DEWAN P.N. CHOPRA & CO.

Impact of Covid-19 on Financial Statements

IMPACT OF COVID-19 ON FINANCIAL STATEMENTS

Brief On COVID-19

COVID-19, an infectious disease caused by a novel Coronavirus is exponentially spreading illness and causing deaths to citizens throughout the globe and has been recognized as a global pandemic by the WHO.

The various governments are taking drastic measures, including locking down of entire country to reduce the impact of this catastrophe. You are already aware that these disruptions are hugely impacting businesses significantly and bring with it several issues and challenges to preparers of financial statements and auditors on various aspects concerning preparation and audit of financial statements.

Keeping in mind the above, following important areas need attention:

Impact of COVID-19 on Presentation of Financial Statements, Consolidated Financial Statements, Property Plant and Equipment, Borrowing Cost (IND AS 1, IND AS 110/AS-21, IND AS 16/AS-10, IND AS 23)

1. Presentation of Financial Statements [Ind AS 1]

- **Breach of loan covenants (including classification of liabilities into current and non-current)**

  Ind AS 1- Due to COVID-19 there may be instances of breach of loan covenants which may trigger the liability becoming due for payment and liability becoming current. However, as per paragraph 74 of Ind AS 1, such a liability shall not be classified as current, if the lender agreed, after the reporting period and before the approval of the financial statements for issue, not to demand payment as a consequence of the breach.

- **Sources of estimation uncertainty under Ind AS 1**

  Paragraph 125 of Ind AS 1, Presentation of Financial Statements, requires an entity to disclose information about the assumptions it makes about the future, and other major sources of estimation of 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 within the next financial year. COVID-19 may have created many uncertainties about the likely future scenarios which may affect the estimations of amounts recognised in the balance sheet as of reporting date. Entities shall be guided by the prescriptions in paragraphs 125 to 133 of Ind AS 1.

- **Comparative information**

  Ind AS 1 requires presentation of minimum comparative information. Framework for the preparation and presentation of financial statements under Ind AS considers comparability as an important qualitative characteristic of financial statements. The Framework requires that users must be able to compare the financial statements of an entity through time in order to identify trends in its financial position and performance and also compare it with financial statements of other entities. COVID-19 may have affected the financial performance and financial position of entities. Therefore, preparers may consider making adequate disclosures and explanatory notes regarding the impact of COVID 19 on its financial position, performance and cash flows.

2. Consolidated Financial Statements [Ind AS 110 / AS 21]

Ind AS 110 prescribe that the financial statements of parent and subsidiaries used in the preparation of the consolidated financial statements are usually drawn upto the same date. It may be noted that in any case, the difference between the reporting dates should not be more than three months.

3. Property Plant and Equipment (PPE) [Ind AS 16/ AS 10]

Ind AS 16 and AS 10 require that useful life and residual life of PPE needs revision in annual basis. Due to COVID-19, PPE can remain under-utilized or not utilized for a period of time. It may be noted that the standards require depreciation charge even if the PPE remains idle. Further, COVID-19 impact may have affected the expected useful life and residual life of PPE.

The management may review the residual value and the useful life of an asset due to COVID 19 and, if expectations differ from previous estimates, it is appropriate to account for the change(s) as an accounting estimate in accordance with Ind AS 8, Accounting Policies, Changes in Accounting Estimates and Errors and AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies.

4. Borrowing Costs [Ind AS 23 / AS 16]

Above standards require that the capitalisation of interest is suspended when development of an asset is suspended. The management may consider this aspect while evaluating the impact of COVID-19.

The Impact of COVID-19 on Inventories Valuation (IND AS 2)

The COVID-19 pandemic may affect the recoverability of inventory balances. Some entities with inventories that are seasonal or are subject to expiration may have to assess whether a write-down for obsolescence or slow-moving stock may be necessary at an interim or annual period as a result of a slower sales pace. Other entities may have to assess whether a decline in their future estimated selling price is expected, which may require a write-down in the cost of inventory in an interim or annual period.

Applying IAS 2 *Inventories*, inventories are measured at the lower of their cost and net realisable value (NRV). In a difficult economic environment, the NRV calculation may be more challenging and require more detailed methods or assumptions. Interim inventory impairment losses should be reflected in the interim period in which they occur, with subsequent recoveries recognised as gains in future periods.

In addition, manufacturing entities may have to reassess their practices for fixed overhead cost absorption if production volumes become abnormally low during the year as a result of plant closures or lower demand for their products.

Ind AS 2 requires that variable production overhead costs should be allocated to each unit of production based on the **actual use** of the production facilities. It also calls for the allocation of fixed overhead costs to each unit of production based on the **normal capacity** of the production facilities.

The COVID-19 pandemic may affect manufacturing entities in a number of ways (e.g. shortages of labour and materials or unplanned factory downtime) that, if sustained, may result in an abnormal reduction of an entity's production levels. In such circumstances, an entity should not increase the amount of fixed overhead costs allocated to each inventory item. Rather, the unallocated fixed overhead costs are recognised in profit or loss in the period in which they are incurred.

Applying Ind AS 2/AS-2 Inventories, inventories are measured at the lower of their cost and net realisable value (NRV). In a difficult economic environment, the NRV calculation may be more challenging and require more detailed methods or assumptions. Interim inventory impairment losses should be reflected in the interim period in which they occur, with subsequent recoveries recognised as gains in future periods.

In addition, manufacturing entities may have to reassess their practices for fixed overhead cost absorption if production volumes become abnormally low during the year as a result of plant closures or lower demand for their products. Ind AS 2/AS-2 requires that variable production overhead costs should be allocated to each unit of production based on the actual use of the production facilities. It also calls for the allocation of fixed overhead costs to each unit of production based on the normal capacity of the production facilities.

The COVID-19 pandemic may affect manufacturing entities in a number of ways (e.g. shortages of labour and materials or unplanned factory downtime) that, if sustained, may result in an abnormal reduction of an entity's production levels. In such circumstances, an entity should not increase the amount of fixed overhead costs allocated to each inventory item. Rather, the unallocated fixed overhead costs are recognised in profit or loss in the period in which they are incurred.

Entities should assess the significance of any write-downs and whether they require disclosure in accordance with Ind AS 2/AS 2 as well as paragraph 98 (a) of Ind AS 1, Presentation of Financial Statements, and paragraph 14(a) of AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies. It is unlikely that the normal production capacity is to be reviewed for allocating fixed production overheads for the year 2019-2020, because of adverse impact on the utilisation of the production capacity due to the impact of coronavirus on the overall economy or the segment (s) in which the entity is operating.

