

Disclosures

Given the inherent level of uncertainty and the sensitivity of judgements and estimates, the disclosure of the key assumptions used and judgements made in estimating ECL is particularly important. This is the case both for annual reporters and for entities that will prepare interim financial statements under IAS 34, as the inputs into the ECL measurement will likely have significantly changed compared to their most recent annual or interim financial report. Important disclosures would include, for example, the values of the key macroeconomic inputs used in the multiple economic scenario analysis and the probability weights of these scenarios, as well as the assumptions used to determine how the different challenges for specific sectors and regions have been taken into account and the effect of any management overlays.

Lenders will be expected to provide more information on their exposures by sector and region. To the extent that entities have the legal and regulatory flexibility to do so, it is likely that some of the disclosures normally given in an interim report which are not related to credit risk will be reduced, to focus on the information of particular concern to users at this time.

In addition, entities should provide disclosures to allow users of financial statements to understand the nature of any material reliefs offered to their borrowers, including those enforced by governments, and how they have assessed whether they constitute forbearance, whether they result in a substantial modification of the contract, their effect on staging and the impact on the overall ECL. Entities should also disclose any material form of government grant or government assistance received in accordance with IAS 20.

How we see it

The assessment of the impact of the coronavirus outbreak on ECL will require significant judgement, especially as it is not directly comparable with any recent similar events. Entities will have to update their macroeconomic scenarios and consider the use of top-down 'management overlays' to embed in the ECL risks not yet fully captured by their models. Given the level of uncertainty and the sensitivity of judgements and estimates, disclosures of the key assumptions used and judgements made in estimating ECL, as well as the impact of any relief measures, is going to be critical.

4. Financial instruments (IAS 39)

Considerations under IAS 39 applied by insurance companies

Although IFRS 9 replaced IAS 39, many insurance companies currently still apply IAS 39 as allowed by IFRS 4 *Insurance Contracts*. For those insurance companies, different classification and measurement requirements and different impairment requirements apply from those described for IFRS 9 (see section 3 above). In addition, there are some differences related to (de)recognition, hedge accounting and disclosures, although, for these topics, many of the aspects mentioned above are also relevant to IAS 39. The main accounting considerations for financial assets under IAS 39 in light of the coronavirus outbreak are set out below.

Classification

IAS 39 applies a classification model to financial assets based on the following measurement categories:

- At fair value through profit or loss
  - Designated as at fair value through profit or loss
  - Held for trading
- Held-to-maturity investments
- Loans and receivables
- Available-for-sale assets

Classification takes place at initial recognition. However, IAS 39 allows certain reclassifications of financial assets between these measurement categories subsequently. Such reclassifications include, amongst others, a reclassification out of the held-for-trading portfolio into the available-for-sale or held-to-maturity portfolios in 'rare circumstances'. The combination of events caused by the coronavirus outbreak and the related containment measures qualifies, in our view, as 'rare circumstances' under paragraph 50B of IAS 39.

Any reclassifications are applied prospectively from the date the entity decides to make the reclassification. Derivatives and financial assets designated as at fair value through profit or loss cannot be reclassified.

If entities intend to sell instruments classified as held-to-maturity, e.g., for liquidity reasons, they should be aware of the 'tainting' provisions, which if triggered, result in a reclassification as available-for-sale, with the asset being remeasured to fair value and any associated gain or loss recognised in other comprehensive income.

Measurement

IAS 39 sets out the measurement requirements for each of the measurement categories mentioned above. Important measurement impacts of the coronavirus outbreak are related to determining: (a) the fair value of financial assets for measurement and disclosure purposes; and (b) whether a financial asset not measured at fair value through profit or loss is impaired and, if so, estimating the amount of the impairment.

For the considerations on determining the fair value of financial assets, refer to section 12 of this publication. The considerations on the impairment of financial assets are further addressed below.

Impairment

Under IAS 39, all financial assets, except for those measured at fair value through profit or loss, are subject to review for impairment. Assessments should be made at the end of each reporting period as to whether there is any objective evidence that a financial asset or group of assets is impaired.

Under IAS 39, all financial assets, except for those measured at fair value through profit or loss, are subject to review for impairment. Assessments should be made at the end of each reporting period as to whether there is any objective evidence that a financial asset or group of assets is impaired.

A financial asset or a group of assets is impaired (and impairment losses are determined) if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after initial recognition (a loss event) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of assets that can be reliably estimated.

It may not be possible to identify a single discrete event that caused the impairment. Rather, the combined effect of several events may cause an impairment, which is important to consider under the current circumstances as the coronavirus outbreak and the resulting containment measures are causing a range of adverse effects, for example, a sharp decline in financial markets, strongly reduced sales, a sharp increase in unemployment rates.

Losses expected as a result of future events, no matter how likely, are not recognised under IAS 39.

Available-for-sale equity instruments

A significant or prolonged decline in the fair value of an investment in such an instrument below its cost gives rise to objective evidence of impairment of an investment in equity instruments classified as available-for-sale.

This trigger applies in addition to those specific to debt instruments described in the next section.

Insurance companies applying IAS 39 often classify their investments in equity instruments as available-for-sale. The current decline in financial markets following the coronavirus outbreak may have caused the value of these equity securities to drop below their cost. Entities need to assess whether these market conditions give rise to a significant or prolonged decline in fair value that is objective evidence of impairment, in which case, the negative amount recognised in other comprehensive income for the impaired instruments should be recycled to profit or loss immediately. The determination of what is 'significant or prolonged' requires judgement. The basis for what is considered 'significant or prolonged' needs to be applied consistently from period to period.

As the current volatile market conditions may continue for a while, entities should continue to closely monitor the developments and determine the impact on the recognised impairment amounts. For any equity instruments for which a prior impairment loss has been recognised, 'significant' should be evaluated against their original cost at initial recognition and 'prolonged' should be evaluated against the period in which the fair value of the investments has been below original cost at initial recognition. Consequently, once an impairment loss has been recognised, any further decline in fair value at the next reporting date, whatever its cause, should be recognised in profit or loss as well. Any subsequent increase in the fair value of the equity instrument is recognised in other comprehensive income and the impairment loss previously recognised in profit or loss is not reversed through profit or loss.

Impairments of available-for-sale equity instruments recognised in a previous IAS 34 interim report should not be reversed in a subsequent interim period or the annual period.

Available-for-sale debt instruments

A financial asset or a group of assets is impaired (and impairment losses are determined) if, and only if, there is, at the reporting date, objective evidence of impairment as a result of one or more events that occurred after initial recognition (a loss event) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of assets.

IAS 39 refers to several examples of events where observable data from these events could provide such objective evidence, for example, significant financial difficulty of the issuer or obligor, a breach of contract (such as a default or delinquency in interest or principal payments), the lender granting to the borrower a concession that would not otherwise be considered, the increasing probability that the borrower will enter bankruptcy, or other financial reorganisation, or national or local economic conditions that correlate with defaults on the assets in the group.

Other factors that would be considered in determining whether an impairment loss has been incurred include information about the debtors' or issuers' liquidity, solvency and business and financial risk exposures, levels and trends in delinquencies for similar financial assets, national and local economic trends and conditions, and the fair value of collateral and guarantees.[1]

Entities should carefully consider whether the observable data from current stressed market conditions and the economic situation following the coronavirus outbreak may give rise to objective evidence of a loss event. For example, measures such as the extension of repayment terms for a short period of time (e.g., 3 or 6 months) which are available country-wide regardless of the credit standing would generally not be considered an impairment trigger per se. However, the fact that a measure is offered to a certain sector or industry may be considered evidence of impairment for issuers in the sector or industry and would require further assessment.

