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COVID-19: Impact on Key Financial Reporting Areas

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ABSTRACT

The pandemic of the novel coronavirus (COVID-19) is spreading quickly across the world. The virus has taken a huge toll not only on human life, but also on companies and financial markets, the magnitude of which is ambiguous at present. Entities ought to consider the accounting consequences of this case carefully. Although the epidemic has had an effect either implicitly or explicitly on almost all entities, some of the worst-hit industries are aviation, tourism, and retail, with more and more industries coming under its radar with extensive lockdowns being implemented worldwide. This paper reviews key aspects of financial disclosure that companies need to address when assessing the effect on their organization and their financial reports on results, financial condition and disclosures.

Key Words: COVID-19, Financial reporting, Pandemic, Industries, Disclosure, Lockdown

INTRODUCTION

Financial reporting refers to the exchange of financial reports, such as financial statements, with recipients of financial statements, such as investors and creditors. Financial reporting is usually seen as financial statements issued by corporations. A balance sheet, income statement, owner's equity statement, and cash flow statement are a general purpose series of financial statements, but financial reporting is much broader than just a set of financial statements. It covers all financial communications, including press releases, shareholder minutes, management letters and analysis, auditor reports, and even financial statement notices, from the corporation to outside users. Basically, something that can relay financial information to the public is known as some sort of financial reporting.

LITRARTURE REVIEW

There has been a serious series of outbreaks of flu-like illnesses in the last two decades. These outbreaks have shown that the methods needed to monitor and curb transmittable diseases such as Serious Acute Respiratory Syndrome (SARS-Coronavirus) in 2003, Swine Influenza Pandemic (H1N1) in 2009, Avian Influenza (H7N9) in 2013 (Springborn et al., 2015) and Ebola Virus (World Bank, 2016) need to be constantly strengthened. In the short run, SARS-CoV has mainly impacted economic growth through demand reduction. In many countries, consumer morale has weakened dramatically, triggering a drastic decline in spending on personal consumption. Most of the effect comes from the great uncertainty of the initiated by the SARS virus and terror. To minimise the risk of being contaminated, people have chosen to stay at home (Fan, 2003). In addition, exports of services, especially tourism-related exports, have having been profoundly affected. Moreover, investments have been affected as the overall demand has reduced, fears exacerbated and threats amplified. The 2009 Swine influenza (H1N1) pandemic has resulted in numerous economic impacts, including a decline in hospitality, trade and retail consumption. The growing absence, which increased demand for various medical services, also had a negative effect on businesses and schooling (Verikios et al. , 2011) Avian influenza (H7N9) had a much less serious economic effect than that of SARS. This mainly resulted in the closure of live poultry markets and a decline in the meat and poultry price index, resulting in a loss of more than RMB 40 billion for the Chinese poultry industry. Nevertheless, in contrast to SARS, H7N9 had no global economic influence (Qiu et al. , 2018).

Today, the novel Coronavirus (COVID-19) continues to spread from one nation to another. The German government and the Robert Koch Institute have reported that it is predicted that the virus will continue to spread worldwide. There are a growing number of positive cases of the disease identified in Deutschland. This serious trend is already showing an economic effect on organisations because of supply and trade constraints or because of restrictions on travel. To check any material doubt regarding its ability to continue as a continuing concern, it must perform several possible forms of sensitivity analysis. The effect may be a necessity, particularly if there is some material uncertainty, for further disclosures. Management needs to take close note of the effect of the latest Coronavirus outbreak on both interim and annual financial statements, as it may be important for many organisations and industries. All organisations, not just those that are most significantly affected, should recognise the effects of the virus epidemic, which include the unintended effects arising from low economic activity (PwC, 2020). In disclosing significant threats and uncertainties, organisations must decide whether to disclose the possible effects of the COVID-19 outbreak on their industry. If mitigating operations can be performed, they must also be reported together with an explanation of what the risk is. The carrying value of assets and liabilities may also be influenced by the need to carry out more impairment checks and to determine whether leases become burdensome in addition to potential inclusion of key risks and uncertainties within the statements of a company (Parker Russell Intl., 2020). The researchers address the effect of the latest Coronavirus (COVID-19) outbreak on financial reporting in this paper, which involves not only the assessment of assets and liabilities, but also disclosure and the organisation's ability to continue as an on-going concern. The effects of the epidemic, including the indirect consequences arising from a low level of economic activity, must be taken into account by all forms of organisations, not just those most significantly affected.

