

Analysis of COVID-19 effects must be included in 2020 financial statements

I. Accounting Standards Committee issues new recommendations

At the end of December 2020 the Accounting Standards Committee prepared and published its recommendations entitled "Financial statements in the time of the COVID-19 pandemic". As stated in an announcement on the webpage of the Ministry of Finance, the document is directed to those responsible for the preparation of financial statements, i.e. entity managers, those who have been entrusted with the preparation of financial statements (entity accountants, owners and employees of accounting offices), employees of financial and accounting services, as well as stakeholders expecting true and fair information about the financial positions and financial results of entities.

II. Recommendations to make preparation of 2020 financial statements easier

As indicated in the publication, its purpose is to support those responsible for accounting as they make decisions to include the effects of COVID-19 in the books of account and financial statements for the year 2020, as well as in reports on activities, if such are prepared. Entities not required to prepare reports on activities should, in the Committee's opinion, consider applying the recommendations, if they determine that information about the effects of COVID-19 on their operations is desirable. In such situations, they should include it in the notes and explanations to the financial statements.

III. Guidelines relate to aspects of financial statements affected by the pandemic

The recommendations include guidelines on matters such as: validity of preparing financial statements on a going concern basis (in conditions of unknown risks and material uncertainty about the future) while allowing for subsequent events; physical count in the time of a pandemic; recognition, presentation and disclosure of aid received as part of the so-called Crisis Shield; additional operating costs caused by COVID-19; responsible application of prudent valuation of assets and liabilities, changes in estimates and in the valuation of assets, including in the valuation of finished products due to production capacity unused as a result of COVID-19.

The Accounting Standards Committee has published its recommendations on the inclusion of the effects of COVID-19 in 2020 financial statements and books of account. Particularly important due to the pandemic is an appropriate assessment of the assumption of going concern.



IV. Management and supervisory board responsible for assessment of going concern

The Committee has reiterated that the entity's management is responsible for assessing its ability to continue as a going concern, disclosing, as applicable, any matters related to going concern and using the going concern basis of accounting, except in situations where the management intends to either liquidate the entity or discontinue its operations, or has no realistic alternative but to do so. The supervisory board, and for public interest entities also the audit committee, is responsible for overseeing the financial reporting process, including for the proper adoption by the entity's management of the assumption of going concern, identification of material uncertainties and presentation of the related relevant disclosures.

V. Analysis of financial and operational risks and threats necessary

When assessing the validity of the assumption of going concern, the entity's management should analyze risks and threats of a financial, operational or another nature, which could have a negative effect on the entity's ability to continue as a going concern. In a pandemic, such an analysis requires the consideration of special pandemic-related circumstances, as well as of any financing and relief received as part of government and non-government aid and support, potential sources of replacement financing, the situation of suppliers and buyers and its effect on the anticipated profitability or continuation of supplies and services, restrictions on movement and travel, loss of income, supply chain disruptions, absence of essential workers and other constraints. It is also necessary to consider whether the entity will be able to maintain liquidity sufficient to enable it to meet its financial obligations as they become due. The management should also consider any negative, but still realistic scenarios of further pandemic spread and its effect on the entity.

VI. Management must assess its own plans to counteract threats, and forecasts

While assessing the entity's ability to continue as a going concern, the management updates its forecasts by considering any identified risk factors and the various possible future scenarios (it is imperative to also consider negative scenarios), and evaluates the entity's ability to perform contracts under the various scenarios. The entity's management should also assess its plans to counteract events and conditions that could negatively affect the entity's ability to continue as a going concern, including in particular any issues with access to sources of financing, as well as the achievability and feasibility of such plans. It is recommended to document assessments of the entity's ability to continue as a going concern and their results.

VII. Introduction to financial statements must contain description of actions

Introduction to the financial statements should contain a description of the indications and any undertaken or potential actions based on which the management found that the assumption of going concern is valid, irrespective of whether it is in the end determined that material uncertainty with regard to going concern exists or not. In the introduction to the financial statements the management indicates whether the financial statements have been prepared on a going concern basis, and – if there are circumstances pointing to material uncertainty with regard to going concern, and such may include pandemic-related conditions – indicates those threats.



VIII. COVID-19 related matters need to be disclosed in notes

While preparing its financial statements (in accordance with Appendix No. 1 to the Accounting Act), in the notes to the financial statements the entity provides a detailed explanation of any circumstances that point to significant threats to its going concern, and states whether the financial statements contain any related adjustments. The notes should also contain a description of any actions planned or undertaken to prevent negative effects. Explanations should contain a description of the main events or conditions that could raise serious concerns as to the entity's ability to continue as a going concern, and the management's plans with respect to such events or conditions, as well as clearly state that there is material uncertainty with regard to events or conditions that could raise serious concerns as to the entity's ability to continue as a going concern and that therefore the entity may not be able to achieve the planned economic benefits from its assets or meet its obligations in the ordinary course of business.



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IX. Recommendations on more than just going concern

Our alert presents the most important recommendations of the Accounting Standards Committee on assessing going concern. As, however, we have mentioned, the recommendations cover many other matters. We will revisit those in the future editions of our alert. At this time we would like to point out that the recommendations contain important guidelines on physical counts in the context of the problems this process may encounter due to the COVID-19 pandemic. The Committee points out that for assets that are subject to being inventoried by way of a physical count, physical completion of the count procedures should be performed no later than by 15 January. Whereas accounting for the inventory count may take longer, as long as the results of the count and any differences therefrom are reflected in the financial statements for the financial year. If the performance of a physical count is not possible for valid reasons, the law permits a count by comparing the data in the books of account with the corresponding documents and verifying the values of those items.

If you would like more details on the Committee's guidelines, please refer to the recommendations or contact our experts.

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