When a decline in the fair value of an available-for-sale debt instrument has been recognised in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss within equity should be reclassified to profit or loss. The amount of the loss that should be reclassified is the difference between the acquisition cost of the asset (net of any principal repayment and amortisation for assets measured using the effective interest method) and current fair value, less any impairment loss on that asset previously recognised in profit or loss. If, in a subsequent period, the fair value of an available-for-sale debt instrument increases, and the increase can be

[1] A downgrade of an entity's credit rating is not, of itself, evidence of impairment, although it may be when considered with other available information. Also, a decline in the fair value of a financial asset below its cost or amortised cost is not necessarily evidence of impairment, for example, the fair value of a debt instrument may decline solely due to an increase in the risk-free interest rate.

objectively related to an event occurring after the loss was recognised in profit or loss, the impairment loss should be reversed and recognised in profit or loss. Judgement is required to determine whether a recovery in the fair value of an available-for-sale debt security relates to an event that occurred after the loss was recognised.

Amortised cost debt instruments

Financial assets carried at amortised cost follow the same principle of a loss event as available-for-sale debt instruments (see above). If there is objective evidence that an impairment loss has been incurred on loans and receivables or held-to-maturity investments, that loss should be measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. Those cash flows, which should exclude future credit losses that have not been incurred, should be discounted at the original effective interest rate of the financial asset, i.e., the effective interest rate computed at initial recognition.

If, in a subsequent period, the amount of the impairment or bad debt loss decreases and the decrease can be objectively related to an event occurring after the write-down (such as an improvement in the debtor's credit rating), the previously recognised impairment loss should be reversed with the reversal recognised in profit or loss.

Modifications

In respect of contract modifications and any resulting derecognition of financial instruments, refer to those described for IFRS 9 in section 3 as the guidance on derecognition in IAS 39 is comparable. However, a noticeable difference is related to the modification of the cash flows of a financial liability and the liability is not derecognised. In such a situation, IFRS 9 requires that any modification gains or losses are recognised in profit or loss immediately, whereas under IAS 39, it would be acceptable to recognise such gains or losses over the remaining term of the liability due to a lack of specific guidance.

Hedge accounting

Business transactions may be postponed or cancelled, or they may occur in significantly lower volumes than initially forecasted. The resulting hedge accounting considerations for financial instruments are addressed in section 3 on IFRS 9, which also describes the implications under the hedge accounting guidance of IAS 39.

Disclosures

The current situation caused by the coronavirus outbreak may result in a need for additional disclosure, for example, regarding vulnerability due to concentration and liquidity risks. See section 3 on concentration and liquidity disclosures.

Within the context of applying IAS 39's incurred loss model, entities should provide several disclosures relating to the following aspects of credit risk: the maximum exposure to credit risk; credit quality of financial assets; financial assets that are either past due or impaired; collateral; and other credit enhancements obtained. Entities should consider in their disclosures how these aspects have been affected by the coronavirus outbreak. These disclosures would include an explanation of the nature of any material reliefs offered to borrowers, including those enforced by governments, and how the entities have assessed whether they constitute evidence of impairment and whether they result in a substantial modification of the contract.

How we see it

Even though IAS 39 has been applied for many years, the coronavirus outbreak is unprecedented and may result in various challenges in the accounting for financial assets held by insurance companies. In particular, the recent sharp decline in financial markets and the stressed economic situation require a careful analysis of whether these developments have given rise to objective evidence of an incurred loss event.

In addition, insurers should carefully consider the impact of the changes in the values of their financial assets on the insurance liabilities as the measurement of some types of insurance labilities is affected by the results from those financial assets through profit sharing features and shadow accounting mechanisms.

5. Impairment assessment

An asset is impaired when an entity is not able to recover its carrying value, either by using it or selling it. An entity estimates the recoverable amount of the asset for impairment testing. Recoverable amount is the higher of the fair value less costs of disposal (FVLCD) and the value in use (VIU). Value in use is defined as the present value of the future cash flows expected to be derived from an asset or cash generating unit. The calculation of an asset's value in use incorporates an estimate of expected future cash flows and expectations about possible variations of such cash flows.

IAS 36 *Impairment of Assets* requires an entity to assess, at the end of each reporting period, whether there is any impairment for an entity's non-financial assets. For goodwill and intangible assets with indefinite useful lives, the standard requires an annual impairment test and when indicators of impairment exist. In accordance with IFRIC 10 *Interim Financial Reporting and Impairment,* an entity may not reverse an impairment loss recognised in a previous IAS 34 interim report in respect of goodwill. For other classes of assets within the scope of the standard, an entity is required to assess at each reporting date whether there are any indications of impairment. The impairment test only has to be carried out if there are such indications.

Events after the reporting period and information received after the reporting period should be considered in the impairment indicator assessment only if they provide additional evidence of conditions that existed at the end of the reporting period. Similarly, the determination of the recoverable amounts of an asset should only consider the information obtained after the reporting date if such information relates to conditions existing as of the reporting period end. Judgement of all facts and circumstances is required to make this assessment.

Existence of impairment indicators

As mentioned above, an entity is required to assess at the reporting date whether there are any indicators of impairment. With the recent developments of the outbreak, there are both external and internal sources of information, such as the fall of stock and commodity prices, decrease of market interest rates, manufacturing plant shutdowns, shop closures, reduced demand and selling prices for goods and services, etc., indicating an asset may be impaired.

Measurement

When assessing impairment, entities are required to determine the recoverable amounts of the assets. FVLCD is the fair value as defined in IFRS 13 which has been explained in section 12 *Fair value measurement* in this publication. The estimation of the VIU involves estimating the future cash inflows and outflows that will be derived from the use of the asset and from its ultimate disposal and discounting the cash flows at an appropriate rate.

When estimating the recoverable amount based on the value in use, the forecasted cash flows should reflect management's best estimate of the economic conditions that will exist over the remaining useful life of the asset.

In cases where the recoverable amount is estimated based on value in use, the considerations on accounting estimates apply. The forecasted cash flows should reflect management's best estimate at the end of the reporting period of the economic conditions that will exist over the remaining useful life of the asset. With the current uncertain situation, significant challenges are expected to prepare the forecast of or budgets for future cash flows. In these circumstances, an expected cash-flow approach based on probability-weighted scenarios may be more appropriate to reflect the current uncertainty than a single best estimate when estimating value in use.

Since the remaining useful life for many assets, such as goodwill, is long term, entities should consider not just the short term effects, but especially the long term effects.

Disclosure

The more the current environment is uncertain, the more important it is for the entity to provide detailed disclosure of the assumptions taken, the evidence they are based on and the impact of a change in the key assumptions (sensitivity analysis).

Given the inherent level of uncertainty and the sensitivity of judgements and estimates, disclosures of the key assumptions used and judgements made in estimating recoverable amount will be particularly important. This is especially the case as they will have likely been materially updated compared to the key assumptions, judgements and estimates applied in the latest annual financial statements. These would include, for example, the values of the key assumptions and the probability weights of multiple scenarios when using an expected outcome approach

How we see it

As the crisis evolves and the conditions are unpredictable, at this stage, management is required to exercise significant judgement to assert reasonable assumptions which reflect the conditions existing at the reporting date for impairment testing. We expect that in the current situation, majority of these assumptions are subject to significant uncertainties. As such, entities should consider providing detailed disclosures on the assumptions and sensitivities.

6. Government grants

Requirements

IAS 20 applies to the accounting for, and the disclosure of, government grants and to the disclosure of other forms of government assistance. The distinction between government grants and other forms of government assistance is important because the standard's accounting requirements only apply to the former. Government grants are transfers of resources to an entity in return for past or future compliance with certain conditions relating to the entity's operating activities. The purpose of government grants, which may be called subsidies, subventions or premiums, and other forms of government assistance is often to encourage a private sector entity to take a course of action that it would not normally have taken if the assistance had not been provided.

