Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting
(ISAR)

38th SESSION
9 – 12 November 2021

Wednesday, 10 November 2021

Agenda item 3. Review of practical implementation, including measurement, of core indicators for entity reporting on the contribution towards the attainment of the Sustainable Development Goals

Presented by

Donna Street, Director, Research and Educational Activities, International Association for Accounting Education and Research; Professor, Al and Marcie Mahrt Chair in Accounting, University of Dayton, United States of America

Effects of COVID-19 on Financial Reporting, Nonfinancial Reporting and Assurance

UNCTAD ISAR IAAER Workshop

Geneva, Switzerland, November 8, 2021

IAAER

INTERNATIONAL ASSOCIATION FOR ACCOUNTING EDUCATION & RESEARCH

Panel Members

Effects of COVID-19 on Financial Reporting, Nonfinancial Reporting and Assurance – Forthcoming Chapter UNCTAD ISAR 2021 Annual Review

- Dr. Katherine Schipper
  Duke University and IAAER Past President
- Dr. Donna L. Street
  University of Dayton and IAAER Director of Research and Educational Activities

Svitlana Vorobei, Deputy Minister of Finance, Tetiana Iefymenko and Liudmyla Lovinska, Academy of Financial management, Ukraine

Cagnur Balsari, Dean, Dokuz Eylül Üniversitesi, Faculty of Business, Izmir,

Joanna Krasodomska, Associate Professor, Financial Accounting Department, Cracow University of Economics, Poland

Sebastian Hoffmann**,** IAAER Vice President, Membership, Professor HHL, Leipzig, Germany

Holger Erchinger, Partner KPMG LLP New York, Member of the IAAER Advisory Board

Schipper and Street

Effects of COVID-19 on all forms of commerce around the world placed substantial pressure on financial reporting, nonfinancial reporting and assurance

- *Objective of Schipper and Street*:
  - Summarize **early findings** of effects using several information sources
    - Securities regulators
    - Standard setters
    - Professional accountancy firms and organizations
    - Practice-oriented research
    - Academic research
- *Important limitation:*
  - Research, especially academic research, is sparse and tends to use small nonrandom samples
  - We expect the breadth and depth of research to increase as more data become available
    - Some examples introduced by panel members

Regulators: IOSCO

- Early awareness of likely difficulties with financial reporting: IOSCO (May 2020)
  - Investors need timely entity-specific information about effects of COVID-19 on operations, financial position, liquidity and future prospects
  - Preparers should use the best available (imperfect) information in an evolving and uncertain environment
  - Disclosures and management commentary should discuss both effects of COVID-19 and measures taken to mitigate those effects
  - Areas of concern
    - Going concern assessments
    - Asset impairments and credit losses
    - Effects of government relief such as debt repayment moratoriums
    - Subsequent events
    - Non-GAAP (alternative) performance measures

Special accommodation: some securities regulators extended 2019 annual and 2020 interim reporting deadlines

Standard setters: IASB

- Targeted IASB actions (examples)
  - IFRS 9: Assessments of **expected credit losses (ECLs)** may require adjustments (overlays) to results from models
  - IFRS 16: Practical expedient to account for rent concessions as if they are not lease modifications
  - IAS 1 and IAS 10: Going concern assessments and events after the reporting period (subsequent events)

The profession: accountancy firms, IFAC, PAOs

- The profession provided non-authoritative guidance and resources to assist financial statement preparers and auditors
- Links to relevant websites are in the discussion paper
- Examples
  - Going concern assessments
  - Asset impairments including goodwill
  - Realizability of deferred tax assets
  - Contract modifications and breaches
  - Subsequent events/events after the reporting period
  - Alternative performance measures
  - Restructurings
  - Leases
  - Compensation and employee benefits (including termination benefits)
  - Government assistance

Non-academic research on effects of COVID-19 on financial reporting

- Features of this research
  - Primarily from large (multinational) accountancy firms
  - Focuses on **descriptive analysis of financial reporting issues and outcomes in reports covering 2019 and the first half of 2020**
- Examples of findings
  - Some (but not all) banks reported declines in credit quality of loans
  - Substantial variation in the degree of detail of COVID-19-related disclosures
    - Liquidity and actions taken to increase liquidity
      - Suspend or reduce dividends
      - Defer or cancel capital expenditures
      - Renegotiate lending agreements
      - Issue equity
    - Supply chain issues

Non-academic research on effects of COVID-19 Banks - KPMG

Bialkowska, E. 2020a. Covid 2019 How is the pandemic affecting bank books? May. Available at: https://home.kpmg/xx/en/home/insights/2020/05/ifrs-blog-covid-banks-disclosures-ifrs9.html.

