A collective voice for the development of UK-based business

THE HUNDRED GROUP
OF FINANCE DIRECTORS

Looking ahead

COVID-19 special edition

June 2020

The 100 Group briefing

Dear members of The 100 Group,

Welcome to the latest edition of The 100 Group briefing. Coronavirus (COVID-19) has put enormous strain on an already challenging economic environment for many companies in the UK. In this edition, we focus on a number of the potential implications for accounting, reporting and auditing.

Over the last few months, the pandemic, the lockdown, and the government's response, has given rise to a great deal of regulatory activity affecting accountants and finance teams.

You could be forgiven for being overwhelmed by the array of new regulatory announcements, filing extensions and guidance that has been issued over the last four months. While individually, each development has been helpful for companies dealing with the challenging circumstances the pandemic has created, in total there is now an additional layer of materials that need to be read, understood, and followed.

To help you navigate through this complexity, in a departure from our usual approach, we have provided a digest of the regulatory developments that have been issued over the last few months in relation to COVID-19. We compiled and refined this information into an easy-to-follow format to ensure you and your teams are up to speed with the latest developments.

We need to stress that this document is only accurate up to the date of writing and therefore any developments from the end of June onwards will need to be separately assessed. However, in covering the period from March through to June, we hope this digest will assist your efforts in keeping abreast of the multitude of new regulatory publications.

I hope you find the briefing useful - please do let me know what you'd like to see more of in future publications.

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Looking ahead

The 100 Group briefing, *Looking ahead*, is a quarterly briefing commissioned by the 100 Group of Finance Directors. Its aim is to brief the Group on key developments in the capital markets and proposed changes in regulation and standards that might require response, lobbying, or which are important for general awareness.

For further information, please contact *Gilly Lord.*

Executive summary

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Publishing annual financial reports		The FCA, FRC and PRA have issued a joint statement in which the FCA has allowed main market listed companies an extra two months to publish their audited annual financial reports, giving them six months in total. The London Stock Exchange (LSE) has said that AIM companies with financial year-ends between 30 September 2019 to 30 June 2020 are also allowed a three month extension to publish their annual financial reports.
Filing accounts at Companies House		Companies House has allowed an extra three months for public companies and private companies to file their annual accounts.
Publishing half year financial reports		The FCA has released a statement of temporary relief for listed companies to publish their half yearly reports, allowing an extra month after the half year-end, taking the deadline to four months. The LSE has also allowed AIM listed companies an extra month to notify half yearly reports.
Regulatory reports and returns		The PRA and FCA have issued temporary deadline extensions for submission of annual report and accounts and other regulatory returns.
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Corporate and narrative reporting		The FRC has issued guidance for companies on corporate/narrative reporting in their annual reports to focus on the information of most interest to investors and to help apply existing FRC Guidance to the current circumstances.
Modern slavery		The government has launched a new web page to provide guidance for businesses reporting under the Modern Slavery Act during the COVID-19 pandemic.
Alternative performance measures		ESMA and the FRC have each issued guidance on reporting of COVID-19 related alternative performance measures.
Section 172 reporting		Section 172 reporting and stakeholder engagement, as well as the areas of increased emphasis in the 2018 UK Corporate Governance Code, could be highly relevant for reporting on the impact of COVID-19.
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Going concern		The FRC, FCA, ICAEW and ICAS have all offered guidance to help companies navigate accounting complexities around COVID-19, including forecasting for purposes of going concern assessments.
Other accounting matters		There have been updates and guidance on a range of other accounting matters including: ● Application of regulatory capital, payment holidays and IFRS 9 ● Expected loss provisions under IFRS 9 ● Capital maintenance ● Events after the reporting date ● Valuation uncertainties ● Leases and rent concessions ● Capital maintenance

Executive summary (cont'd)

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Specific governance considerations for preparers		The FRC has issued guidance for companies on governance considerations when preparing annual reports and financial statements in the current uncertain environment.
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Working capital statements		The FCA is overriding the requirement that bans assumptions from being disclosed by allowing unqualified working capital statements to include disclosure of COVID-19 related assumptions underlying the reasonable worst case scenario.

