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ESMA Issues Public Statement on Implications of COVID-19 Pandemic on Half-Yearly Financials

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On May 20, 2020, the European Securities and Markets Authority issued a public statement on the impact of the COVID-19 pandemic on the half-yearly financials of listed issuers. In particular, ESMA addressed the preparation of interim financial statements according to International Financial Reporting Standards and interim management reports for 2020 half-yearly reporting periods.

Timing of publication

ESMA acknowledges that some issuers may consider setting the timing of publication of their half-yearly financial reports later than usual within the available time span, but reminds issuers to continue to comply with the Market Abuse Regulation in providing timely, relevant and reliable information.

Issuers should carefully consider the impact on their financial statements of any material events occurring after the end of the reporting period and provide the relevant disclosures in accordance with paragraph 16A(h) of International Accounting Standard (IAS) 34.

Half-yearly financial statements

Application of IAS 34

- ESMA reminds issuers that the extent of the information provided should be proportionate to the objective of providing an update on the latest complete set of annual financial statements, including, as indicated in paragraph 6 of IAS 34, new activities, events and circumstances that have not been captured in the most recent annual financial statements. It is expected that the impact of COVID-19 will, for a large proportion of issuers, warrant extensive disclosure and constitute a "significant event" under paragraphs 15-15C of IAS 34.
- ESMA emphasises that paragraphs 17 and 31 of IAS 1 Presentation of Financial Statements require additional disclosures to those required by individual IFRSs – beyond the minimum disclosures required by IAS 34 – when necessary to enable a user's understanding of the impact of particular transactions, other events and conditions. Accordingly, some of the disclosures that are normally required by individual IFRSs for a complete set of annual financial statements may be used to provide relevant information on the consequences arising from the COVID-19 pandemic in the condensed financial statements for the half-year.
- ESMA notes that one of the key consequences of the current situation is the availability of various relief and support measures for which an issuer's entitlement to the programme may require compliance with particular conditions. ESMA recommends that issuers provide transparency regarding the application of these measures in terms of eligibility, conditions and consequences, as well as in terms of the underlying judgements they made. In accordance with paragraph 15C of IAS 34, ESMA encourages issuers to consider the relevant disclosure requirements in the individual IFRSs based on which such measures are accounted for (e.g., IAS 20 Accounting for Government Grants and Disclosure of Government Assistance, IAS 12 Income Taxes, IFRS 16 Leases).

Disclosures reflecting significant uncertainties, going concern and risks linked to COVID-19

- The COVID-19 pandemic has introduced uncertainty in the conduct of most businesses and, as a result, a significant risk of material adjustment to the carrying amounts of assets and liabilities may have arisen.
- ESMA urges issuers to update the assessment made at year-end about the assumptions regarding the future and other major sources of estimation uncertainty as provided in accordance with paragraph 125 of IAS 1. Issuers are reminded that

paragraph 16A(d) of IAS 34 requires disclosures of the nature and amount of changes in estimates of amounts reported in prior interim reporting periods of the current financial year or changes in estimates of amounts reported in prior financial years.

- ESMA notes that the uncertainties arising from the COVID-19 pandemic may in some cases cast doubt on an issuer's ability to continue as a going concern. When this is the case, in accordance with paragraph 25 of IAS 1, the entity shall disclose those uncertainties. ESMA expects that in making the assessment of their ability to continue as a going concern, issuers shall take into account all available information about the future (at a minimum 12 months from the end of the reporting period), including the expected profitability and any restrictions to readily access financial resources.
- ESMA highlights that, in the context of the annual financial statements, the IFRS Interpretations Committee in July 2014 noted the need for issuers to disclose the judgements based on which the management has concluded that no material uncertainties remain on the issuer's ability to continue as a going concern, if reaching this conclusion required significant judgement. ESMA expects issuers most significantly impacted by COVID-19 to provide disclosures in half-yearly financial statements about the going concern assessment and the related underlying judgements where these are significant.
- The COVID-19 pandemic may have triggered financial risks which were in full or in part unknown or not relevant at the end of the last annual reporting period. Events and transactions that might unveil these risks include, for example, debt renegotiations, new financial arrangements and the breach of debt covenants. In this respect, ESMA reminds issuers of the importance of providing disclosures regarding those risks and to consider the requirements in IFRS 7 Financial Instruments: Disclosures regarding, in particular, the exposures of issuers to credit, liquidity and other risks and the related sensitivities, in order to provide the necessary updates of the information presented in the latest annual financial statements. ESMA highlights that some of these disclosures are also relevant in relation to the calculation of expected credit losses in accordance with IFRS 94, including disclosures to explain the assumptions and judgements applied and other considerations addressed in ESMA's public statement.