Bialkowska, E. 2020b. Canadian banks and COVID-19 – impacts on half year results. June. Available at: https://home.kpmg/xx/en/home/insights/2020/06/ifrs-blog-canadian-banks-covid-disclosures-ifrs9.html.

Bialkowska, E. 2020c. European banks and COVID-19 – impacts on half-year results. August. Available at: https://home.kpmg/xx/en/home/insights/2020/08/ifrs-blog-european-banks-h1-covid-disclosures-ifrs9.html.

Bialkowska, E. 2020d. European banks impacts on 2020 Q3 results. November. Available at: https://home.kpmg/xx/en/home/insights/2020/11/ifrs-blog-european-banks-q3-covid-disclosures-ifrs9.html.

Bialkowska, E. 2021. European banks and COVID-19 – What do 2020 annual accounts say? April. Available at: https://home.kpmg/xx/en/home/insights/2021/04/ifrs-blog-european-banks-q4-covid-disclosures-ifrs9.html.

Non-academic research on effects of COVID-19
EY

Dekker, P. 2020. An EY survey of recent financial statements shows a wide range of COVID related disclosures. December. Available at: https://www.ey.com/en_no/ifrs/what-covid-19-disclosures-to-expect-in-2020-financial-statements.

Van der Tas. 2020. Finance teams can learn from the experience of their peers who have already filed 2020 interim or annual accounts. October. Available at: https://www.ey.com/en_gl/ifrs/how-to-prepare-for-year-end-closing-under-covid-19.

Non-academic research on effects of COVID-19 PwC

- PwC. 2020a. How has COVID-19 affected financial reporting? analysis of the impact of COVID-19 on March to May reporters. Available at: https://www.pwc.co.nz/insights-and-publications/2021-publications/how-has-covid-19-affected-financial-reporting.html.

- PwC. 2020b. How has COVID-19 affected financial reporting? analysis of the impact of COVID-19 on June reporters. Available at: https://www.pwc.co.nz/insights-and-publications/2021-publications/how-has-covid-19-affected-financial-reporting.html.

- PwC. 2020c. How has COVID-19 affected financial reporting? analysis of the the impact of COVID-19 on July to December reporters. Available at: https://www.pwc.co.nz/insights-and-publications/2021-publications/how-has-covid-19-affected-financial-reporting.html.

Non-academic research on effects of COVID-19 Deloitte – best practice disclosures

- Koster, O., and Igoe, S. 2020a. How COVID-19 infects financial reporting and results presentations - Q1 2020. Available at:
  https://www2.deloitte.com/ch/en/pages/audit/articles/ financial-reporting-survey-q1-2020.html.

- Koster, O., and Igoe, S. 2020b. How COVID-19 continues to infect financial reporting - financial reporting survey Q3 2020.

  Available at:
  https://www2.deloitte.com/ch/en/pages/audit/articles/ financial-reporting-survey-q3-2020.html.

Academic research on effects of COVID-19

- Research is sparse, tends to be country-specific and based on small samples covering at most fiscal 2020
  - Data availability, including in machine-readable commercial databases
  - Lengthy peer review processes
- Tends to document effects on reporting outcomes and disclosures
  - Subsequent events/events after the balance sheet date
  - Asset impairments
  - Declines in revenues and/or profitability
  - Declines in investing activity
  - Discussions of COVID-19 effects

COVID-19's impact on nonfinancial/sustainability reporting

- Advice from regulators, accountancy firms and sustainability advocacy and consulting firms
  - Regulatory reviews of nonfinancial information to focus on COVID-19's effects on, in particular, **social/employee matters, value creation, risks related to climate change**
    - e.g., ESMA (2021)
  - Some securities regulators encourage disclosures to **assist investors in evaluating COVID-19's effects "through management's eyes"**
    - Guidance from the US SEC Division of Corporate Finance (2020)
      - Effects on employees, for example, job security and telework/ "work from home" arrangements
      - Effects on suppliers and supply chains
      - Efforts to support local communities

Research on COVID-19's impact on nonfinancial reporting

- Research is sparse, and tends to report descriptive analyses of small nonrandom samples including corporate responses to COVID-19 in terms of safety, logistics, maintaining continuity of operations and, human rights
    - *Examples of findings in some (not all) research reports/papers*
        - 2020 declines in meeting sustainability goals and in sustainability reporting performance as compared to 2018/2019
        - Financial constraints associated with COVID-19 result in re-allocations of resources away from sustainability efforts and sustainability reporting

- We identified only three academic research papers related to COVID-19's effect on nonfinancial reporting.