Due to the severe impact on many entities' business activities of the coronavirus outbreak, many countries' governments, agents or similar bodies have introduced (or are expected to introduce) relevant measures to assist entities. However, not all of these measures are considered as government grants. Entities should evaluate the measures carefully and determine which standards should govern the respective accounting treatment.

SIC-10 *Grants with no specific relation to operating activities* addresses the situation in some countries where government assistance is provided to entities, but without any conditions specifically relating to their operating activities, other than to operate in certain regions or industry sectors.

Scope

Recently many countries' governments, agents or similar bodies have introduced (or are expected to introduce) relevant measures to assist entities in response to the coronavirus. These measures include direct subsidies, tax exemptions, tax reductions and credits, extended expiry period of unused tax losses, reduction of public levies, rental reductions or deferrals and low-interest loans.

Whilst the benefit of a low-interest loan would be accounted for under IFRS 9 and IAS 20, not all these measures are accounted for as government grants. For example, a reduction of income tax is accounted for under IAS 12 *Income Taxes*; and rental reductions or deferrals may be accounted for under IFRS 16 *Leases*. Accordingly, entities should analyse all facts and circumstances carefully to apply the appropriate relevant accounting standards. We will focus on the accounting for government grants under IAS 20 in this section and will have more detailed analysis in other sections to discuss the accounting for those measures which are governed by accounting standards other than IAS 20.

Recognition in the statement of financial position

Government grants should be recognised as an asset only when there is reasonable assurance that the entity will comply with the conditions attaching to them and the grants will be received. For example, when the government has decided to give out special subsidies to the affected entities, government grants can be recognised only when it is confirmed that an entity is eligible to receive the subsidy and that any conditions attaching to these subsidies are met. In cases where subsidies relating to coronavirus outbreak are given to entities without any specified conditions, an asset can be recognised at the time when it is reasonably certain that the grants will be received. Nevertheless, it is important to note that the receipt of a grant does not of itself provide conclusive evidence that the conditions attaching to the grant have been, or will be, fulfilled.

Recognition in the income statement

Government grants must be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate. In cases where a grant relates to expenses or losses already incurred, or for the purpose of giving immediate financial support to the entity with no future related costs expected to be incurred, the grant should be recognised in income when it becomes receivable.

Government may decide to stimulate economic activity by providing subsidies on investments by entities. If these subsidies are related to investment in assets which will be used by the entities over a longer term, the grant should be recognised in profit or loss over the useful lives of those related acquired assets.

Measurement

Direct cash assistance or subsidies will be measured at their fair value. However, government grants can take other forms. For example, when a government grant takes the form of a low-interest government loan, the loan should be recognised and measured in accordance with IFRS 9 (at its fair value) and the difference between this initial carrying value of the loan and the proceeds received is treated as a government grant. A forgivable loan from government, the repayment of which will be waived under certain prescribed conditions, is initially accounted for as a financial liability under IFRS 9 and would only be treated as a government grant when there is reasonable assurance that the entity will meet the terms for forgiveness. When government grants take the form of a transfer of non-monetary assets, such as plant and equipment, for the use of the entity, entities may apply an accounting policy choice to account for such grants at fair value of the non-monetary assets or at a nominal amount

Presentation

Grants that are related to assets should be presented in the statement of financial position either by setting up the grant as deferred income, which is presented as income over the useful life of the asset; or by deducting the grant in arriving at the carrying amount of the asset, in which case, the benefit is presented in profit or loss as a reduction to depreciation.

Grants related to income should be presented either as a credit in the income statement, either separately or under a general heading such as ‘other income’, or as a deduction in reporting the related expense.

Disclosure

IAS 20 requires entities to disclose the following information:

- The accounting policy adopted for government grants, including methods of presentation adopted in the financial statements
- The nature and extent of government grants recognised in the financial statements and an indication of other forms of government assistance from which the entity has directly benefited
- Unfulfilled conditions and other contingencies attaching to government assistance that has been recognised

How we see it

Whether IAS 20 should be applied depends on the facts and circumstances of the specific measures implemented by the government, including government agencies and similar bodies. Entities need to analyse all facts and circumstances carefully to determine the appropriate accounting treatment.

7. Income taxes

Requirements

Recent government responses to the coronavirus outbreak have included income tax concessions and other rebates. Entities need to consider the impacts of these legislative changes on their accounting for income taxes.

A range of economic stimulus packages have been announced by governments around the world. Recent government responses to the coronavirus outbreak have included income tax concessions and other rebates. Entities need to consider the impacts of these legislative changes on their accounting for income taxes. IAS 12 *Income Taxes* requires current tax liabilities and assets for current and prior periods to be measured at the amount expected to be paid to (or recovered from) the taxation authority, using the tax rates and laws that were enacted, or substantively enacted, by the end of the reporting period. Deferred tax assets and liabilities must be measured at the tax rates expected to apply to the period when the asset is realised or the liability is settled, also using the tax rates and laws that were enacted, or substantively enacted, by the end of the reporting period.

Accounting estimates

To avoid errors in the preparation of financial statements, paragraph 5 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* requires an entity to use reliable information that was available when those financial statements were authorised for issue and could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements. Changes in accounting estimates that result from new information or new developments are not considered corrections of errors and should be accounted for in the period of the change (and future periods, if affected). Future changes to amounts recognised in the financial statements that result from new information or more experience would generally be treated as changes in accounting estimates.

In applying their judgement, entities may wish to consider IFRIC 23 *Uncertainty over Income Tax Treatments*. Although IFRIC 23 was not specifically developed to deal with tax law changes or the current coronavirus outbreak in mind, it provides helpful guidance that entities may wish to consider in accounting for the uncertainties that exist with respect to their tax positions in light of any changes in legislation. It requires an entity to consider whether it is probable that a taxation authority will accept an uncertain tax treatment. If the entity concludes that the position is not probable of being accepted, the effect of the uncertainty needs to be reflected in the entity's accounting for income taxes.

Substantively enacted or not

In some jurisdictions, announcements of tax rates (and tax laws) by the government have the substantive effect of actual enactment. In such circumstances, tax assets and liabilities are measured using the announced tax rate. However, this is not always the case and an entity would need to consider when the tax concessions (e.g., reduced tax rates) become substantively enacted in their jurisdiction, for example, by considering the legislative process and consensus in its jurisdiction for when a law becomes substantively enacted.

Recognition

Conditions attached to tax relief

Some governments might structure their tax relief so it applies only to entities who have been impacted by the coronavirus outbreak based on certain qualifying criteria, for example, only entities in certain sectors, or entities of a certain size (e.g., by revenue), or that have suffered a certain amount of economic impact. This may give rise to uncertainty and the need for entities to make judgements and estimates when assessing their income tax position, for example, whether for that taxation period, the entity will fall below the revenue threshold in order to receive the tax concession. Entities will need to determine whether it is probable that the taxation authority will accept their position. If not, IFRIC 23 requires entities to assess whether to recognise any additional liability for uncertain tax positions. The same requirement applies to recognition of uncertain tax assets.

Tax credits

Tax relief may come in the form of tax credits. Tax credits are not defined within IFRS, and entities need to exercise judgement in determining how the receipt of a tax credit should be accounted for, as a reduction in tax liability under IAS 12, or the receipt of a government grant under IAS 20, when it is structured as a cash payment or has other indicators of a grant such as non-tax related conditions being attached to it (for example, cash spend on approved research and development related activities). A tax credit to be treated in accordance with IAS 12 will have indicators such as reducing income taxes payable (being forfeited or deferred if there are insufficient taxes payable) and having few, if any, non-tax conditions attached to it. A tax credit to be treated in accordance with IAS 20 will often be directly settled in cash in the case of insufficient taxes payable and have non-tax conditions attached. In any case, all facts and circumstances relating to the specific relief need to be considered in assessing the substance of the arrangement.