The Impact of COVID-19 on Employee Benefit Expenses (IND AS 19/ AS-15)

The COVID-19 pandemic may affect the many companies' employee benefits expenses. That can impact on the following:

- Changes to Remuneration Policies
- Updating Estimates including actuarial assumptions
- Impact on Share Based Payments
- Changes to Remuneration Policies

Some companies may offer their employees paid absence in addition to any sick or annual leave entitlement. If new paid absence entitlements do not accrue through past service and do not accumulate, then it is unlikely that a company would recognise a liability for these paid absences. Instead, it would expense the cost as absences are taken. Companies will need to consider, more generally, whether they have any legal or constructive obligations to its employees as a result of these events.

If a company implements a restructuring plan that includes employee redundancies, then it recognises an expense and a corresponding liability for termination benefits at the earlier of when it:

- Recognizes a restructuring provision under Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets that includes the payment of termination benefits; and can no longer withdraw the offer of those benefits.
- A company recognises a restructuring provision when it has a formal plan with sufficient detail of the restructuring and has raised a valid expectation in those affected by the plan – i.e. it has either started to implement the plan or has announced the main features to those affected by it.
- Updating estimates, including actuarial assumptions

- Companies may need to consider the potential impact on estimates, including actuarial assumptions used in measuring employee benefits.

During periods of mandatory quarantine or lockdowns, employees could be required to use existing employee entitlements – e.g. sick or annual leave entitlements. Therefore, companies may need to consider the impact on the measurement of employee benefits – e.g. they may need to revise estimates of the likelihood and timing of employees using these entitlements.

There could also be an impact on certain demographic and financial assumptions used to measure these benefits – e.g. the discount rate used to measure the present value of employee benefit obligations.

Companies preparing interim financial statements should consider whether net defined benefit obligations/assets need to be remeasured. Under Ind AS 19 / AS -15 Employee Benefits, re-measurements are recognised in the period when they arise; therefore, if adjustments at the interim reporting date are considered to be material, then they will need to be recorded at that date. An updated measurement of plan assets and obligations is required when a plan amendment, curtailment or settlement is recognised. In addition, significant market fluctuations may trigger the need for an updated actuarial valuation.

Practically, many companies obtain actuarial valuations a few months before the reporting date. This is acceptable if the valuation is adjusted for material subsequent events up to the reporting date. Therefore, companies should consider the timing of their actuarial valuation reports and whether they reflect material events between the valuation and reporting date.

Share-Based Payments

Companies with share-based payments whose vesting depends on achieving non-market performance conditions – e.g. earnings per share targets – may need to revise their estimate of the number of instruments expected to vest, which would impact the charge in the income statement over the remaining vesting period. However, expectations of achieving market performance conditions – e.g. achieving a specified total shareholder return and non-vesting conditions – and grant-date fair value are not revised.

Modifications to share-based payment arrangements will need to be assessed as to whether they are either beneficial or non-beneficial to the employee and accounted for accordingly. For example, if plans are modified such that market conditions are easier to achieve, then this may constitute a beneficial modification which increases the value of the award in the hands of the employee. In this case, the incremental fair value is recognised over the modified vesting period.

Actions for management to take now

- Consider the appropriate accounting for new employee benefit arrangements – e.g. new remuneration policies.
- Assess when to recognise an expense and corresponding liability for termination benefits.
- Update estimates, including actuarial assumptions used to measure employee benefits, as appropriate.
- In preparing interim financial statements, consider the need for updated actuarial valuation reports and whether any plan re-measurements should be recognised.
- For any actuarial valuation reports obtained before the reporting date, consider how to reflect material events occurring between the valuations and reporting dates.

- Update the estimate of the number of awards that will vest for achieving non-market performance conditions in share-based payment arrangements.
- Evaluate whether modifications to share-based payment arrangements are non-beneficial or beneficial.

The Impact of COVID-19 on Government Grants (IND AS 20)

Identifying Government Grants

Indian Accounting Standards include accounting requirements specifically for government assistance in the form of a government grant. Therefore, companies need to consider the distinction between government grants and other forms of assistance carefully. Ind AS 20 defines a government grant as a transfer of resources in return for past or future compliance with certain conditions relating to the operating activities of the company.

Government grants may come in many forms. For example, companies may receive grants in the form of forgivable loans, below-market interest rate loans, waivers of expenses, non-monetary assets and other subsidies. However, government assistance in the form of benefits that are available when determining taxable profit or tax loss, or are determined on the basis of a company's income tax liability, are not in the scope of Ind AS 20.

Accounting for Government Grants

A company recognises a government grant when it has reasonable assurance that it will comply with the relevant conditions and the grant will be received. This may be a judgmental matter, particularly when governments are introducing new programme that may require new legislation, or for which there is little established practice for assessing whether the conditions to receive a grant are met.

If the conditions are met, then a company recognises government grants in profit or loss on a systematic basis and in line with its recognition of the expenses that the grants are intended to compensate.

Companies need to consider the conditions associated with the grant carefully to determine whether it compensates expenses already incurred or future costs.

Measurement and presentation of government grants depends on the nature of the grant and the company's accounting policies. For example, companies may need to develop accounting policies for:

- grants in the form of non-monetary assets – whether to measure at nominal or fair value
- grants related to assets – whether to deduct the grant from the cost of the asset (net presentation) or present the grant separately as deferred income to be amortised over the useful life of the asset (gross presentation); and
- grants related to income – whether to offset the grant against the related expenditure or to include it in other income.

Actions for Management to Take Now

- Monitor government actions and legislation to identify all assistance that may meet the definition of a government grant.
- Develop accounting policies and procedures for government grants.
- Consider expanding disclosures on the accounting policies for government grants and the impact of grants and other assistance on the financial statements.

Impact of COVID-19 on Non-Financial Assets (IND AS 36)

Impairment under Ind AS 36 "Impairment of assets"

Ind AS 36 *Impairment of Assets* applies to a variety of non-financial assets including property, plant and equipment, right-of-use assets, intangible assets and goodwill, investment properties measured at cost and investments in associates and joint ventures. Following needs to assess:

- Investment in Subsidiary, Associates and Joint Ventures
- Goodwill and Other Non-Financial Assets
- Impact on Useful life and Residual Value

Investments in Subsidiary, Associates and Joint ventures

The guidance in Ind AS, Investments in Subsidiary, Associates and Joint Ventures is used to determine whether it is necessary to perform an impairment test for investments in equity-accounted investees. If there is an indication of impairment, then the impairment test follows the principles of Ind AS 36.