COVID-19's impact on assurance (1)

- Advice from IOSCO, IFAC, IAASB and accountancy firms to assurance professionals
  - Regulators and others acknowledge challenges/difficulties with performing audits ***but*** **professional responsibilities are unchanged**
    - *Examples*
      - Reporting on critical/key audit matters and how they were addressed
      - Communications with management and audit committees/governing boards
      - Assessing management's judgment with respect to the entity's ability to continue as a going concern
      - Difficulty (or inability) to obtain sufficient appropriate audit evidence because of travel restrictions, lockdowns and distancing requirements
        - » *Example:* EY audit of Target Corporation (NYSE) included steps to address suspension of physical inventory counts

COVID-19's impact on assurance (2)

- Practice-oriented and academic research
  - Discussions of features of the COVID-19 audit environment (applicable to both financial reporting and non-financial reporting)
    - Geographically dispersed audit teams all working remotely (not in offices)
      - Quality control, supervision and the review process
      - Remote work could be persistent feature of audits
    - Operating and financial pressures on management might increase misstatement risk
    - Ways to address difficulties in obtaining audit evidence
  - Descriptive analyses of audit reports
    - Frequency of COVID-19-related critical (key) audit matters by area (for example, intangible assets including goodwill)
    - Cross-sectional analyses by industry and firm size

Suggestions for future research

- Bauer, T. D., Humphreys, K. A. and Trotman, K. T. 2021. Group judgment and decision making in auditing: Research in the time of COVID-19 and beyond. Auditing: A Journal of Practice & Theory.

- Humphreys, K.A. and Trotman, K.T. 2021. Judgment and decision making research on CSR reporting in the COVID-19 pandemic environment, Accounting and Finance.

Audit Analytics

- Audit Analytics. 2020. Covid-19 impacts on European audit opinions. November. Available at: https://blog.auditanalytics.com/covid-19-impacts-on-european-audit-opinions/.

- Coleman, D. Conley, M., and Hallas, N. 2021. Audit Analytics Impacts of COVID-19 on public companies. August. Available at https://www.auditanalytics.com/doc/AuditAnalytics_Impacts_of_COVID-19_on_Public_Companies.pdf.

- Hallas, N. 2021. Insights from COVID-19 references in CAMs. March. Available at: https://blog.auditanalytics.com/insights-from-covid-19-references-in-cams/.

Concluding comments

- Schippper and Street found no systematic evidence that existing financial reporting and auditing standards are insufficiently robust to pressures from effects of COVID-19
  - *However:* the pressures are far from over and the evidence available to us is based on small nonrandom samples
- Some evidence suggests COVID-19 related changes to the conduct of assurance engagements might be durable
  - Use of technology to co-ordinate dispersed audit teams and to communicate with audit committees/governing boards
- Found examples of thoughtful suggestions for future research (as more archival data become available and as researchers develop experimental instruments to analyze COVID-19-related changes in judgments and decisions)
  - Did standards to account for credit losses promulgated in response to the financial crisis of 2007-2009 perform well under COVID-19-related pressure?
  - How did the high uncertainty caused by COVID-19 affect nonfinancial reporting and assurance and the willingness to pursue sustainability efforts?
  - How does a reduction in face-to-face work (in financial reporting and auditing) affect outcomes?

Effects of COVID 19 on Financial Reporting, Nonfinancial Reporting and Assurance

Early Findings from Research and Information Provided by Securities Regulators, Standard Setters and Professional Accountancy Organizations

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A reflection on credit loss accounting in European banks under Covid-19

A discussion prepared for the UNCTAD-ISAR – IAAER Workshop
8 November 2021

Sebastian Hoffmann, HHL Leipzig Graduate School of Management & University of Edinburgh

Topic: Expected Credit Loss (ECL) Accounting

ECL During COVID-19

Markets

ECB Gives Banks Further Virus Relief With Break on Bad Loans

By Alexander Weber, Nicholas Comfort, and John Ainger
20 March 2020, 15:30 GMT *Updated on 20 March 2020, 16:17 GMT*

- Banks will benefit from state guarantees, payment holidays
- ECB recommends that banks avoid excessive loss provisions