OBJECTIVES OF THE STUDY

1. To identify the key financial reporting areas affected by COVID-19
2. To study the impact of COVID-19 on financial reporting

GOING CONCERN ASSUMPTION

The financial reports are typically prepared under the basis that, for the near future, a company is a continuing concern and will continue to function. Entity management the effect of COVID-19 and the measures taken on its ability to continue should be evaluated as an on-going concern. In deciding whether the presumption of concern is reasonable or not, it is also necessary to consider the impact of COVID after the reporting date.

INVENTORY

Any entities can experience delays in the supply chain. A fall in property prices may affect real estate firms with inventories and below-construction properties. Due to injury, pollution, physical degradation, obsolescence, changes in price levels or other factors, seasonal stocks and perishable items might be exposed to the risk of loss. Companies will need to determine whether an adjustment to the realizable amounts of their inventory is needed on their reporting date to get them to their net realisable value in compliance with the AS 2 'Inventories' principles.

In view of the uncertainty posed by the pandemic, estimating net realisable value in such unpredictable market conditions may also be a challenge. If the level of output of an entity is abnormally low (e.g. due to a temporary output shutdown), the inventory costs will need to be checked to ensure that unallocated fixed overheads are regarded as profit or loss over the duration in which they are incurred (i.e. 'excess capacity' should be expensed rather than added to inventory costs).

REVENUE RECOGNITION

Enterprises to whom AS is appropriate may have delayed the recognition of revenue in view of the effect of COVID-19 because of substantial collection uncertainty. Revenue Recognition AS-9 allows organisations to report the situations in which the identification of revenue has been delayed until substantial issues have been resolved.
If the entity's consumer contract covers variable components (e.g. discounts), then it must determine whether its initial estimates continue to be acceptable in this regard.

Some contracts for sales can even become less lucrative or even loss-making. For example, due to delays or incurring additional expenses that cannot be recovered due to replacing staff or seeking substitute providers, an agency can face penalties. Management has to determine whether any contracts are in an 'onerous' situation and whether it is appropriate to accept a liability / provision.

Onerous contracts are those contracts under which the inherent costs of meeting treaty duties outweigh the economic benefits that the contract is meant to bring. The minimum net cost of quitting the contract, the lower the cost of fulfilling it, and any benefits or penalties arising from the failure to execute the contract it, are unavoidable costs under a contract. As a result of COVID-19, such contracts are costly for reasons such as the imposition of penalties as a result of delays in the delivery of goods or rises in the cost of materials, labour, etc. Business should determine whether any of its arrangements have become burdensome. As per AS 29, the same should be accounted for. Company should report that, because of the adverse effects of COVID -19, it has determined whether executor contracts are onerous. If, due to the inadequacy of details, administration is unable to determine if any of the executive contracts have become onerous, the same should be revealed.

PROPERTY, PLANT AND EQUIPMENT (PPE) & INTANGIBLE ASSETS

- PPE may remain under-used or not used for a period of time because of COVID-19. It should be remembered that, even if the PPE remains idle, the requirements require depreciation charges. In addition, the expected useful life and residual life of PPE may have been affected by the COVID-19 effect.

- Major changes The degree or way in which the asset is used or is scheduled to be used (e.g. idling a machine to affect its future productivity growth, a machine being used in a way that is different from its intended intent, such as manufacturing products to support the fight against COVID-19, which may reduce its future economic output

- Major changes in the legal or economic environment that could impact the valuation of the asset (e.g. an entity expects its exports to a specific foreign market to decline as a result of long border closures). In addition, uncertainty about the capacity of the company to survive as an on-going issue is a general impairment measure for all properties.

EMPLOYEE BENEFITS

- Some entities have or may downsize their workforce as a result of tough economic conditions. If the company provides or is expected to pay the affected employee(s) termination compensation, management must consider how and when the liability / expense are compensated for.

- Estimating and using assumptions (e.g. the required interest rate, potential pay increases, and employee turnover) are involved in calculating a defined benefit obligation. An organisation should recognise the effect on its defined benefit obligation(s) in view of the sudden fall in markets and the decrease in high-quality corporate bond rates that have occurred as a result of COVID-19.

- Corporations should have consultations with their actuaries to decide if any assumptions in their reports have been changed by COVID-19 so that their calculations might need to be revisited. Guidance for future events on whether an adjustment or non-adjustment event should occur should also be considered.