Goodwill and other Non-Financial Assets

Ind AS 36 requires goodwill and indefinite-lived intangible assets to be tested for impairment at least annually and other non-financial assets when there is an indication of possible impairment (a triggering event). It provides examples of indicators of triggering events, including:

- when significant changes have taken place during the period (or will take place in the near future) in the market or in the economic environment in which the company operates and these changes will have an adverse effect on the company; and

- when the carrying amount of the company's net assets is higher than its market capitalisation.

The impacts of Covid-19 have caused a significant deterioration in economic conditions for many companies and an increase in economic uncertainty for others, which may constitute triggering events.

- Certain sectors have been significantly impacted – e.g. travel tourism, entertainment, retail, construction, manufacturing, insurance and education.
- Companies in extractive industries may also have been significantly affected by decreases in commodity prices and companies in countries that are economically dependent on these commodities may also be exposed to a greater risk of adverse economic impacts.

  Certain types of investment properties (and right-of-use assets arising from leased real estate) – e.g. retail and industrial properties – may be considerably affected by Covid-19.

- Tenants that have been forced to suspend operations may not be able to pay rent in the near term or may ask to renegotiate a lower rent. They may also become less creditworthy. Similar considerations would also apply for companies that lease assets (e.g. aircraft and shipping vessels) to the transport sector.

Management should consider whether:

- COVID-19 and the measures taken to control it are likely to reduce future cash inflows or increase operating and other costs for the reasons described above;
- these events, including for example a fall in an entity's share price such that market capitalisation is lower than carry value, are an indicator of impairment requiring that goodwill and indefinite lived intangible assets are tested outside of the annual cycle or that other assets are tested;
- the assumptions and cash flow forecasts used to test for impairment should be updated to reflect the potential impact of COVID-19;
- budgets, forecasts and other assumptions from an earlier impairment testing date that were used to determine the recoverable amount of an asset should be revised to reflect the economic conditions at the balance sheet date, specifically to address increased risk and uncertainty;
- an expected cash flow approach (multiple probability-weighted scenarios) might be a better way to estimate recoverable amount than a single predicted outcome to capture the increased risk and uncertainty. The potential impact of measures taken to control the spread of the virus could be included as additional scenarios in an expected cash flow approach. There might be a range of potential outcomes considering different scenarios;
- the factors used to determine the discount rate, however the recoverable amount is determined, should be revised to reflect the impact of the virus and the measures taken to control it, for example the risk-free rate, country risk and asset risk.

- The discount rate used in a single predicted outcome approach should be adjusted to incorporate the risk associated with COVID-19. Management should ensure that appropriate risk is reflected in either the cash flows or the discount rate.

Whichever approach management chooses to reflect the expectations about possible variations in the expected future cash flows, the outcome should reflect the expected present value of the future cash flows. When fair value is used to determine the recoverable amount, the assumptions made should reflect market participant assumptions.

Impact on Useful Life and Residual Value

If recent events have changed the company's usage or retention strategy for any of its property, plant and equipment, then management should review whether the useful life and residual value of these assets, and the depreciation method applied to them, remains appropriate. This review may also be required after testing a CGU or an asset for impairment. Any such changes are accounted for prospectively as a change in accounting estimate.

Disclosure

Annual reports

In the context of impairment testing of goodwill and indefinite-lived intangible assets, Ind AS 36 requires disclosure of the key assumptions used to determine the recoverable amount. It also requires sensitivity disclosures if a reasonably possible change in a key assumption would cause the CGU's carrying amount to exceed its recoverable amount. Furthermore, Ind AS 1 Presentation of Financial Statements requires disclosure of the key assumptions that a company makes about the future and other major sources of estimation uncertainty at the reporting date that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities in the next financial year.

Because the uncertainty associated with management's assumptions about the future is likely to be significant, it is important that management develops robust disclosures to help users understand the degree of estimation uncertainty that exists in estimating the recoverable amount and the sensitivity of the recoverable amount to reasonably possible changes to key assumptions. For example, it may be appropriate to disclose management's views about the degree of uncertainty associated with the macroeconomic outlook (such as the severity and duration of the impact that Covid-19 is expected to have on the company's business) and/or the potential significance of disruption to the supply chain, factory shutdowns, fall in demand etc.

Interim condensed reports

Ind AS 34 Interim Financial Reporting requires disclosure of the nature and amount of changes in estimates. Impairment losses are examples of events and transactions that require disclosure under Ind AS 34 if they are significant.

Ind AS 36 disclosures are not required in interim condensed financial statements. However, given the current economic uncertainties – and depending on the circumstances of the company – providing some or all of the disclosures required by Ind AS 36 may be helpful to users in understanding management's assessment of the economic outlook and how different scenarios could impact the recoverability of assets.

The Impact of COVID-19 – Provisions, Contingent Liabilities and Contingent Assets(IND AS 37/ AS-29)

Due to COVID-19, there is a need for exercising judgement in making provisions for losses and claims. A provision may be accounted for only to the extent that there is a present obligation for which the outflow of economic benefits is probable and can be reliably estimated.

Ind AS 37/AS-29 does not permit provisions for future operating costs or future business recovery costs. However, it requires that an entity should disclose the nature of the obligation and the expected timing of the outflow of economic benefits.

Ind AS 37 requires a provision to be recognised only

- where an entity has a present obligation
- it is probable that an outflow of resources is required to settle the obligation; and
- a reliable estimate can be made.

Entities to Whom Ind AS is Applicable

Provisions, Contingent Liabilities and Contingent Assets

1. Onerous contracts

Indian Accounting Standards provide specific guidance for onerous (loss making) contracts – i.e. those in which the unavoidable costs of meeting the obligations exceed the economic benefits expected to be received under the contract. The unavoidable costs are the lower of the net costs of fulfilling the contract and the cost of terminating it.

A sales contract may become onerous if costs rise or are expected to rise – e.g. because the company needs to stop production, find an alternative supplier or hire additional employees. A sales contract may also become onerous if benefits are expected to be lower – e.g. because a fall in demand affects the pricing. When assessing the unavoidable costs, companies should consider the contract terms carefully, including termination and force majeure clauses.