Taxable temporary differences related to investments

IAS 12 requires a deferred tax liability to be recognised for all taxable temporary differences associated with investments (both domestic and foreign) in subsidiaries, branches and associates or interests in joint arrangements, unless:

- The parent, investor, joint venturer or joint operator is able to control the timing of the reversal of the temporary difference
- It is probable that the temporary difference will not reverse in the foreseeable future

In our view, IAS 12 requires the group to make provision for the taxes payable on the retained profits of the group as at each reporting date based on the best evidence available to it at the reporting date. Therefore, if an entity's expectations regarding intragroup dividends have changed, it will need to update the above assessment for the new information.

Measurement

Current and deferred tax balances

Many governments announced tax stimulus packages in early 2020. This would not impact the measurement of current tax balances and deferred tax balances as at 31 December 2019. Some tax concessions such as tax rate reductions could relate to prior years. Because IAS 12 states that these balances are to be measured in accordance with the rates and laws that had already been substantively enacted as at reporting date, any impacts relating to prior taxation years would only be recorded in the financial period in which the amending legislation was substantively enacted.

Entities with reporting periods ended or ending in 2020 need to consider if the tax concessions announced in early 2020 are substantively enacted prior to reporting period end. As noted earlier, entities need to consider what is generally understood as 'substantively enacted' in their own jurisdiction. If determined to be substantively enacted by reporting date, then current tax balances and deferred tax balances would be measured based on the tax incentives including reduced tax rates under the stimulus package.

In cases where the tax concessions are staggered over several years, such as incremental tax rate reductions, the expected timing of the reversal of deferred tax balances will also need to be assessed.

Carry forward of tax losses

In assessing the probability of the future realisation of carry forward tax losses, entities will need to consider whether the adverse economic conditions arising as a result of the coronavirus outbreak existed as at reporting date. If so, the entity will need to consider the deterioration of the economic outlook in its forecasts of taxable profits and reversals of taxable temporary differences. If not, the event is non-adjusting, but the entity should consider disclosure around the nature of the subsequent event.

Disclosure

In addition to subsequent event disclosures, the following will also be relevant for entities impacted by the coronavirus outbreak: an explanation of changes in the applicable tax rate compared to the prior period; the amount and expiry date of any carry forward tax losses; and the nature of evidence supporting the recognition of deferred tax assets when the entity has suffered a loss in the current period. The entity should also consider disclosure of the nature of any significant judgements or estimates made when determining the appropriate accounting for the matters described above. Such judgements may include whether the tax laws were substantively enacted as of reporting date, and the determination of the accounting for income tax credits.

How we see it

Entities need to determine whether changes to tax rates and laws as part of government responses to the coronavirus outbreak, were substantively enacted as of the reporting date. The characteristics of any tax relief or rebates received by the government need to be carefully assessed in order to determine whether they should be accounted for as a reduction to the income tax expense, or the receipt of a government grant. Uncertainties relating to income taxes arising from these new government measures will require entities to consider whether they should recognise and measure current and/or deferred tax assets or liabilities at a different amount.

8. Liabilities from insurance contracts

IFRS 4 requires an entity issuing insurance contracts to account for its rights and obligations from the insurance contracts that it issues. The current coronavirus outbreak could affect an entity's liabilities for issued insurance contracts for a range of product lines. For example, entities issuing life or health products may be faced with claims caused by the impact of the outbreak on policyholders' health status. Entities may also be affected by claims where cover is provided for events driven by the disruption caused by the outbreak, for example, business interruption insurance, event cancellation insurance, travel insurance and credit insurance. However, since coronavirus is a new disease, contractual terms may not be clear on whether policyholders can claim against the insurer and may require further interpretation (e.g., whether the coronavirus outbreak gives rise to *force majeure* and the possible impact of such a qualification). Also, entities need to consider any interpretations, directives or rulings by local authorities (e.g., government, regulator or health agency) that could impact the obligations under the contract for the entity, for example, guidance issued by the local regulator on how to treat customers fairly within the context of the current circumstances.

Measurement

Entities issuing insurance contracts will, therefore, need to assess the impact the coronavirus, or the disruption caused by the outbreak, to their insurance liabilities based on their specific accounting policies, including the effect on the liability adequacy testing of the insurance liabilities.

Entities issuing insurance contracts will therefore need to assess the impact of the coronavirus, or the disruption caused by it, on their insurance liabilities based on their specific accounting policies. This includes the effect on the liability adequacy testing of the insurance liabilities (including related deferred acquisition costs and intangibles, such as those arising from insurance contracts acquired in a business combination or portfolio transfer).[2] This assessment would need to consider factors including, but not limited to, the effect on reported claims, the effect on incurred but not (enough) reported claims, the impact of these effects on the assumptions for estimating expected future claims, and the impact on the entity's claims handling expenses. Where the entity reinsured risk from its insurance contracts, it should also consider the associated recovery through its asset from reinsurance contracts held.[3] In determining these effects, the entity should consider not only the terms and conditions of its insurance contracts, but also the implications of any interpretations, directives or rulings by local authorities for those terms and conditions (see above). Where an entity's accounting policies for the measurement of its insurance liabilities may also involve the use of current estimates of market variables, for example, interest rates and equity prices, the entity should reflect the impact of market developments on these variables in its measurement. This impact includes the effects of results from related investments on the valuation of the insurance liabilities through profit sharing and shadow accounting mechanisms.

[2] Several intangible assets such as value in force, value of distribution agreements and possible deferred participation reserve (if in an asset position) may require additional evaluation of their recoverability.
[3] Reimbursement rights of policyholders, other than the situation of a reinsurance contract held by a cedant, is covered in section 10, Insurance recoveries, of this publication.

Entities should also assess whether the coronavirus gives rise to events after the reporting period and determine the implications for the financial statements. As the coronavirus outbreak continues to evolve, situations and conditions are changing rapidly, entities that will report their interim or annual financial statements with a reporting date in early 2020 (e.g., 31 March 2020) would face significant challenges when considering the events after the reporting date. Insurers are required to perform a careful analysis of the nature and impact of these subsequent events to determine if they are adjusting or non-adjusting in accordance with IAS 10 *Events after the Reporting Period* (see section 14). Also refer to section 4 for considerations on the accounting for financial assets under IAS 39 by insurance companies.

Disclosure

Entities will need to disclose the assumptions used to make their estimates, highlight the uncertainties and explain the sensitivities of the measurement of the insurance liabilities if alternative assumptions were used, explaining how these are influenced by incorporating consequential effects of the coronavirus. Other disclosure items, like insurance risk concentrations, claims developments, credit risk and market risk may be affected as well. Entities should also consider the implications on capital disclosures as capital ratios may come under pressure due to a fall in asset values and stressed capital requirements.

Even though the full extent of the impact on insurance entities may not be clear and a number of uncertainties around the impact may remain, disclosure explaining these uncertainties and possible effects will be needed. Such disclosure would need to include an explanation of events that happened after the reporting date, for any events that relate to conditions that existed at the end of the reporting period, as well as for events that relate to conditions that arose after the reporting period.

How we see it

The coronavirus outbreak will affect insurance entities as they deal with the effect of events on the insurance cover they provide, ranging from coverage provided in relation to changes in health status of policyholders due to the wide spread of the disease, to coverage for events related to disruption caused by the coronavirus outbreak. However, the impact on insurance entities is expected to be much broader than the effect on the accounting for insurance liabilities as the current situation raises various challenges for insurers. For example, entities would have to identify and monitor new risks, and determine the magnitude of their impact on the insurance business. Entities would also have to deal with the impact of the developments on financial markets on their asset liability management strategies.