Opinion **Inside Business**

Bank accounting an early casualty of Covid-19

Rules designed to resolve the tests of the last financial crisis have already flunked this one

BoE warns bank loan reserves risk choking business funding

New accounting rules pose threat to banks amid coronavirus crisis

A Dialogic Mobilisation of The Public Interest

— A Coordinated Regulatory Push

EUROPEAN COMMISSION

Commission Interpretative Communication on the application of the accounting and prudential frameworks to facilitate EU bank lending

Supporting businesses and households amid COVID-19

- Coordinated regulatory guidance by the ECB, EBA, and PRA, specifically on the implementation and operation of ECL within banks during the COVID-19 crisis.
- Result: a coordinated re-interpretation of IFRS 9's ECL framework in order to
    - Provide banks with **more accounting flexibility**
    - **Prevent** the use of public support measures from becoming **a loss signal** in terms of expected credit loss estimation
    - **Mitigate pro-cyclicality** and the impact of COVID-19 on financial stability, crucially through long-term macroeconomic forecasting

A Dialogic Mobilisation of The Public Interest

— Stirring Traditional Responsibilities For Accounting & Control

ECL as the amalgam of governmental and managerial interference

Government Measures

- Payment holidays delay the materialisation of defaults
- Government guarantees transfer default risks from commercial banks to the state
- Regulatory guidance for banks, to prevent a credit and liquidity crunch of the economy

Management Policies

- Prudent lending
- Good-quality loan books
- Proactive risk management
- Conservative estimates
- Management overlays

ECL

ECL and Prudential Regulation

1. **Adding to existing studies on de facto prudential biases in the practices of accounting due to supervisory intervention (e.g. García Osma et al. (2019), Novotny-Farkas (2016), and Giner & Mora (2019))**
2. **The case of IFRS 9 ECL: Regulators and governments become "earnings managers" of banks.**
3. **The usefulness, uses, utilities and limitations of financial reporting in highly regulated settings???**

38th ISAR
Covid 19 effect on financial reporting in Turkey

Prof. Dr. Cagnur Kaytmaz Balsari
Dokuz Eylul University, Faculty of Business

AACSB Business Education Alliance Member

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Research Findings in Turkey

Financial Effect

- Covid 19 did not have the same effect in all industries, but some common effects are;
  - **Liquidity issues**
  - **Short term financing increased**
  - **Inventory management, trade credits & e-commerce**
- Banks funded the economy generously.

Reporting Issues

- Covid 19 has been mentioned in the financial reports in at least in one section.
- Explanations about Covid-19 are mostly included in the footnotes of **events after the reporting period.**
- Banking sector has made the most explanation in financial reports.
- Mostly reported Key audit matters are; revaluation, impairment, and revenue recognition.
- Very few audit reports addressed “Going Concern”.

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Thank you…

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- Balsari C., Sigali S., Dalkilic A. F. , Demir G.; 2021, "Covid 19 sürecinin ulaştırma depolama ve haberleşme sektöründeki işletmelerin finansal tabloları üzerine etkisinin değerlendirilmesi (A review of Covid-19 effect on financial statements in transportation and telecommunication industries)", Covid 19 Salgınının İşletmelerin Finansal Tabloları Üzerine Etkisine İlişkin Araştırma Sonuçlarının Değerlendirilmesi (Evaluation of research findings of Covid-19 pandemic effect on financial statements), pg 734-747, Editors, Akdoğan N, Doğan D, Cetinkaya N; Gazi Yayinevi, ISBN: 978-625-7530-48-4.
- Baskan, Tuba Derya, (2020), "Analyzing The Going Concern Uncertainty During The Period of Covid-19 Pandemic in Terms of Independent Auditor's Reports", ISPEC International Journal of Social Sciences & Humanities, Y. 4, S. 2, s. 28-42.
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- Köse, Tunç; Ağdeniz, Şafak, (2020), "Covid-19 Salgınının BDS 570 İşletmenin Sürekliliği Standardının Uygulama Sürecine Etkileri", Mali Çözüm Dergisi, Volume 30/161, s. 69- 94
- Karakaya, Gencay, (2020), "Covid - 19 Gündeminde İşletme Sürekliliği ve Bağımsız Denetim İlişkisi", İstanbul Ticaret Üniversitesi Sosyal Bilimler Dergisi, Y. 19, S. 37 Bahar (Covid19-Özel Ek) , s. 14-29.

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