Filing deadlines

Due to the many uncertainties surrounding COVID-19, a number of regulators and other bodies have decided to allow companies additional time to publish and/or file their annual and half yearly financial reports and other regulatory returns.

1. Publishing and filing of annual financial reports

Publishing annual financial reports
On 26 March 2020 the Financial Conduct Authority (FCA), Financial Reporting Council (FRC) and Prudential Regulation Authority (PRA), issued a joint statement and related guidance for companies and auditors in dealing with the impact of COVID-19. This allowed main market listed companies an extra two months to publish their audited annual financial reports, which means six months in total. Both the FCA and the FRC strongly encourage companies to consider the full use of this timetable.

The London Stock Exchange (LSE) has said that AIM companies with financial year-ends between 30 September 2019 to 30 June 2020 are also allowed a three month extension to publish their annual financial reports. An AIM company currently has six months to publish audited financial reports and this extension will increase that period to nine months.

On 6 April the FCA announced that it will allow authorised fund managers of UK UCITS schemes and non-UCITS retail schemes an extra two months to publish their annual financial reports (taking the current requirement from four months post year-end to six months). Firms must let the FCA know if they intend to use the extension.

Filing annual financial statements with Companies House
Companies House has also extended the filing deadlines for public companies to nine months and private companies to 12 months.

2. Publishing half yearly financial reports

On 27 May the FCA released a statement of temporary relief for listed companies to publish their half yearly reports. The existing deadline is three months after the half year-end. The extension allows an extra month, taking the deadline to four months. There is no stated timeline for how long this forbearance will last.

The Q&A included in the statement provides more details over which other companies this temporary relief applies to.

On 9 June, the LSE set out temporary changes relating to an AIM company's obligation to notify half-yearly reports in accordance with the AIM Rules for Companies (AIM Rules). Currently under the AIM Rules, an AIM company must notify its half-yearly report within three months from the end of the period to which it relates.

From 9 June, AIM Regulation permits AIM companies that need extra time to prepare their half-yearly report an additional one month in which to notify them. This extension is temporary whilst the UK faces the disruption resulting from the coronavirus (COVID-19) pandemic. An AIM company wishing to utilise the additional one month period must notify via an RIS its intention to do so prior to the AIM company's reporting deadline under AIM Rule 18 and the company's nominated adviser must separately inform AIM Regulation.

On 6 April the FCA also announced that it will allow authorised fund managers of UK UCITS schemes and non-UCITS retail schemes an extra one month to publish half-yearly reports (taking the current requirement from two months post half year-end to three months). Firms must let the FCA know if they intend to use the extension.

Filing deadlines (cont'd)

3. Regulatory reports and returns

PRA regulatory reporting
On 2 April the PRA issued an announcement outlining their approach to regulatory reporting. In the statement, the PRA stated that it will accept delayed submission for annual reports and accounts of up to two months where the remittance deadlines contained in the PRA rulebook fell on or before 31 May 2020. This deadline has now passed, but the PRA did also say that they will consider whether the actions in the announcement will be extended to reporting beyond that due by the end of May 2020 in due course.

FCA regulatory reporting
On 22 April, the FCA issued temporary extensions to deadlines for certain regulatory reports that were due up to and including 30 June 2020. These regulatory returns include those required by the SUP16 Handbook and several other Handbook returns. On 26 June the FCA said that, for the following returns, the two month extension would continue for reports due up to and including 30 September 2020:

- Credit union complaints return (CREDS 9 Annex 1R)
- Complaints Return (DISP Annex 1R)
- Claims management companies complaints return (DISP 1 Annex 1AB)

For other returns listed in the original announcement (for example, Annual financial reports) forms falling due after 30 June 2020 should be submitted by their usual deadlines.

All of these extensions are expected to be temporary and companies should consult the websites of each individual body for the most up to date information if contemplating making use of an extension.

4. HMRC filing deadlines

As at time of writing, there has been no extension in the HMRC filing deadline for tax returns. Where an HMRC tax return filing deadline is 12 months from the end of the financial year, there could be logistical difficulties in preparing tax returns for companies that have taken advantage of the three month extension to the Companies House accounts filing deadline noted above (taking it to 12 months) as their tax return would be due on the same date. Companies planning to take advantage of the Companies House extension to file their accounts after 12 months, should build in the time to also complete their tax return.