Given the rapid developments and extent of measures taken to contain the effects of the coronavirus outbreak, insurance entities should anticipate uncertainty over the impact on their insurance liabilities in the coming period, and will need to monitor developments closely and determine whether these developments have an impact on the accounting for their insurance liabilities.

9. Leases

IASB document on lease modifications

In April 2020, the IASB released a document, prepared for educational purposes, highlighting requirements within IFRS 16 *Leases* and other IFRS standards that are relevant for entities considering how to account for rent concessions granted as a result of the coronavirus outbreak. The document does not change, remove, nor add to, the requirements in IFRS standards and the intention is to support the consistent and robust application of IFRS 16. The document explains how an entity evaluates whether a rent concession constitutes a lease modification, which is defined under IFRS 16 as a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease.

A change in the scope of a lease

In assessing whether there has been a change in the scope of a lease, an entity considers whether there has been a change in the right of use conveyed to the lessee by the contract. A change in the scope of a lease includes adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual lease term. A rent holiday or rent reduction alone is not a change in the scope of a lease.

A change in the consideration for a lease

In assessing whether there has been a change in the consideration for a lease, an entity considers the overall effect of any change in the lease payments. For example, if a lessee does not make lease payments for a three-month period, the lease payments for periods thereafter may be increased proportionally in a way that means that the consideration for the lease is unchanged.

A change that was not part of the original terms and conditions of the lease

If there has been a change in either the scope of, or the consideration for, the lease, an entity next considers whether that change was part of the original terms and conditions of the lease. As specified in paragraph 2 of IFRS 16, an entity is required to consider the terms and conditions of contracts and all relevant facts and circumstances when applying the standard. Relevant facts and circumstances may include contract, statutory or other law or regulation applicable to lease contracts.

Lease contracts or applicable law or regulation may contain clauses that result in changes to payments if particular events occur or circumstances arise. Government action (e.g., requiring the closure of retail stores for a period of time because of the coronavirus outbreak) might be relevant to the legal interpretation of clauses, such as *force majeure*, that were in the original contract or in applicable law or regulation. Changes in lease payments that result from clauses in the original contract or in applicable law or regulation are part of the original terms and conditions of the lease, even if the effect of those clauses (arising from an event such as the coronavirus outbreak) was not previously contemplated. In such a case, there is no lease modification for the purposes of IFRS 16.

Proposed amendment to IFRS 16

On 24 April 2020, the IASB published an Exposure Draft, *Covid-19-Related Rent Concessions* (the ED) with a 14 day comment period. The ED proposes an amendment to IFRS 16 to permit lessees, as a practical expedient, not to assess whether particular coronavirus-related rent concessions are lease modifications. Instead, lessees that apply the practical expedient would account for those rent concessions as if they were not lease modifications. The ED proposes no change for lessors.

Under the proposal, the practical expedient applies only to rent concessions occurring as a direct consequence of the coronavirus outbreak and only if all of the following conditions are met:

- The change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change
- Any reduction in lease payments affects only payments originally due in 2020 (for example, a rent concession would meet this condition if it results in reduced lease payments in 2020 and increased lease payments that extend beyond 2020)
- There is no substantive change to other terms and conditions of the lease

A lessee that applies the practical expedient will be required to disclose that fact.

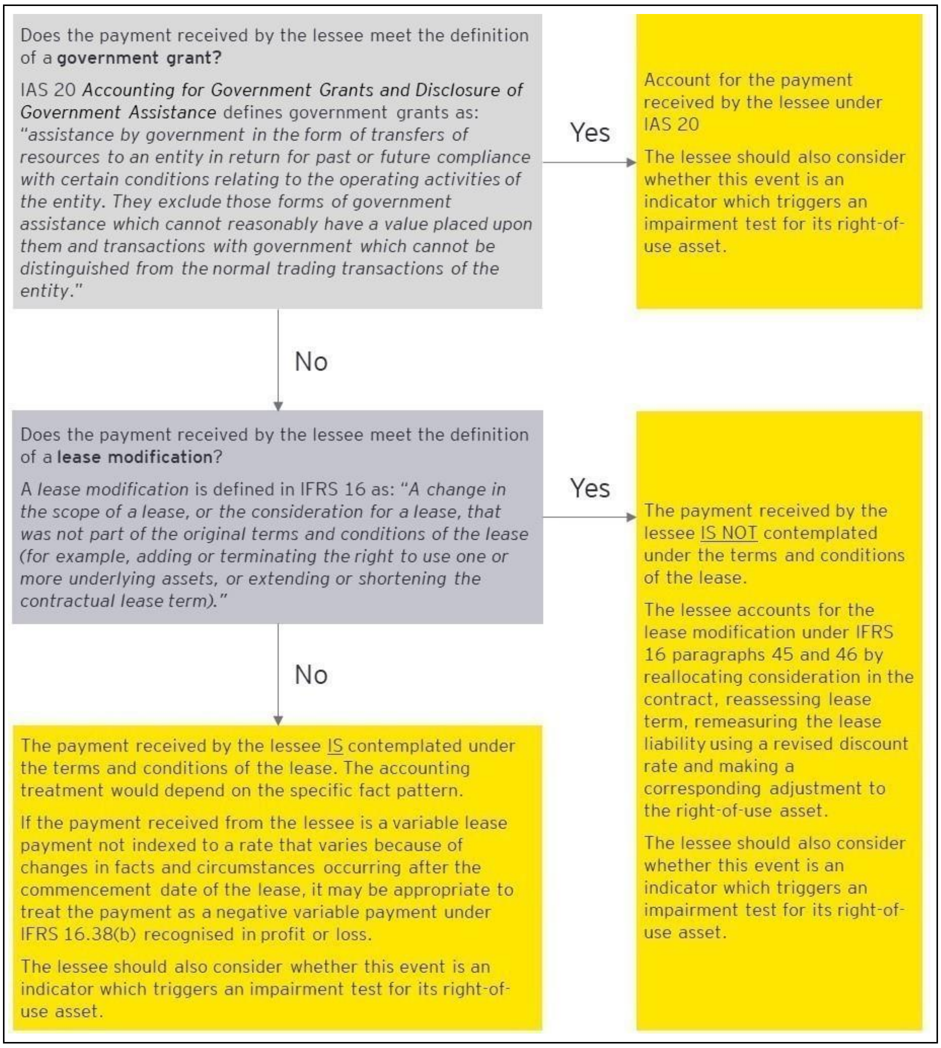
A lessee will apply the amendment retrospectively, recognising the cumulative effect of initially applying that amendment as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the beginning of the annual reporting period in which the lessee first applies the amendment. The proposed practical expedient will be applicable for annual reporting periods beginning on or after 1 June 2020. Earlier application is permitted, including in financial statements not yet authorised for issue at the date the amendment is issued.

Lessee's assessments of payments received (or receivable)

When payments are received by a lessee, it is necessary to evaluate whether IFRS 16 applies to such payments. In some jurisdictions, local authorities have implemented policies to provide subsidies to lessees and others in order to support the local economy and these payments are accounted for under IAS 20. Refer to section 6 for a discussion on the related accounting consideration.

When IFRS 16 applies to such payments made by a lessor, the lessee and lessor need to evaluate if there is a lease modification by considering the original terms and conditions of the lease. For example, a lessor may make a payment to a lessee of retail space in an airport when there are significant flight cancellations and such payment is not contemplated within the terms of the contract. In assessing whether the lease is modified, entities need to carefully evaluate terms of their contracts, including any *force majeure* clauses, which may, in specified circumstances, suspend some of their obligations or provide additional rights in the lease.