When preparing projections of costs and benefits for the onerous contract test, a company needs to reflect expectations at the reporting date and use assumptions that are consistent with those used for other recoverability assessments – e.g. impairment of non-financial assets. As the situation surrounding Covid-19 is rapidly changing, a company may need to update projections it made before the reporting date to reflect the information available, conditions and outlook at the reporting date.

The provision for an onerous contract is discounted if the effect of the time value of money is material. Central banks in many countries are cutting interest rates in response to increasing concerns about the economic impact of Covid-19; this in turn may impact risk-free rates, which are often used to discount provisions. Companies need to update the discount rate if it has changed.

Before recognising a provision for an onerous contract, a company tests all assets dedicated to the contract for impairment.

Additionally, there could be losses from imposition of penalty due to delay in supply of goods, which may need to be considered under the guidance of Ind AS 115, Revenue from Contracts with Customers.

If the management is unable to assess whether some of the executory contracts are onerous due to inadequacy of information, the same should be disclosed. Management should disclose that it has assessed whether executory contracts are onerous due to the adverse impact of COVID -19. If, the management is unable to assess whether some of the executory contracts have become onerous due to inadequacy of information, the same should be disclosed.

2. Penalties

Under Indian Accounting Standards, if a company has a present obligation, which cannot be avoided and is expected to result in the outflow of economic resources, then it recognises a provision if the amount can be estimated reliably.

Companies need to review their existing contracts and consider the interpretation of applicable law, particularly force majeure clauses, to determine whether they have an obligation triggered by Covid-19. In some cases, this may require them to recognise additional provisions – e.g. for failure to comply with applicable laws and regulations. Conversely, in some countries the outbreak may be regarded as force majeure and penalties for non-performance, late delivery or cancellation may be waived. This assessment may require legal advisors to be involved.

3. Restructuring costs

The Standard provides that a provision for restructuring costs is recognised only when the general recognition criteria for provisions are met and when there is a detailed formal plan for the restructuring and there is evidence that the entity has started to implement a restructuring plan, for example, by dismantling plant or selling assets or by the public announcement of the main features of the plan.

4. Contingent Assets - Insurance claims

Entities may have insurance policies that cover loss of profits due to business disruptions due to events like COVID-19. Entities claims on insurance companies can be recognised in accordance with Ind AS 37 only if the recovery is virtually certain i.e. the insurance entities have accepted the claims and the insurance entity will meet its obligations.

Entities to Whom AS is Applicable

AS 29 Provisions, Contingent Liabilities and Contingent Assets

Onerous contracts are those contracts for which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. Unavoidable costs under a contract are 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. As a result of COVID -19, some contracts may become onerous for reasons such as the imposition of penalty due to delay in supply of goods or increase in cost of material, labour, etc. Management should consider whether any of its contracts have become onerous. The same should be accounted for as per AS 29. Management should disclose that it has assessed whether executory contracts are onerous due to adverse impact of COVID -19. If, the management is unable to assess whether some of the executory contracts have become onerous due to the inadequacy of information, the same should be disclosed.

Impact of COVID-19 – Going Concern Assessment(AS-1, AS-4)

The Financial statements are normally prepared on the assumption that an entity is a going concern and will continue in operation for the foreseeable future. In assessing whether the going concern assumption is appropriate, management considers all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period.

Entities to Whom Ind AS is Applicable

Going concern considerations, including financing challenges

Under Indian Accounting Standards, management is required to assess a company's ability to continue as a going concern. A company is no longer a going concern if management either intends to liquidate the entity or cease trading, or has no realistic alternative but to do so.

Companies are required to disclose material uncertainties related to events or conditions that may cast significant doubt on their ability to continue as a going concern. In addition, disclosure is required when management concludes that there are no material uncertainties but reaching that conclusion involved significant judgement (a 'close call').

When management assesses the company's ability to continue as a going concern, it will need to consider the current economic uncertainty and market volatility caused by the Covid-19 outbreak, which has been further exacerbated by a decline in oil prices.

In assessing whether the going concern assumption is appropriate, management assesses all available information about the future (which is at least, but not limited to, 12 months from the reporting date), considering the possible outcomes of events and changes in conditions, and the realistically possible responses to such events and conditions that are available.

Revising budgets and forecasts

In many cases, 2020 budgets and forecasts prepared in 2019 may now be of limited relevance given the rapidly changing economic and business circumstances. These may require significant revision – e.g. for forecast sales, gross margins and changes in working capital – to be able to support management's assessment in the current environment.

It is important that management's assessment considers different scenarios, including a reasonably plausible downside scenario. After updating the forecasts, management will need to assess whether it expects to remain in compliance with financial covenants.

It will be critical for management to assess what impacts the current events and conditions have on a company's operations and forecast cash flows, with the key issue being whether a company will have sufficient liquidity to continue to meet its obligations as they fall due.

For example, a company may need to consider whether:

- it has sufficient cash and unused credit lines/borrowing facilities to meet short-term needs;
- further actions are needed by management to enable the company to generate sufficient cash flows to meet its obligations when they fall due;
- it needs to negotiate with lenders to restructure and/or increase borrowing facilities;
- to restructure operations to reduce operating costs;
- to defer capital expenditure; or
- to seek financial support from shareholders and/or government programme designed to support businesses.

Financing challenges

Management should reassess the availability of finance because it may not be easily replaced and the costs may be higher in the current circumstances.

- Borrowers with weaker credit ratings may find it more difficult to access bond markets, and may find banks and other lenders less willing to renew or increase borrowing facilities.
- Lenders may demand new terms, such as significantly higher yields or improved collateral, particularly for companies in highly exposed sectors.
- Lenders themselves may be experiencing liquidity issues and may need central bank assistance to be able to continue to provide, or increase, financing.
- Borrowers with foreign currency-denominated debt may find that debt servicing costs increase significantly due to the depreciation of their local currency.
- Covenants in loan agreements may provide lenders with an opportunity to withdraw financing.

If management concludes that the consequences of the outbreak will result in deterioration in operating results and financial position after the reporting date that is so severe that the going concern assumption is no longer appropriate, then the financial statements would need to be adjusted – i.e. a change in the going concern assumption is considered an adjusting event.

Disclosures

To the extent that events and conditions are identified that may cast significant doubt on a company's ability to continue as a going concern, disclosure of uncertainties is required if these events constitute material uncertainties or management's conclusion that there are no material uncertainties involved significant judgement.