Annual General Meetings (AGMs)

There has been a general concern about the feasibility of holding in-person AGMs when COVID-19 lockdown or social distancing measures are in place. Also, questions have been raised over the current AGM deadline of six months after the financial year-end in light of the FCA's allowance that a listed company also now has up to six months to publish their annual financial information and what this means for the required notice period.

The Business Secretary said on 28 March that *"the government will introduce legislation to ensure those companies required by law to hold Annual General Meetings (AGMs) will be able to do so safely, consistent with the restrictions on movement and gatherings introduced to address the spread of coronavirus. Companies will temporarily be extended greater flexibilities, including holding AGMs online or postponing the meetings."* This legislation is included in the Corporate Governance and Insolvency Bill that was published on 20 May and received Royal Assent on 25 June.

In respect of AGM deadlines, the existing deadline for a public company AGM is that the meeting must be held no later than six months after the end of the financial year. For those companies required to hold their AGM prior to 30 September 2020, for example, by the end of June, July or August, the Bill gives retrospective effect to an extended period allowing them to hold the AGM up to 30 September 2020. That means that extension benefits companies with February 2020 or earlier year-ends. The legislation provides a mechanism for allowing further extensions if it is determined these are needed.

BEIS and the FRC have jointly issued a Q&A on this legislation as it relates to annual and other company meetings. The Q&A includes discussion of the provision for extending the deadline for holding an AGM.

The Q&A also sets out responses to queries including flexibility for holding AGMs, use of technology for virtual meetings and provision of hard copies of documentation including notice of AGMs.

This is an evolving area and companies should consult the relevant government website for the most up-to-date information if contemplating making use of the changes to their AGM.

Company reporting

It's very likely there will be increased scrutiny on company reporting during and after the COVID-19 pandemic. Transparent and robust reporting will be essential to help shareholders navigate the impact the pandemic has had on the company. As a result, a number of pieces of guidance around company reporting, in particular risks and uncertainties, going concern and viability and alternative performance measures, have been issued by a number of different bodies.

1. Corporate and narrative reporting

The FRC has issued guidance for companies on corporate/narrative reporting in their annual reports that is intended to focus on the information of most interest to investors and to help apply existing FRC guidance to the current circumstances – including the need to be forward-looking and company-specific. Particularly relevant parts of the annual report will include:

- *Principal risks and uncertainties:* The FRC notes that *“a company should consider the specific resources, assets and relationships that are most under threat and the steps being taken to protect them”*. This will include the workforce in many cases.

- *Viability statements:* The FRC recognises that there will often be a lower degree of confidence than usual, and encourages boards to *“describe the limits of the predictions, the level of confidence with which they have been made and the uncertain future events that could prove critical to viability”.*

The FRC guidance also contains comments relating to going concern disclosures. These are included in the section on Accounting.

The FRC’s Reporting Lab has also produced an infographic setting out five areas in which investors are looking for information, from cash holdings, liquidity options and cost control measures through to assessing and protecting the ongoing viability of the business model.

The FRC's Financial Reporting Lab has also issued two reports on the areas of reporting that investors have emphasised as being most important during the COVID-19 pandemic. The first report, 'COVID 19 – Resources, action, the future', expands on the topics highlighted in the Lab’s infographic. The second report addresses the impact of COVID-19 on 'Going concern, risk and viability'.

Both reports include reminders of existing guidance, questions for boards to consider, and a large number of examples of current reporting practices.

Overall, the FRC has said that *“the need for fuller disclosure is paramount”* – despite the sensitivity that will often be connected with the relevant information.

Modern slavery
On 20 April, the government launched a new web page to provide guidance for businesses reporting under the Modern Slavery Act during the COVID-19 pandemic. In light of the pandemic, the guidance says that, as well as focusing on the health and safety of their workers, businesses will need to consider how fluctuations in demand and changes in their operating model may lead to new or increased risks of labour exploitation. It also recognises that businesses may need to delay the publication of their modern slavery statement by up to six months and will not penalise those that do so.