Figure 1: Lessee's assessment of payments received (or receivable)



Accounting for lease modifications

Lessee consideration

A lease modification is a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease.

For a lease modification that is not accounted for as a separate lease, at the effective date of the lease modification, a lessee is required to allocate the consideration in the modified contract, determine the lease term of the modified lease and remeasure the lease liability by discounting the revised lease payments using a revised discount rate. If the modification decreases the scope of the lease, the lessee accounts for the remeasurement of the lease liability by decreasing the carrying amount of the right-of-use asset to reflect the partial or full termination of the lease and recognises in profit or loss any gain or loss relating to the partial or full termination. For all other modifications, the lessee makes a corresponding adjustment to the right-of-use asset.

How we see it

The modification of the lease requires the remeasurement of the lease liability using a revised discount rate. Given that the interest rate implicit in the lease is generally not readily determinable by the lessee, it is necessary for the lessee to determine a revised incremental borrowing rate. The coronavirus outbreak has exacerbated market volatility and central banks in many jurisdictions are cutting interest rates. Assessing a revised incremental borrowing rate may also require judgement in these circumstances.

Lessor consideration

Lessor accounting for lease modifications depends on the classification of the lease. A lessor accounts for a modification to an operating lease as a new lease from the effective date of the modification, considering any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease. For a modification to a finance lease that is not accounted for as a separate lease, the lessor accounts for the lease modification as a new lease from the effective date of the modification and measures the carrying amount of the underlying asset as the net investment in the lease immediately before the effective date of the lease modification if the lease had been classified as an operating lease. Otherwise, the lessor applies the requirements of IFRS 9 to the modification to a finance lease that is not accounted for as a separate lease.

10. Insurance recoveries

Requirements

A reimbursement is recognised when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation.

In accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement is recognised when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The amount of the provision is not reduced by any expected reimbursement. Instead, the reimbursement is treated as a separate asset and the amount recognised for the reimbursement asset is not permitted to exceed the amount of the provision.

A contingent asset is defined as a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. An entity does not recognise a contingent asset because this may result in the recognition of income that may never be realised. However, when the realisation of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate. A contingent asset is subject to disclosure where an inflow of economic benefits is probable. An entity needs to continually assess its contingent assets to ensure that developments are appropriately reflected in the financial statements. If an inflow of economic benefits has become probable (when, previously, it was possible but not probable), an entity is required to disclose the contingent asset. If it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs.

Recognition

An entity may experience a loss related to the coronavirus outbreak. For example, as a result of the shutdown of its production facilities as required by the local government, an entity continues to incur expenses for staff costs, rent and property taxes. Entities often enter into insurance policies to reduce or mitigate the risk of loss arising from business interruption or other events.

The accounting for insurance claims will differ based on a variety of factors, including the nature of the claim, the amount of proceeds (or anticipated proceeds) and the timing of the loss and corresponding insurance recovery. In addition, any accounting for insurance proceeds will be affected by the evaluation of coverage for that specific type of loss in a given situation, as well as an analysis of the ability of an insurer to satisfy a claim.

In some instances, it may be clear that the recognition threshold for the reimbursement is met when the reimbursable expense is incurred. In other instances, a careful analysis of the terms and conditions of an entity's business interruption policies is required due to the wide variety of terms relating to the nature and level of losses covered. Some policies covering lost revenue or operating margins that typically are measured over a longer term require comparisons with similar periods in prior years. In such cases, no compensation would be available if revenue or operating margins recover during the measurement period that is set under the terms of the insurance policy. For example, a claim under a policy with a quarterly measurement period would not be valid if a retailer were to lose an entire month's revenue, but recover that revenue before the end of the quarter.

Decisions about the recognition (and measurement) of losses are made independently of those relating to the recognition of any compensation that might be receivable. It is not appropriate to take potential proceeds into account when accounting for the losses.

IAS 37 prohibits the recognition of contingent assets. In such a situation, the recognition of the insurance recovery will only be appropriate when its realisation is virtually certain, in which case, the insurance recovery is no longer a contingent asset. 'Virtually certain' is not defined in IAS 37, but it is certainly a much higher hurdle than 'probable' and, indeed, more challenging than the term 'significantly more likely than probable' in Appendix A of IFRS 5 *Non-current assets held for sale and discontinued operations*.[4] It is reasonable to interpret 'virtually certain' to be as close to 100% as to make any remaining uncertainty insignificant. In practice, this means that each case must be assessed on its own merits. In the context of a potential insurance recovery, determining that there is a valid insurance policy for the incident and a claim will be settled by the insurer, may require evidence confirming that the insurer will be covering the claim.

If a previously unlikely receipt becomes probable, but it is still a contingent asset, it will only be disclosed. This assessment extends to the analysis of information available after the end of the reporting period and before the date of approval of the financial statements. In applying IAS 10, an asset is recognised only if the information about the insurance recovery, that becomes available in the subsequent period, provides evidence of conditions that existed at the end of the reporting period and its realisation was virtually certain at that time. For example, the later receipt by the entity of confirmation from the insurer that its insurance policy does cover this type of loss would provide evidence of cover as at the end of the reporting period.

Measurement

Once it is established that it is virtually certain that the entity will be compensated for at least some of the consequences of the coronavirus outbreak under a valid insurance policy, any uncertainty as to the amount receivable should be reflected in the measurement of the claim.

Presentation

'Netting off' is not allowed in the statement of financial position, with any insurance reimbursement asset classified separately from any provision. However, the expense relating to a provision can be shown in the income statement net of any corresponding reimbursement.

In accordance with IAS 7 *Statement of Cash Flows*, cash flows from operating activities are described as cash flows from the principal revenue-producing activities of the entity and other activities that are not investing or financing activities. If the insurance proceeds are related to business interruption, the corresponding cash flows are classified as operating cash flows.

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[4] According to paragraph 23 of IAS 37, an event is regarded as probable if the event is more likely than not to occur.

How we see it

The terms and conditions of an insurance policy are often complex. In the context of a potential insurance recovery, determining that there is a valid insurance policy for the incident and a claim will be settled by the insurer, may require evidence confirming that the insurer will be covering the claim.

Once it is established that it is virtually certain that the entity will be compensated for at least some of the consequences of the coronavirus outbreak under a valid insurance policy, any uncertainty as to the amount receivable should be reflected in the measurement of the claim.

11. Onerous contract provisions

If an entity has a contract that is onerous, IAS 37 requires the entity to recognise and measure the present obligation under the contract as a provision.

Requirements

An onerous contract is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. If an entity has a contract that is onerous, IAS 37 requires the entity to recognise and measure the present obligation under the contract as a provision. Before a separate provision for an onerous contract is established, an entity recognises any impairment loss that has occurred on assets dedicated to that contract. See section 5 for further details on impairment considerations.

Recognition

One significant impact of the coronavirus outbreak is the disruption to the global supply chain. For example, when a manufacturing entity has contracts to sell goods at a fixed price and, because of the shutdown of its manufacturing facilities, as required by the local government, it cannot deliver the goods itself without procuring them from a third party at a significantly higher cost, the provision for the onerous contract will reflect the lower of the penalty for terminating the contract or the present value of the net cost of fulfilling the contract (i.e., the excess of the cost to procure the goods over the consideration to be received). Contracts should be reviewed to determine if there are any special terms that may relieve an entity of its obligations (e.g., *force majeure*). Contracts that can be cancelled without paying compensation to the other party do not become onerous as there is no obligation.

How we see it

In assessing the unavoidable costs of meeting the obligations under a contract at the reporting date, entities, especially those with non-standardised contract terms, need to carefully identify and quantify any compensation or penalties arising from failure to fulfil it.