Supply chain, logistics and other disruptions or significant changes in demand can have implications for a company's working capital. Many companies would need to adjust the way they manage liquidity to respond to the current market turmoil, including the use of alternative sources of funding. Additional disclosures will be needed, explaining those changes and how the company manages its liquidity in these difficult economic conditions.

Entities to Whom AS is Applicable

AS 1 Disclosure of Accounting Policies

AS 4 Contingencies and Events Occurring After the Balance Sheet Date (revised 2016)

The Financial statements are normally prepared on the assumption that an entity is a going concern and will continue in operation for the foreseeable future. Management of the entity should assess the impact of COVID-19 and the measures taken on its ability to continue as a going concern. The impact of COVID- 19 after the balance sheet date should also be considered in assessing whether going concern assumption is appropriate or not. Events occurring after the balance sheet date may indicate that the enterprise ceases be a going concern. It may be necessary for the management to evaluate whether it is proper to use the fundamental accounting assumption of going concern in the preparation of the financial statements.

Actions for Management to Take Now

When assessing a company's ability to continue as a going concern, management may need to do the following.

- Update forecasts and sensitivities, as considered appropriate, taking into account the risk factors identified and the different possible outcomes. It is important to consider downside scenarios – e.g. taking into account the impacts of a 'lockdown', when relevant.
- Review projected covenant compliance in different scenarios.
- Assess its plans to mitigate events or conditions that may cast significant doubt on the company's ability to continue as a going concern. In particular, management would be expected to reassess the availability of finance. The company needs to assess whether its plans are achievable and realistic.

Auditor's Role:

SA 570 – Going concern:

COVID-19 is resulting in significant operational disruption and presents an existential threat for many businesses. Entities and audit teams need to consider the implications on the assessment of going concern and viability in the financial report and whether these circumstances will result in prolonged operational disruption which will significantly erode the financial position of the entity or otherwise result in failure.

This is critically important for the going concern assessment. Auditors will need to consider whether the threat to liquidity as a result of supply/demand disruption presents a material uncertainty to the going concern status for the 12 months look forward period.

SA 570(Revised) also requires auditors to consider events that may cast significant doubt on the entity's ability to continue as a going concern beyond the period of management's assessment.

Audit teams should robustly assess the going concern and viability risks relating to COVID-19 threat in compliance with SA 570(Revised). This includes evaluating whether there is adequate support for the assumptions underlying management's assessment and the consistency of these assumptions across the entity's business activities.

Impact of COVID-19 on Financial Instruments (IND AS 109)

Measurement of ECLs

Where an entity has any financial instruments that are in the scope of Ind AS 109 Expected Credit Loss model (ECL) management should consider the impact of COVID-19 on the ECL. Instruments to be considered include loans, trade and other receivables, debt instruments not measured at fair value through profit or loss, contract assets, lease receivables, financial guarantees and loan commitments

Management should consider the impact of COVID-19 on both:

- whether the ECL is measured at a 12-month or lifetime ECL. If the credit risk (risk of default) has increased significantly, since initial recognition the ECL is measured at the lifetime ECL rather than the 12-month ECL (except for assets subject to the simplified approach, such as short-term receivables and contract assets, which are always measured using lifetime ECL); and
- the estimate of ECL itself. This will include all of
    - the credit risk (risk of default). For example, this may increase if the debtor's business is adversely impacted by COVID-19;
    - the amount at risk if the debtor defaults (exposure at default). For example, debtors affected by COVID-19 may draw down on existing unused borrowing facilities, or cease making discretionary over payments, or take longer than normal to pay resulting in a greater amount at risk; and
    - the estimated loss as a result of default (loss given default). For example, this may increase if COVID-19 results in a decrease in the fair value of a non-financial asset pledged as collateral.

Even when a borrower is expected to repay all amounts owed but later than contractually required, there will be a credit loss if the lender is not compensated for the lost time value of money.

Ind AS 109 requires that forward-looking information (including macro-economic information) is considered both when assessing whether there has been a significant increase in credit risk and when measuring expected credit losses. Forward-looking information might include additional downside scenarios related to the spread of COVID-19. This might be achieved by adding one or more additional scenarios to the entity's existing scenarios, amending one or more of the existing scenarios (for example, to reflect a more severe downside(s) and/or to increase their weighting), or using an 'overlay' if the impact is not included in the entity's main expected credit loss model.

Certain governments might ask local banks to support borrowers affected by COVID-19. This could be in the form of payment holidays on existing loans or reduced fees and interest rates on new loans. Entities giving such support should consider the impact on their financial statements including whether:

- payment holidays indicate the affected loans have suffered a significant increase in credit risk or default, and therefore moved to stage 2 or 3 of the ECL model; and
- reduced fees or interest rates on new loans indicate that the loans are not made at a market rate.

Management should consider the need to disclose the impact of the virus on the impairment of financial assets. For example, disclosures required by Ind AS 107 Financial instruments: Disclosures that might be affected include how the impact of forward looking information has been incorporated into the ECL estimate, details of significant changes in assumptions made in the reporting period, and changes in the ECL that result from assets moving from stage 1 to stage 2.

Other Financial Instrument Measurement Issues

In addition to considering the impact of the virus on its expected credit losses and the measurement of financial instruments at fair value, management should also consider:

- the impact of the changes to the terms of any borrowing or loan agreement, perhaps because of actions taken by the local government or the renegotiation of terms between a borrower and a lender. Both parties should apply the guidance in Ind 109 to determine the impact of the change in terms including those for determining whether the change to the terms results in derecognition and, if not, for recognizing a modification gain or loss; and
- whether the entity continues to meet the criteria for hedge accounting. For example, if a hedged forecast transaction is no longer highly probable to occur, hedge accounting is discontinued.

Disclosures

A company is required to disclose the nature and extent of risks arising from financial instruments and how it manages those risks. Therefore, a company will need to explain the significant impacts of Covid-19 on the risks arising from financial instruments and how it is managing those risks. It will need to use judgement to determine the specific disclosures that are relevant to its business and necessary to meet these objectives.

Examples of specific disclosures include the following.

- Information about a company's credit risk management practices and how they relate to the recognition and measurement of ECLs. A company may have changed its risk management practices in response to Covid-19 – e.g. by extending debt relief to borrowers or by following specific guidance issued by governments or regulators.