Company reporting (cont'd)

2. Alternative performance measures

ESMA guidelines on APMs

In April, ESMA added an additional FAQ on its Guidelines on Alternative Performance Measures, 'Application of the APM Guidelines in the context of COVID-19'. ESMA acknowledges that companies may decide to disclose new, or to adjust, APMs to reflect the impact of COVID-19, but reminds companies that the definition and calculation of an APM should be consistent over time.

It states that companies should carefully assess whether the revisions to APMs would provide transparent and useful information, and improve the comparability, reliability and/or understandability of the measures presented.

ESMA also observes that it may not be appropriate to include new or adjusted APMs when the impacts of COVID-19 are pervasive. In such cases, ESMA urges companies instead to provide narrative explanations of how COVID-19 has impacted their operations and performance, the level of uncertainty and the measures adopted or expected to be adopted to address the business implications of the outbreak.

FRC guidance on reporting exceptional items and APMs

The FRC has issued guidance for companies to explain how they should report exceptional items and alternative performance measures (APMs). The guidance doesn't introduce any new principles. However, it does reiterate the most relevant principles from previous FRC guidance and how they might apply in the context of COVID-19. In particular, the FRC highlights a number of approaches that are either not permitted or which it discourages companies from following. Specifically, companies should **not**:

- describe amounts as 'non-recurring' or 'one-off' if they are also expected to arise in future periods;
- disclose costs (sometimes described as 'stranded', 'sunk' or 'excess') as exceptional solely because of a reduction in, or elimination of, the related revenue streams due to the COVID-19 pandemic;
- identify incremental costs as exceptional if they result in incremental revenue that is not also described as exceptional; for example, additional staff costs related to managing unusually high levels of sales of in-demand items; or
- present a subtotal derived on a hypothetical or 'pro-forma' basis (for example, by adding back an estimate of 'lost' revenue), either as a line item or in a 'third column' format.

Similar to guidance from ESMA published in April, the FRC observes that the impact of COVID-19 might be pervasive and hard to quantify. In such circumstances, it might be more helpful to provide narrative explanations of the nature of the items and the uncertainties around them. Measures which attempt to provide a measure of 'pro forma' or 'normalised' profit, excluding the estimated effect of COVID-19, are likely to be highly subjective and, therefore, potentially unreliable. In addition to the subjectivity arising around which costs to exclude, there might also be reductions in revenues, adjustment for which would be hypothetical and could not be reflected reliably. Accordingly, the FRC does not expect companies to provide such 'normalised pre-COVID-19' measures in their accounts.

Company reporting (cont'd)

3. Section 172 reporting

Much of the new reporting on Section 172 and stakeholder engagement, as well as the areas of increased emphasis in the 2018 UK Corporate Governance Code, are highly relevant for reporting on the impact of COVID-19. Good reporting will explain the balance that has been struck, and why, in decisions including:

- whether or not to pay dividends (or return capital in other ways);
- whether and how to raise more capital or other forms of finance;
- the treatment of employees and the wider workforce (including changes to pay and conditions);
- executive pay (including bonus entitlements and long-term incentive schemes);
- the treatment of customers and suppliers;
- the use of the various forms of government support that are potentially available;
- other capital allocation decisions including whether to cancel or scale back capital expenditure, research & development and so on.

These disclosures will be particular important for companies who have benefitted from government support and will therefore have to consider the needs and expectations of different groups of stakeholders in a post COVID-19 world.

4. Half yearly reports

ESMA has also issued a Public Statement on the reporting implications of COVID-19 for half yearly reports. There is no new guidance in the statement, but it does provide a useful summary of issues that ought to be considered, in particular:

- encouragement to take sufficient time to provide relevant and reliable information, which may require companies to make use of more of the time allowed by national law while not unduly delaying the timing of publication;
- the importance of updating information included in the latest annual report to adequately inform stakeholders of the impacts of COVID-19, in particular in relation to significant risks and uncertainties, going concern and impairment; and
- the need for entity-specific information on the past and expected future impact of COVID-19 on the company's strategic orientation and targets, operations, and performance, as well as any mitigating actions put in place to address the effects of the pandemic.