INVESTMENTS (OTHER THAN PORTFOLIO INVESTMENTS)

With regard to financial assets falling beyond, companies would have to take careful account of the criteria of AS-13, Accounting for Assets, to allow for a decrease in the value of assets, which is not temporary.

BORROWING COST/DEBT REPAYMENT

- AS-16 requires that when the production of an asset is suspended, the capitalization of interest is suspended. This factor will be regarded by the management when determining the effect of COVID-19.
- Some financial institutions (and other creditors) give debt holders the possibility to delay principal payments for a certain period of time. Companies will need to determine whether the adjustment in terms reflects an adjustment or reduction of the debt obligation and re-examine the aspect of the debt that is deemed current compared with non-current.

FOREIGN CURRENCY TRANSLATION

An entity is expected to convert transactions in a foreign exchange into a reporting / functional currency at the spot rate effective on the date of the transaction. An organisation can convert income earned and expenditure incurred in a foreign exchange using an average rate as a practical expedient. Some currency fluctuations, however, are significantly fluctuating during this time of economic uncertainty. As a consequence, an organisation can need to re-examine in its income statement the manner in which it translates foreign currency transactions and determine whether its current accounting is sufficient.

INSURANCE CLAIMS FOR BUSINESS INTERRUPTION

An individual may have an insurance policy which covers business interruption losses. If, as a consequence of COVID-19, an organisation is required to temporarily suspend operations, it may be entitled to recover any or all of its damages from its insurance company. Such claims in the financial reports would be contingent assets if the company had a clear right to repayment. Although contingent gains / assets in the financial statements of an organisation are not acknowledged until they are practically assured,

LEASE TERM AND CONTRACTS

- There may be adjustments in the terms of the lease agreements due to COVID-19, or the lessor may grant the lessee a certain concession with respect to the lease payments. Such amended terms and conditions or compromises are to be considered during lease accounting. The expected revision should not, however, be taken into consideration. Any potential risks associated with COVID-19 which need to be integrated into the discount rate used to calculate the present value of lease payments for new leases.

- Where any reimbursement is granted / reported by the Government to the lessor for the granting of the concession to the lessee, it should be considered if the same needs to be properly accounted for in accordance with AS 19. If government grants under AS 12 are any assistance provided from the government. Entities would need to specify whether any leasing agreement has become onerous as a result of COVID -19. As per AS-29, the same should be accounted for.

IMPAIRMENT ASSESSMENT

- At the conclusion of each reporting cycle, AS 28 Impairment of Assets allows an agency to determine if there is any evidence that non-financial assets could be affected. There may be a temporary suspension of operations or an immediate drop in demand or prices due to COVID-19, resulting in a reduction in sales and profitability and a drop in economic activity. These are the variables which may be regarded by management as indications which may involve disability testing for the purposes of AS 28

- If the agency is unable to determine the effect of COVID-19 on the assessment of the disability loss due to knowledge inadequacy, the same should be properly reported.

STATUTORY DUES

The submission of legislative dues, such as the Provident Fund, the Employee Provident Fund and the Goods and Services Levy, will also impact cash flow problems which results an adverse opinion in audit report.

PRESENTATION OF FINANCIAL STATEMENTS

Any significantly affected company can explain the low profitability with an additional presentation of line items because of Covid-19. If items of revenue or expenditure are material, the agency shall report their existence and amount separately, and the reason and details may be clarified by separate disclosure undertakings. When reviewing for quantification, the task will be for business to explain the reasoning and for the auditor to certify the same.

CONCLUSIONS AND RECOMMENDATIONS

The study rendered important findings about the impact of the COVID-19 outbreak on financial reporting. The outbreak of the novel COVID-19 will undoubtedly have huge financial implications for the 2020 financial year. Furthermore, the COVID-19 outbreak can impact the activities of an entity and its financial status. It is not possible to measure the effect of the COVID-19 outbreak reasonably, as this The incident occurred at the end of 2019 and continues. Based on this, some of the outbreak's effects will be evident later in 2021, although others might not be apparent in the short term. The COVID-19 has impacted the key area of financial reporting to the greatest extent. The researchers conclude that the preparation of interim financial statements is a must for organisations to disclose the effects of the outbreak of COVID-19, along with the continuous disclosure of all relative details regarding all incidents encountered by the organisations during the time reported. In addition, the on-going review of the analysis of major risks and uncertainties that lead to the required disclosures is functional.

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