12. Fair value measurement

The objective of fair value measurement is to estimate the price at which an orderly transaction to sell an asset or to transfer a liability would take place between market participants at the measurement date under current market conditions (i.e., to estimate an exit price). The impact on fair value measurement (FVM) arising from the coronavirus outbreak and the ensuing economic and market disruptions varies across countries, markets and industries. When valuations are subject to significant measurement uncertainty due to the current environment and there is a wider range of possible estimates of FVM, the entity is required to apply judgement to determine the point within that range that is most representative of FVM in the circumstances.

Below are certain key FVM considerations within IFRS 13 *Fair Value Measurement* that can help entities navigate challenges in the context of volatile and uncertain markets.

The definition of fair value contemplates an orderly transaction, which is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities and it is not a forced transaction (e.g., a forced liquidation or distress sale). While volatility in the financial markets may suggest that the prices are aberrations and do not reflect fair value, it would not be appropriate for an entity to disregard market prices at the measurement date, unless those prices are from transactions that are not orderly. Evidence of whether a transaction is orderly must be evaluated when deciding the weight that is placed on the transaction price when estimating FVM or market risk premiums. If the observed price is based on a transaction that is determined to be forced or disorderly, little, if any, weight should be placed on it compared with other indications of value.

The determination of whether a transaction is orderly is made at the individual transaction level and requires the use of judgement based on the available evidence from all relevant factors. While market factors such as an imbalance in supply and demand and liquidity constraints can affect the prices at which transactions occur in a given market, such an imbalance does not automatically indicate that the parties to a transaction were not knowledgeable and willing market participants or that a transaction was not orderly. The entity's conclusion that it would not sell its own asset (or transfer its own liability) at prices currently observed in the market does not mean these transactions should be presumed to be distressed. IFRS 13 makes clear that fair value is a market-based measurement, not an entity-specific measurement, and notes that the reporting entity's intention to hold an asset or liability in a market downturn is not relevant.

IFRS 13 makes clear that fair value is a market-based measurement, not an entity-specific measurement, and notes that the reporting entity's intention to hold an asset or liability in a market downturn is not relevant.

An active market is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis. The level of activity of a market is determined based on the weight of available evidence, such as the number of transactions taking place, widening bid-ask spreads and significant increases in implied liquidity risk premiums. IFRS 13 is clear that, while observable prices from inactive markets may not be representative of fair value in all cases, this data should not be ignored. Additional analysis is required in these instances to assess the relevance of observed transactions or quoted prices in these markets, including analysis to determine whether the transaction is orderly (as discussed above) and factors specific to the asset or liability being measured, as well as facts and circumstances surrounding the price (e.g., size of the transaction, proximity of the transaction to the measurement date and significant developments of the subject and market conditions between these dates). If the quoted price is based on a transaction that is determined to be orderly, this data point should be considered in the estimation of fair value, albeit adjustments to observable prices (which could be significant) may be necessary or the weight placed on that price in the FVM changed.

A significant decrease in volume or activity in a market can also influence which valuation technique(s) are used, how those techniques are applied and whether inputs are observable at the measurement date. For example, the application of the market approach can prove more challenging and the use of additional valuation techniques may be warranted. Such additional valuation techniques may need the use of unobservable inputs and would need to be calibrated to the initial transaction price (if determined to represent fair value) to ensure that the valuation technique reflects market conditions. These can also impact the categorisation of the FVM within the fair value hierarchy and changes thereto (e.g., transfer from Level 2 to Level 3 if unobservable inputs are significant to the FVM) that will drive the nature and extent of disclosures required by IFRS 13.

In addition, a significant decrease in the volume of transactions does not automatically imply that a market is no longer active. Despite a decrease from recent (or historical) levels of activity, transactions for an asset or liability in that market may still occur with sufficient frequency and volume to provide pricing information on an ongoing basis, such as an equity security traded on a public exchange. Where there is an active market for an identical asset or a liability at the measurement date, entities are required to use the quoted price at the measurement date in that market (i.e., Level 1 input) as the basis of FVM without adjustment. This is required even where higher volatilities are experienced in an active market near to the measurement date.

IFRS 13's fair value hierarchy requires valuation techniques to maximise the use of observable inputs from orderly transactions and minimise the use of unobservable inputs. Consequently, even where the market for an asset has become less liquid due to the current environment, relevant prices or inputs observed from orderly transactions in these markets must still be considered. It would be inappropriate for an entity to default solely to a model's value based on unobservable inputs such as income approach that uses only an entity's own inputs (a Level 3 measurement), when Level 2 (observable) information, such as recent transacted prices, is available. Judgement is required in assessing the relevance of observable market data and whether they reflect orderly transactions, particularly in situations where there has been a significant decrease in market activity for an asset or liability.

How we see it

IFRS 13 provides relevant guidance on FVM of assets and liabilities in markets that have experienced significant volatilities or reduction in volume or activity, which are particularly relevant in this current environment. The application of this guidance to arrive at a reasonable estimate of FVM requires significant management judgement and hinges on the robustness of the entity's FVM determination and review processes.

In certain cases, the changes to the existing valuation techniques and valuation adjustments required in response to the current market conditions may warrant assistance from external valuation specialists who possess the necessary expertise, experience and market knowledge.

Providing transparency over the techniques, key assumptions and inputs used in determining fair value, including the sensitivities by providing disclosures required by IFRS 13, is an integral part of FVM and is key to enhancing the usefulness of financial reporting in this unprecedented time.

13. Revenue recognition

The coronavirus outbreak could affect revenue estimates in ongoing customer contracts in the scope of IFRS 15 *Revenue from Contracts with Customers*. This is because when a contract with a customer includes variable consideration (e.g., discounts, refunds, price concessions, performance bonuses and penalties), an entity is generally required to estimate, at contract inception, the amount of consideration to which it will be entitled in exchange for transferring promised goods or services. The amount of variable consideration an entity can include in the transaction price is constrained to the amount for which it is highly probable that a significant reversal of cumulative revenue recognised will not occur when the uncertainties related to the variability are resolved.

An entity that makes such an estimate is also required to update the estimate throughout the term of the contract to depict conditions that exist at each reporting date. This will involve updating the estimate of variable consideration (including any amounts that are constrained) to reflect an entity's revised expectations about the amount of consideration to which it expects to be entitled, considering uncertainties that are resolved or new information about uncertainties related to the coronavirus outbreak. Estimation of variable consideration and the constraint may require entities to exercise significant judgement and make additional disclosures. For example, an entity is required to disclose information about the methods, inputs and assumptions used for estimating variable consideration and assessing whether an estimate of variable consideration is constrained. Entities should also consider the requirements to disclose the judgements and changes in judgements that significantly affect the determination of the amount and timing of revenue.

Uncertainties related to the coronavirus outbreak could also prompt entities to modify contracts with customers or reassess whether it is probable that the entity will collect the consideration to which it is entitled. If both parties to a contract agree to amend the scope or price (or both) of a contract, an entity should account for the modification under the contract modification requirements in paragraphs 18-21 of IFRS 15. Significant judgement is required to determine when an expected partial payment indicates that: (1) there is an implied price concession to be accounted for as variable consideration; (2) there is an impairment loss (see section 3 on Individual and collective assessment of loans, receivables and contract assets); or (3) the arrangement lacks sufficient substance to be considered a contract under the standard.

Significant judgement may be needed to determine the effect of uncertainties related to the coronavirus on both ongoing and future revenue contracts.

In addition to the effect on ongoing contracts, entities will need to consider how the uncertainties with the coronavirus outbreak affect future contracts with customers. This could require careful consideration of, for example, collectability, price concessions and stand-alone selling prices. Entities may also need to consider how evolutions in their customary business practices affect their assessments under the revenue model. This could, for example, have an effect on an entity's determination that a valid contract exists, its identification of performance obligations and its assessment of whether it has a right to payment for performance completed to date.