- The methods, assumptions and information used to measure ECLs – e.g. a company may need to explain how it has incorporated updated forward-looking information into measuring ECLs, in particular:
    - how it has dealt with the challenge of ECL models that were not designed for the current economic shocks; and
    - how it has calculated overlays and adjustments to these models.
- Quantitative and qualitative information that allows evaluation of the amounts arising from ECLs; the types of analysis disclosed previously may need to be adjusted or supplemented to clearly convey impacts arising from Covid-19.
- Information on the assumptions that the company has made about the future and other major sources of estimation uncertainty at the reporting date that have a significant risk of resulting in material adjustment within the next financial year.

Additional disclosures might also be required. For example, Ind AS 107 requires disclosure of defaults and breaches of loans payable, of gains and losses arising from derecognition or modification, and of any reclassification from the cash flow hedge reserve that results from hedged future cash flows no longer being expected to occur.

Entities to Whom AS is Applicable

- In case of financial assets such as Loans, Trade Receivables etc., entities shall be guided by the requirements of AS 4, Contingencies and Events Occurring After the Balance Sheet Date.
- In respect of financial assets within the scope of AS 13, Accounting for Investments, entities may have to carefully consider the requirements of making provisions for decline in the value of

investments, which is other than temporary.

- In respect of Banks and Insurance Entities, preparers need to consider impact of COVID-19 on classification of Loans and Advances into Standard, Sub- standard, Doubtful and Loss categories in addition to the Prudential Regulatory requirements of RBI and The Insurance Regulatory and Development Authority of India (IRDAI).

Impact of COVID-19 on Hedge Accounting (IND AS 109)

Entities to Whom Ind AS is Applicable

When a transaction has been designated as the hedged item in a cash flow hedge relationship the entity will need to consider whether the transaction is still a "highly probable forecasted transaction" and if not, whether it is still expected to occur. Hedged items in a cash flow hedge that could be affected due to COVID-19 include:

- Sale or purchase volumes that fall below the levels originally forecasted;
- Planned debt issuances that are delayed or cancelled such that interest payments fall below levels originally forecasted; and
- Business acquisitions or disposals that are delayed or cancelled.

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 and defer the gain or loss on the hedging instrument that has been recognised in other comprehensive income accumulated in equity until the forecasted transaction occurs. If the forecasted transaction is no longer expected to occur the entity must immediately reclassify to profit or loss any accumulated gain or loss on the hedging instrument.

When the expected timing of a designated hedged transaction changes, an entity is required to reassess whether the hedged transaction identified in the entity's hedge documentation is still the same hedged transaction (i.e. assess whether the hedged transaction is still expected to occur).

A change in the timing of a hedged forecast transaction when its occurrence remains highly probable may also have an effect on profit or loss. Hedge ineffectiveness can exist because a difference arises in the amount and/or timing of the hedged item and the hedging instrument. It is common for entities to determine a 'hypothetical derivative' to reflect the timing and amount of the hedged item and use the fair valuation of this to compare with the hedging instrument to determine the amount of hedge ineffectiveness to be recognised in profit or loss. As the timing and/or amount of the hedged item changes in response to economic conditions, entities should redefine the hypothetical derivative to ensure hedge ineffectiveness is appropriately recognised.

Finally, increases in credit risk may cause a hedge relationship to fail its hedge effectiveness assessment if credit risk dominates the value changes resulting from the economic relationship between the hedging instrument and the hedged item.

Entities to Whom AS is Applicable

ICAI Guidance Note on Accounting for Derivative Contracts (Issued 2015)

In respect of recognition and measurement of derivatives within the scope ICAI Guidance Note on Derivatives, entities may need to consider the impact on key inputs/assumptions such as foreign currency rate, interest rate, etc. used in their valuation techniques, including the potential impact on hedge accounting.

Impact of COVID-19 on Fair Market Value(IND AS 113)

The fair value of an asset or liability at the reporting date should be determined in accordance with the applicable Indian Accounting standards. When fair value is based on an observable market price, the quoted price at the reporting date should be used. The fair value of an asset reflects a hypothetical exit transaction at the reporting date. Changes in market prices after the reporting date are therefore not reflected in asset valuation.

The volatility of prices on various markets has increased as a result of the spread of COVID-19. This affects the fair value measurement either directly - if fair value is determined based on market prices (for example, in case of shares or debt securities traded on an active market), or indirectly - for example, if a valuation technique is based on inputs that are derived from volatile markets. Counterparty credit risk and the credit spread that is used to determine fair value might also increase. However, the impact of actions taken by governments to stimulate the economy might reduce risk free interest rates.

A change in the fair value measurement affects the disclosures required by Ind AS 113 Fair value measurement, which requires entities to disclose the valuation techniques and the inputs used in the fair value measurement as well as the sensitivity of the valuation to changes in assumptions. It might also affect the sensitivity analysis required for recurring fair value measurements categorised within level 3 of the fair value hierarchy. The number of instruments classified as level 3 might increase.

'Unobservable inputs' are inputs for which market data is not available and that are developed using the best information available about the assumptions that market participants would make in pricing the asset or liability, including assumptions about risk. Unobservable inputs used in valuations may require significant adjustment to reflect the risks and uncertain market conditions at the measurement date.

Reflecting risks and market conditions at the measurement date

Some of the key factors and risks to consider when measuring fair value using a valuation technique include the following:

- **Economic activity levels**: Measures taken to contain the virus may lead to a significant reduction in economic activity in terms of production of and demand for goods and services, and may have a negative impact on forecast future cash flows used in a discounted cash flow valuation method.

- **Credit risk and liquidity risk:** The uncertain economic environment has resulted in increases in credit risk and liquidity risk for many companies. Own credit risk and/or counterparty credit risk used as inputs into valuation techniques may therefore increase.

- **Forecasting risk:** Fair value measurements should reflect the greater uncertainty in making economic and financial forecasts in the near term, due to the difficulty in forecasting the magnitude and duration of the economic impact of Covid-19.

- **Foreign exchange risk:** Companies with significant sales or purchases in foreign currencies may be adversely affected by exchange rate movements.

- **Commodity price risk:** Companies in extractive industries may be significantly affected by decreases in commodity prices. Companies in countries that are economically dependent on these commodities may also have greater risk of adverse economic impacts.

Significant judgment may be needed to quantify risk premiums and other adjustments for these risks. Also, the number of fair value measurements classified as Level 3 in the fair value hierarchy may increase (e.g. due to unobservable inputs such as the credit risk becoming significant in the current environment).