Impairment of non-financial assets

- ESMA reminds issuers that, in accordance with paragraphs 9 and 12 of IAS 36, they should assess whether there are any indications that an asset may be impaired on the basis of a set of internal and external sources of information. In making this assessment, issuers should carefully consider the effects of the COVID-19 outbreak which, in ESMA's view, would most likely constitute a strong basis to conclude that one or more of the impairment indicators in IAS 36 have been triggered.
- ESMA notes that determining the recoverable amount in the current uncertain environment requires a careful assessment of the cash-flow projections over a relevant horizon. Such projections may require, especially in the current circumstances and depending on the level of risk associated with the asset being tested, the consideration of multiple scenarios. The weighting of the different scenarios needs to be calibrated on the basis of reasonable, supportable and realistic estimates and assumptions in order to avoid the risk of overly optimistic or pessimistic biases.
- ESMA highlights that, according to paragraph 55 and 56 of IAS 36, the discount rates used shall reflect current market assessments of the time value of money and the risks specific to the asset being tested and exclude risks and uncertainties that were already taken into account in the projected cash-flows. ESMA notes that, in accordance with paragraph 23 of IAS 36, estimates, averages and other computational shortcuts could also be used to provide reasonable approximations of more detailed computations. However, ESMA considers that the use of such approximations should be carefully assessed, taking into account the level of risk that an impairment loss may occur for the assets being tested.
- ESMA reiterates the importance to issuers of updating the disclosures relating to the significant judgements and assumptions underlying these assessments and the sensitivity analyses (e.g., by expanding the range of reasonably possible changes of key assumptions), as required by paragraphs 122 and 125 of IAS 1 and paragraphs 134(d) and 134(f) of IAS 36, as ESMA expects this update to be significant to an understanding of the changes in an entity's financial position or performance since the last annual reporting period.

Presentation of COVID-19 related items in the statement of profit or loss

- ESMA calls for caution regarding any separate presentation of the impacts of the COVID-19 pandemic in issuers' profit or loss statement as, due to their pervasiveness, such separate presentation may not faithfully present issuers' overall financial performance, position and/or cash-flows, thus being to the detriment of users' understanding of the financial statements.
- In light of these considerations, ESMA instead encourages issuers to provide information, also on a quantitative basis, on the significant impacts of the COVID-19 outbreak as part of the explanations of the amounts presented and recognised in the statement of profit or loss in a single note as part of the notes to the financial statements.

Other disclosure requirements applicable to half-yearly financial statements

- Apart from the items explicitly mentioned above, ESMA highlights that issuers should consider whether other requirements in IFRS are also relevant in the context of their half-yearly financial reporting. These requirements include, but are not limited to, the recognition of deferred tax assets and tax reliefs in accordance with IAS 12, fair value measurement in accordance with IFRS 13 Fair Value, provisions and onerous contracts in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets, and insurance contracts liabilities.
- ESMA recommends that issuers closely monitor the developments in relation to the accounting for COVID-19-related lease concessions based on the expected IASB's amendments to IFRS 16 and the related endorsement process at European level, where material to their specific situation.

Interim management reports

- ESMA recommends that issuers provide detailed and entity specific information in their interim management reports regarding:
    - The impact that the COVID-19 pandemic had on their strategic orientation and targets, operations, financial performance, financial position and cash-flows (in particular, details of the issuer's liquidity position and its liquidity risk management strategy, decrease of revenues, disruptions in supply chains and/or production).
    - Measures taken to address and mitigate the impacts of the COVID-19 pandemic on their operations and performance and their progress/state of completion (including, but not limited to, information of whether issuers have applied or are considering to apply for public support measures, details regarding the nature, amounts and conditions of such assistance, the planned renegotiation of major contracts).
    - Where available, the expected future impact on issuers' financial performance, financial position and cash-flows, related risks and contingency measures planned to mitigate the expected future impact and risk and uncertainties identified.
- In order to complement the information provided above and to facilitate users' understanding, issuers should also include narrative information regarding the estimates and judgements made, as well as assumptions used to determine the future impact of the COVID-19 pandemic on the business of the issuer and how the different uncertainties faced affected the estimates made and the strategy undertaken by the issuer to address the impact of COVID-19.
- Finally, ESMA notes that a new Q&A on the ESMA Guidelines on Alternative Performance Measures in the context of COVID-19 was published and highlights that any new COVID-19 related sub-totals qualifying as APMs and presented simultaneously inside and outside the financial statements are subject to the principles and disclosure requirements provided for in ESMA's Guidelines on APMs and further explained in ESMA's Q&A document. For further information, please refer to our recent alert, ESMA Issues COVID-19 Q&A on Alternative Performance Measure.

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