Refer to our publication ***Applying IFRS: A closer look at IFRS 15, the revenue recognition standard,*** for more information.

How we see it

Entities may need to use significant judgement to determine the effect of uncertainties related to the coronavirus outbreak on its revenue accounting, e.g., estimates of variable consideration (including the constraint) and provide appropriate disclosures. Importantly, the effects are unlikely to be limited to variable consideration. Decisions made in response to the outbreak (e.g., modifying contracts, transacting with customers during collectability concerns, revising pricing) may also have an effect on the accounting and disclosures for ongoing and future contracts.

14. Events after the reporting period

The distinction between an adjusting and non-adjusting event is based on whether the event provides evidence of conditions that existed at the end of the reporting period.

Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. IAS 10 makes a distinction between adjusting and non-adjusting events after the reporting period. The principal issues are how to determine which events after the reporting period are to be reflected in the financial statements as adjusting events and, for non-adjusting events, what additional disclosures to provide.

Recognition

The coronavirus outbreak occurred at a time close to the end of 2019. In late 2019, a cluster of cases displaying the symptoms of a 'pneumonia of unknown cause' were identified in Wuhan, the capital of China's Hubei province. On 31 December 2019, China alerted the World Health Organisation (WHO) of this new virus. On 30 January 2020, the International Health Regulations Emergency Committee of the WHO declared the outbreak a 'Public Health Emergency of International Concern'. Since then, more cases have been diagnosed, also in other countries. Measures were taken and policies imposed by China and other countries. On 11 March 2020, the WHO announced that the coronavirus outbreak can be characterised as a pandemic.

Many governments have introduced various measures to combat the outbreak, including travel restrictions, quarantines, closure of business and other venues and lockdown of certain area. These measures have affected the global supply chain as well as demand for goods and services. At the same time, fiscal and monetary policies are being relaxed to sustain the economy. These government responses and their corresponding effects are still evolving.

For entities that are affected, or expect to be impacted by the outbreak or by the measures taken, the critical judgement and evaluation that management need to make is whether and, if so, what event in this series of events provides evidence of the condition that existed at the end of the reporting period for the entity's activities or their assets and liabilities. When making this judgement, the entity takes into consideration all available information about the nature and the timeline of the outbreak and measures taken.

Disclosure

If management concludes an event is a non-adjusting event, but the impact of it is material, the entity is required to disclose the nature of the event and an estimate of its financial effect. For example, it may have to describe qualitatively and quantitively how the market volatility subsequent to year-end has affected its equity investments and governmental measures imposed on sporting and social activities and border controls have affected or may affect its operations, etc. If an estimate cannot be made, then the entity is required to disclose that fact.

How we see it

Entities need to ensure effective processes are in place to identify and disclose material events after the reporting period which could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements.

15. Other financial statement disclosure requirements

In addition to the disclosure requirements discussed in the above sections, IAS 1 requires disclosure of information about the assumptions concerning the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities, such as non-current assets subject to impairment, within the next financial year (with the exception of assets and liabilities measured at fair value based on recently observed market prices). The disclosures are required to be presented in a manner that helps users of financial statements to understand the judgements that management makes about the future and about other key sources of estimation uncertainty. The nature and extent of the information provided will vary according to the nature of the assumption and other circumstances. Examples of the types of disclosures that an entity is required to make include:

- The nature of the assumption or other estimation uncertainty
- The sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity
- The expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year in respect of the carrying amounts of the assets and liabilities affected
- An explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved

When it is impracticable to disclose the extent of the possible effects of an assumption or other source of estimation uncertainty at the end of a reporting period, the entity discloses that it is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions used could require a material adjustment to the carrying amount of the asset or liability affected.

An entity is also required to disclose the judgements, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Disclosure (for year end reporting purposes)

The financial statement disclosure requirements for entities directly and/or indirectly affected by the outbreak will vary depending on the magnitude of the financial impact and the availability of information. Where such a decline in value is determined to be non-adjusting in accordance with the guidance described in the earlier sections, the entity does not adjust the carrying amounts, but instead, disclose such a fact and its financial effect if it can be reasonably estimated.

The occurrence of the outbreak has certainly added additional risks that the carrying amounts of assets and liabilities may require material adjustments within the next financial year.

Because the outbreak may also result in obligations or uncertainties that an entity may not have previously recognised or disclosed, an entity also needs to consider whether to disclose additional information in the financial statements to explain the impact of the outbreak on areas that might include provisions and contingent assets/liabilities, in addition to asset impairments after the reporting period as discussed above.

For entities which have their next quarterly reporting timeline close to the issuance of their annual financial statements, it is possible that quantitative financial information about the impact of the outbreak may become available by the time they issue the annual financial statements. In that case, they should consider providing such quantitative disclosures in their annual financial statements, if the effect is material.

In relation to the assumptions and estimation uncertainty associated with the measurement of various assets and liabilities in the financial statements, the occurrence of the outbreak has certainly added additional risks that the carrying amounts of assets and liabilities may require material adjustments within the next financial year. Therefore, entities should carefully consider whether additional disclosures are necessary in order to help users of financial statements understand the judgement applied in the financial statements. Such disclosure may include, for a financial statement item with a carrying amount that is more volatile in response to the outbreak, a sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation.

How we see it

Entities need to consider the magnitude of the disruptions caused by the outbreak to their businesses and adequately disclose the information about those assets and liabilities that are subject to significant estimation uncertainty, in order to provide users with a better understanding of the financial impact.

Disclosure (for interim reporting purposes)

In accordance with IAS 34, an entity is required to 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 entity since the end of the last annual reporting period. Information disclosed in relation to those events and transactions should also update the relevant information presented in the most recent annual financial report. IAS 34 includes a number of required disclosures as well as a non-exhaustive list of events and transactions for which disclosures would be required if they are significant. For example, where significant, an entity needs to disclose changes in the business or economic circumstances that affect the fair value of the entity's financial assets and financial liabilities, whether those assets or liabilities are recognised at fair value or amortised cost. In addition, an entity is also required to disclose any loan default or breach of a loan agreement that has not been remedied on or before the end of the reporting period and transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments where significant. The standard presumes a user of an entity's interim financial report will have access to the most recent annual financial report of that entity. Therefore, it is unnecessary for the notes to an interim financial report to provide relatively insignificant updates to the information that was reported in the notes in the most recent annual financial report. However, as most entities are only recently impacted by the outbreak which is rapidly evolving, they may not have included much relevant information in their last annual financial reports and thus may need to include more comprehensive disclosure on, especially, where relevant, the topics discussed in this publication for interim financial reporting purposes.

While other standards specify disclosures required in a complete set of financial statements, if an entity's interim financial report includes only condensed financial statements as described in IAS 34, then the disclosures required by those other standards are not mandatory. However, if disclosure is considered to be necessary in the context of an interim report, those other standards provide guidance on the appropriate disclosures for many of these items. In light of these requirements and depending on the entity-specific facts and circumstances, higher-level disclosures may be sufficient in condensed interim financial statements.

16. Other accounting estimates

Apart from the above, the following are some of the other key accounting estimates required to be made by management under IFRS. These estimates generally include management's assumptions about the future recoverability of an asset:

- Net realisable value of inventories under IAS 2 *Inventories*
- Impairment charge of investments in associates and joint ventures accounted for in accordance with the equity method under IAS 28 *Investments in Associates and Joint Ventures*
- Remaining useful life and residual value of property, plant and equipment, intangible assets and right-of-use assets under IAS 16 *Property, Plant and Equipment*, and IAS 38 *Intangible Assets* and IFRS 16, respectively.

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