Accounting

Measures to prevent transmission of COVID-19 include limiting the movement of people, restricting flights and other travel, temporarily closing businesses and schools, and cancelling events. This has had an impact on businesses such as tourism, transport, retail and entertainment. It has also affected supply chains and the production of goods throughout the world, and lower economic activity has resulted in reduced demand for many goods and services. Financial services entities (such as banks that lend to affected entities, insurers that provide protection to affected individuals and businesses, and funds or other investors that invest in affected entities) have also been affected.

Companies should carefully consider the impact of COVID-19 on both half yearly and annual financial statements. The impact could be significant for many businesses. The implications for financial statements include not only the measurement of assets and liabilities but also disclosure and possibly an entity's ability to continue as a going concern. The implications, including the indirect effects from lower economic activity, should be considered by all entities, not just those in the territories most significantly affected.

Here are some of the most recent developments in this area:

1. Going concern

Forecasting issues
Companies continue to face challenges around forecasting for purposes of going concern assessments in such uncertain times, in particular when anticipating the likely shape of any economic recovery. So, it's worth remembering the FRC's comment in their guidance for companies that the UK Office for Budget Responsibility, the International Monetary Fund and the OECD have produced projections for economic activity that companies may use as an anchor for their own scenarios (refer to the section on going concern and material uncertainties).

The FRC guidance also contains comments relating to going concern disclosures that it is likely that more companies will disclose 'material uncertainties' over going concern in current circumstances and management should consider the potential implications of COVID-19 and the measures taken to control it when assessing the company's ability to continue as a going concern. Note that a company is no longer a going concern if management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. Even if a company is assumed to be a going concern, there may still be a material uncertainty that may cast significant doubt on whether it will continue to be a going concern, which should be disclosed. Similarly, if the directors conclude that there is not a material uncertainty that meets the criteria for disclosure, but this conclusion requires the exercise of significant judgement, then this also should be disclosed.

Accounting (cont'd)

Going concern considerations for different sized companies
Both ICAEW and ICAS have been active in providing guidance to companies around assessing and disclosing matters relating to going concern:

- **ICAEW issues a guide to going concern considerations for preparers**
  ICAEW has issued a guide that summarises management's responsibilities for assessing going concern and the associated practical implications for financial reporting, in light of the COVID-19 pandemic. The guide is aimed primarily at entities preparing accounts in accordance with FRS 102 but includes considerations that they say can be broadly applied to all entities.

- **ICAEW and ICAS issue joint guidance on going concern for SMEs**
  ICAS and ICAEW jointly published guidance on going concern for small and medium entities (SMEs). The publication aims to explain to small and medium business owners and directors the importance of forecasting cash flow and how to reflect the impact of COVID-19. Additionally, it provides suggestions on how to work with auditors and accountants during the pandemic, including the need to provide evidence which shows that conclusions reached regarding going concern are reasonable.

- **ICAS issues guidance for large private companies on going concern assessments**
  ICAS has issued guidance to assist directors of large private companies in their assessment of whether use of the going concern concept of accounting is appropriate when preparing financial statements.The guidance complements the joint guidance on going concern with ICAEW targeted at the directors of SMEs.

- **ICAEW issues an introduction to reverse stress testing**
  ICAEW has issued a guide that introduces reverse stress testing as a tool that all entities can use to enhance their going concern assessments and improve risk assessment during the COVID-19 pandemic and beyond.

The FCA has also released a statement that it understands that issuers may face difficulties where the auditor's review of the going concern assessment highlights a need for auditors to include remarks in their opinion and that this will be viewed unduly negatively by investors and intermediaries. In the statement, the FCA stresses that it is vital that investors are properly informed as to the impact of COVID-19 and are continuing to urge issuers and auditors to be clear and transparent about these impacts in their financial statements.

However they reiterate what was said in the joint statement on 26 March, that in these extraordinary circumstances, previous market practice needs to adjust. Market participants, including intermediaries, should not draw unduly adverse inferences from these disclosures, nor from issuers changing their financial calendars to make use of the extra time we have allowed them.