Disclosure

Given the impact of the increase in economic uncertainty on forecasting cash flows and other unobservable inputs used in valuation techniques (e.g. certain risk-adjusted discount rates), companies may need to provide sensitivity disclosures – together with disclosure of the key assumptions and judgements made by management – to enable users to understand how fair value has been determined. These disclosures are required under both Ind AS 113 Fair Value Measurement and Ind AS 1 Presentation of Financial Statements. Ind AS 113 also contains specific disclosure requirements when amounts are transferred into Level 3 of the fair value hierarchy, including sensitivity disclosures.

Actions for Management to Take Now

- Consider whether the valuation:
  - reflects market participants' assumptions based on information available and market conditions at the measurement date; and
  - incorporates the risk premiums that would arise from the increased uncertainty and other impacts of Covid-19.

- Consider whether unobservable inputs have become significant, which would result in a Level 3 categorisation and require additional disclosures.
- Consider expanding disclosures about the key assumptions, sensitivities and major sources of estimation uncertainty.

Entities to Whom AS is Applicable

AS 13 Accounting for Investments

- In respect of financial assets within the scope of AS 13, entities have to carefully consider the impact of COVID-19 on determination of fair value for valuation of investments classified as Current Investments.

Impact of COVID -19 on Revenue Recognition (IND AS 115)

Entities to Whom Ind AS is Applicable

Contract Existence

Under Ind AS 115 Revenue from Contracts with Customers, companies account for a contract with a customer only when the agreement creates enforceable rights and obligations under the law. That is, a company recognises revenue if, and only if, the contract passes the contract existence test in Step 1 of the five-step model for revenue recognition .

When entering into new contracts, companies need to consider carefully whether these Step 1 criteria are met. For example:

- Are both parties committed to performing their respective obligations?
- Is it probable that consideration will be collected?
- Does the contract allow each party to terminate a wholly unperformed contract without compensating the other party?

If a new contract with a customer does not meet all of the contract existence criteria, then a company does not recognise revenue. In addition, companies may need to reassess whether the contract existence criteria continue to be met for existing contracts – i.e. if there is a significant change in facts and circumstances. If an existing contract with a customer no longer meets these criteria, then a company stops recognising revenue for that contract.

Contract modifications

Companies and their customers may seek to modify existing contracts to respond to the impacts of COVID-19 on their business. Under Ind AS 115, a contract modification is a change in the scope or price of a contract, or both. This may be described as a change order, a variation or an amendment.

Companies account for contract modifications when they are approved and when they create or change the enforceable rights and obligations of the parties to the contract. Companies may need to exercise judgement to assess when contract modifications are approved, particularly when contracts are modified frequently or there is continuing uncertainty about how a contract will be completed.

Accounting for contract modifications can be complex. There are different approaches for different circumstances, depending on factors such as how the modification is priced and whether the current contract is being accounted for over time. Companies need to apply the specific requirements in Ind AS 115.

Identifying Variable Consideration

Under Ind AS 115, if a contract includes variable consideration, then a company estimates the amount of consideration to which it will be entitled. Variable consideration includes discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties and other similar items. It may be explicit or implicit – e.g. based on the company's customary business practices or specific statements. Companies need to consider carefully whether actions taken to respond to the COVID-19 outbreak result in additional variable consideration – e.g. incentives or concessions offered to customers. Additionally, if a company's supply chain or labour force is disrupted such that it cannot satisfy its obligations, then this could result in penalties that reduce the transaction price.

Estimating variable consideration

A company estimates variable consideration but includes it in the transaction price only to the extent that it is highly probable that a significant reversal of revenue will not occur (‘the constraint’).

A company’s estimate of the constrained amount may be impacted significantly by COVID-19. For example, falling demand may impact whether customers will qualify for rebates or volume discounts. Further, transport companies may need to update estimated revenue for an increase in refunds to customers for cancelled or delayed journeys. Companies need to reassess the estimated transaction price at each reporting date.

Stand-alone selling prices

Under Ind AS 115, a company allocates the transaction price to each performance obligation identified on a relative stand-alone selling price basis. The stand-alone selling price is the price at which a company would sell a promised good or service separately to a customer. When the stand-alone selling price is not directly observable, a company estimates it considering all reasonably available information and maximising the use of observable inputs. COVID-19 may impact these estimates significantly, either because observable selling prices change or because inputs to estimate techniques change. This may in turn affect the amount of revenue recognised as each good or service in the contract is transferred. Companies need to ensure they use up-to-date estimates to allocate the transaction price for new contracts. However, after contract inception the transaction price is not reallocated to reflect subsequent changes in stand-alone selling prices. [IFRS 15.88]

Revenue recognition over time

When a company transfers control of a good or service over time, revenue is recognised by measuring the progress towards complete satisfaction of that performance obligation. This is common in sectors such as real estate, construction, engineering, aerospace and defence.

A company applies a single method of measuring progress to depict its performance in transferring control of goods or services, using an output or an input method.

When a company uses an input method to measure progress – e.g. costs incurred as a percentage of expected total costs – it needs to estimate the total expected inputs that will be needed to satisfy the performance obligation. COVID-19 may impact project timelines if work cannot be completed to schedule. It may also push up the costs of key inputs.

Companies need to ensure that the estimated progress and revenue recognised reflect the latest expectations. Any changes in this estimate are accounted for prospectively.

Disclosures

In annual financial statements, companies are required to disclose information about the methods, inputs and assumptions used for estimating variable consideration (including the constraint) and estimating stand-alone selling prices. Companies may need to expand or update these disclosures for the impact of COVID-19.

In interim financial statements, companies need to include information about disaggregated revenue. However, companies should consider whether to provide other disclosures for revenue to meet the requirements in Ind AS 34 Interim Financial Reporting – e.g. if there is a change in a company's accounting policies for revenue.

Entities to whom AS is applicable,

Entities may have postponed recognition of revenue duetosignificantuncertaintyofcollectioninviewoftheimpactofCOVID-19.AS 9, Revenue Recognition requires entities to disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.

Impact of COVID-19 on Leases (IND AS 116)

Due to COVID-19, there may be changes in the terms of lease arrangements or lessor may give some concession to the lessee with respect to lease payments, rent free holidays etc. Such revised terms or concessions shall be considered while accounting for leases, which may lead to the application of accounting relating to the modification of leases. However, anticipated revisions should not be taken into account.

