

Financial Reporting Hot Topics: Coronavirus

Three questions for 2019 year-end

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The novel coronavirus outbreak has caused extensive disruptions to businesses operating in or having close trading associations with companies in China and beyond.

In this inaugural issue of the *Financial Reporting Hot Topics* newsletter, we discuss general financial reporting considerations as a result of the outbreak, with a specific focus on Hong Kong-listed issuers.

The fluid situation can make it difficult to assess the likely impact. That said, companies strive to be highly attuned and maintain a heightened state of readiness for the increased uncertainties. As your organisation evaluates the current and potential effects on your business and financial reporting, we highlight three questions that your C-level executive team and board of directors might consider.

1) Does the impact warrant a separate announcement about inside information?

In their [Joint Statement in relation to Results Announcements in light of Travel Restrictions related to the Severe Respiratory Disease associated with a Novel Infectious Agent](#) (“the Joint Statement”) issued on 4 February 2020, the Securities and Futures Commission (“SFC”) and the Stock Exchange of Hong Kong Limited (“the Exchange”) notes that issuers should consider disclosing inside information if the outbreak has caused material disruptions to their business operations, reporting controls, systems, processes or procedures.

To ensure timely disclosure in accordance with the relevant rules and regulations, it is advisable to review your organisation’s systems and processes in this regard and to be on the lookout for potentially disclosable issues, so that they are promptly identified, assessed and escalated for the attention of the board of directors. A close working relationship with your legal adviser would also facilitate resolving such issues in a timely manner.

2) Have you thought through how the impact is to be reflected in your organisation’s annual report?

The impact of the outbreak on your organisation may be reflected in both the front-end and back-end of your annual reports.

Financial statements

With respect to 31 December 2019 financial statements, the financial reporting impact arising from the outbreak will likely be limited to non-adjusting subsequent events under International or Hong Kong Financial Reporting Standards given that the changes in business activities and economic conditions occurred after the reporting period.

On the one hand, this may result in additional challenges in distinguishing pre-31 December and post-31 December impact. For example, impairment estimates for financial and non-financial assets at 31 December 2019 should reflect reasonable and supportable information available as at that date, and care should be taken to avoid the application of hindsight or the incorporation of valuation inputs that are not consistent with the conditions or reasonable expectations at that date. The assessment may be less clear-cut in some cases. For example, a customer’s bankruptcy after the reporting date is often the culmination of a sequence of events that started before that date (e.g. US-China trade tensions or social unrest in Hong Kong), which may make the receipt of information about the bankruptcy an adjusting event and result in recognition of additional losses in the 31 December 2019 financial statements.

On the other hand, material non-adjusting events require disclosures – including an estimate of the financial effect if that can be determined – in the financial statements. For example:

- Changes in economic circumstances that may impact impairment evaluations and fair-value measurements of financial and non-financial assets and liabilities
- Changes in credit risk of customers
- Covenant breaches, amendments, or waivers in lending agreements
- Potential inventory write-downs
- Strategies and policies to manage risk.

Additionally, more extensive disclosures about your organisation's policies and processes for managing its credit or liquidity risk exposures may become necessary.

Business review in management discussion and analysis

As a business review is required to include a description of the principal risks and uncertainties facing your organisation and the particulars of important events affecting your organisation that have occurred since the end of the financial year, it serves a key role in complementing and supplementing the financial statements. It also bridges the gap between the discussion of what happened during the financial year under review and the discussion of the likely future developments of the business.

With all the increased uncertainties prompted by the outbreak, it is important that your organisation put due effort in bringing a sufficiently specific and up-to-date story to your investors, in line with Schedule 5 of the Hong Kong Companies Ordinance and the guidance in [Accounting Bulletin 5](#) issued by the Hong Kong Institute of Certified Public Accountants.

In this regard, your usual KPMG contact can provide you with copies of the following KPMG publications:

- [A Practical Guide to the Business Review](#) – this discusses how a business review can both embrace the HKICPA's Accounting Bulletin 5 guidance and meet the Listing Rule requirements and recommendations relating to the management discussion and analysis. This publication is available from our external website.
- HK Companies Ordinance Checklist on the Business Review for Listed Companies – this helps companies ensure that the minimum requirements of Schedule 5 and the Listing Rules are met, and to help when assessing the extent to which the business review has taken the guidance in AB5 into account.

3) Is your organisation on top of challenges in meeting the reporting timetable?

Delays in year-end closing processes and additional work and audit procedures necessitated by the severity of the impact of the outbreak (for example, additional impairment and going-concern assessments) may create additional challenges in meeting the reporting timetable of your organisation and those imposed by the Listing Rules.

Maintaining continued dialogue with your auditors, agreeing on a realistic timetable, monitoring the integrity and progress of the financial reporting and audit processes, communicating issues with the board early: in short, better communication and coordination can be more important than ever to meet the reporting timetable.

The audit committee plays an instrumental role in meeting these challenges.

Notwithstanding the above, circumstances may be such that your organisation might not be able to obtain an agreement from their auditors following the guidance of [Practice Note 730](#) at the time of making a preliminary results announcement. This would be the case if the audit is not complete or if it is not at an advanced stage that any matters outstanding with respect to the audit may result in changes to the results.

In such cases, the Joint Statement issued by the SFC and the Exchange on 4 February 2020 provides guidance on dealing with delays in announcing audited results with reference to the Listing Rules under the following scenarios:

Scenario 1 Issuer can publish a results announcement in full compliance with the Listing Rules other than only obtaining agreement from its auditors	Scenario 2 All other cases
<ul style="list-style-type: none"> • Publish preliminary results on or before the deadline • The Exchange will normally allow trading in the securities of the issuer to continue 	<ul style="list-style-type: none"> • Consult with the Exchange on the financial information that it is able to report on • The Exchange, in consultation with the SFC, will assess whether publication of such information will be sufficient to maintain an orderly, informed and fair market so that trading in the securities of the listed issuer can continue. The Exchange and the SFC will consider the views of the issuer's audit committee on the unaudited financial information available to the issuer.

Under either scenario, issuers shall follow the requirements of Main Board Rules 13.49(3) and (4) in making the preliminary results announcement. Issuers are required, among others, to explain how the outbreak has impacted their financial reporting and/or audit process and state the expected date when the audited results will be available.

As such, it is advisable that your organisation be on top of the impact of the outbreak on your financial reporting and/or audit processes, and contact the Exchange as soon as you foresee there would be difficulties in meeting the deadline for publishing a preliminary results announcement in accordance with the Listing Rules, to avoid a trading suspension. The whole board of directors is responsible for an issuer's financial reporting and ensuring compliance with the Listing Rules. The audit committee's view is particularly important to the Exchange and SFC for assessing the quality of information that can be published should your organisation fall into scenario 2 above.

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If you have any questions about the matters discussed in this publication, please feel free to contact the following partners or your KPMG contacts.



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