Variable lease payments may be significantly impacted, especially those linked to revenues from the use of underlying asses due to contracted business activity. Discount rate used to determine the present value of new lease liabilities may need to incorporate any risk associated with COVID-19.

If any compensation is given/declared by the Government to the lessor for providing concession to the lessee, it should be considered whether the same needs to be accounted for as lease modification as per Ind AS 116 or whether assistance received from Government is to be accounted as government grants under IndAS-20.

Reassessment of Options

Ind AS 116 Leases requires a lessee to determine whether it is reasonably certain:

- to exercise an option to extend the term of the lease;
- to exercise an option to purchase the underlying asset at the end of the lease; or
- not to exercise an option to terminate the lease early.

In doing so, lessees consider all relevant facts and circumstances that create an economic incentive for them to exercise an option or not.

A lessee applies judgement when identifying significant events or significant changes in circumstances that trigger reassessment of these options. The lessee then considers the effect of current economic incentives to determine whether it is reasonably certain to exercise, or not to exercise, each option. For example, a retailer concludes that revised commercial plans developed in response to the COVID-19 outbreak trigger a reassessment of renewal options in its store leases. In assessing whether it is reasonably certain to exercise the renewal options, the retailer considers the economic incentives existing at the date of the reassessment.

Accounting for reassessments

If a lessee changes its assessment of whether it is reasonably certain to exercise a renewal or purchase option, or not to exercise an option to terminate the lease early, then it remeasures its lease liability using a revised discount rate. The lessee adjusts the carrying amount of the right-of-use asset for the remeasurement of the lease liability. If the carrying amount of the right-of-use asset is reduced to zero, then any further reductions are recognised in profit or loss.

As a result, reassessment can have a significant impact on the carrying amount of lease assets and liabilities at the date of the reassessment. In turn, this may affect the amount and profile of depreciation and interest expense recognised subsequently.

For example, suppose a company that leases a vehicle initially assessed that it was reasonably certain to exercise an option to purchase the vehicle at the end of the lease term. As a result, it included the exercise price of the purchase option in the initial carrying amount of its right-of-use asset and lease liability, and depreciated the right-of-use asset over the useful life of the vehicle. Subsequently, the company concludes that it is not reasonably certain to exercise the purchase option. It therefore remeasures the right-of-use asset and lease liability, and depreciates the right-of-use asset over the lease term.

Actions for management to take now

- Consider whether COVID-19-related events and circumstances have triggered a requirement to reassess renewal, termination or purchase options.
- Consider the impact of any changes in economic incentives on whether a company is reasonably certain to exercise, or not to exercise, such options.
- Provide clear and meaningful disclosures about judgements and estimates made in reassessing lease options and lease terms.

Entities to whom AS is applicable Leases (AS 19, AS 29)

- Due to COVID-19 there can be changes in the terms of lease arrangements or lessor maygive some concession to the lessee with regard to lease payments. Such revised terms or concessions shall be considered while accounting for leases. However, anticipated revision should not be taken into account.
- Discount rate used to determine present value of minimum lease payments of new leases may need to incorporate any risk associated with COVID-19.
- If any compensation is given/declared by the Government to the lessor for providing concession to the lessee, it should be considered whether the same needs to be accounted for appropriately as per AS 19. Whether any assistance received from government are government grants under AS 12.
- Entities will need to determine whether as a result of COVID -19, any lease arrangement has become onerous. The same should be accounted for as per AS 29.

Impact of COVID-19 on Income Tax (IND AS 12)

Entities should consider how profitability, liquidity, and impairment concerns that could result from the impacts of COVID-19 might also affect their income tax accounting under Ind AS 12. For example, a reduction in current-period income or the actual incurrence of losses, coupled with a reduction in forecasted income or a forecast of future losses, could result in a reassessment of whether it is probable that some or all of an entity's deferred tax assets can be recovered.

Such assessments will be particularly challenging in situations in which the changes in current and projected future profitability actually result in, or are expected to result in, cumulative losses and the entity has not had a stable earnings history before the impacts of COVID-19. If declining earnings or impairments generate losses, entities also need to evaluate whether there is sufficient income of the appropriate character to fully realise the related deferred tax asset.

The rate and tax base used to calculate the deferred tax balances should reflect the manner in which the entity expects, at the end of the reporting period, to recover the asset or settle the liability. Accordingly, entities will need to consider whether strategies considered to address the challenges brought by the COVID-19 pandemic have an effect on the recognition and measurement of deferred tax amounts. This may be the case for example, if an entity plans to sell an asset to improve liquidity and the tax consequences of selling an asset are different from those resulting from using the asset in operations (the original intent of the entity).

Deferred tax consequences of adjustments to the carrying amounts of assets and liabilities (for example, as a result of impairment losses or decreases in the value of a pension surplus) will also need to be considered.

As permitted by Ind AS 12, an entity may have not recognised deferred tax liabilities for taxable temporary differences associated with subsidiaries, branches and associates, and interests in joint arrangements, because it controls the timing of the reversal of the temporary difference and it has been probable until now that the temporary difference will not reverse in the foreseeable future.

Conversely, it may have recognised deferred tax assets for deductible temporary differences associated with such investments because it was probable that the temporary difference would reverse in the future (and it was probable that the deferred tax asset could be recovered). It may be appropriate to reconsider these conclusions if there is a change in intent with respect to repatriation of undistributed earnings in an investee to help with liquidity issues.

Other uncertain tax positions may also arise as a result of the consequences on the entity of the COVID-19. This may be the case for tax positions related to transfer pricing arrangements, where previously prepared benchmarking studies to support the policy may no longer be valid. Some jurisdictions establish whether an entity is subject to taxation in a jurisdiction based on residency, often determined by a “central management and control” test, which is determined based on factors such as physical attendance at board meetings. Travel restrictions may require entities to consider whether they have met all of the requirements to be subject (or not subject) to taxation in a jurisdiction.

Entities to whom AS is applicable

AS 22, Accounting for Taxes on Income

COVID-19 could affect future profits and/or may also reduce the amount of deferred tax liabilities and/or create additional timing differences due to various factors. Entities with deferred tax assets should reassess forecast profits and the recoverability of deferred tax assets in accordance with AS 22, Accounting for Taxes on Income, considering the additional uncertainty arising from the COVID- 19 and the steps being taken by the management to control it.

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