Accounting (cont'd)

2. Other accounting matters

Guidance on application of regulatory capital, payment holidays and IFRS 9
The Bank of England (BoE) has issued a statement updating their previous statement on the challenges of COVID-19 and their Dear CEO Letter to UK banks and building societies that provided guidance on, among other things, the application of Expected Credit Losses (ECL) and of the regulatory definition of default in the context of COVID-19. This new statement notes that there is no change to the guidance for payment deferrals granted to borrowers for the first time. However, borrowers coming to the end of an existing payment deferral will have different abilities to pay and varying financial situations. This statement highlights that the key judgment for regulatory capital and ECL purposes is whether those borrowers who do not resume full payments at the end of a payment deferral should be treated in default (for CRR) or as having suffered a significant increase in credit risk or credit impaired (for IFRS 9) and provides guidance for UK banks and building societies to consider in that regard.

Expected loss provisions under IFRS 9
The PRA has issued guidance that goes into detail on the approach that should be taken by banks, building societies and PRA-designated investment firms in assessing expected loss provisions under IFRS 9. This subject has attracted a great deal of attention, such that the IASB took the unusual step of publishing its own educational material on the subject. The PRA encourages lenders to consider the need to treat covenant breaches which arise from the COVID-19 pandemic differently from other covenant breaches.

Capital maintenance
The FRC has issued guidance for companies highlighting the importance of capital maintenance and the need to have sufficient reserves to cover dividends when they are paid as well as proposed. For some businesses, the impact of COVID-19 in recent weeks has been significant and it should not be assumed that distributable profits that existed at the most recent balance sheet date still exist. Directors must therefore specifically consider whether the company will still be solvent following payment of a proposed dividend to fulfill their fiduciary duties. This should take into account both any change in the financial position of the company since the last balance sheet date and the future cash needs of the company, which may have changed significantly since the dividend was proposed. Separately, the PRA wrote to the seven largest systemically important UK deposit-takers to ask them to cancel dividends (and cash bonuses) for the rest of 2020.

Events after the reporting date
The FRC guidance also highlights considerations in relation to events after the reporting date. The global situation is evolving rapidly. Companies should therefore consider whether the latest developments provide more information about the circumstances that existed at the balance sheet date. Events that provide more information about the spread of the virus and the related costs might be adjusting events. Events, such as the announcement or enactment of new measures to contain the virus or decisions taken by management are likely to be non-adjusting. Clear disclosure of non-adjusting events is required when this is material to the financial statements. Remember that events after the reporting date that indicate an entity is no longer a going concern are always an adjusting event.

Accounting (cont'd)

Valuation uncertainties
Following the declaration of COVID-19 as a pandemic by the World Health Organisation, the Royal Institution of Chartered Surveyors (RICS) announced that all forthcoming RICS independent valuations should, at the valuers' discretion, include a statement highlighting 'Material Valuation Uncertainty' in response to COVID-19 and the impact it is having on real estate markets. RICS has issued additional guidance stating that the clause is a disclosure and not a disclaimer. They expect the valuer to be able to prepare fair valuations at 31 March 2020 onwards despite the clause on material valuation uncertainty but feel that it is appropriate, in the current extraordinary circumstances, to draw attention to that fact that less certainty can be attached to the valuation than would otherwise be the case. It may, therefore, be appropriate to include disclosures in the financial statements referring to the resulting significant estimation uncertainty where there are material property valuations, including disclosures relating to pension schemes where a material proportion of the schemes' assets is invested in property and property funds.

Leases and rent concessions
The IASB has issued an amendment to IFRS 16 to provide lessees with an optional exemption from having to determine whether certain rent concessions (such as rental holidays or deferrals) occurring as a consequence of the COVID-19 pandemic should be accounted for as lease modifications.

Applying IFRS 16's requirements to a potentially large volume of COVID-19-related rent concessions could be practically difficult, especially in the light of the many other challenges companies are facing. In the absence of the new exemption, IFRS 16 requires a lessee to assess individual lease contracts to determine whether any concessions are to be accounted for as lease modifications, which would result in remeasurement of (and potentially an increase in) the lease liability using a revised discount rate. By applying the exemption, a lessee will instead in most cases treat a rent concession as a variable lease payment in the period in which it arises.

The new exemption applies to COVID-19-related rent concessions that reduce lease payments due on or before 30 June 2021, and is effective immediately, although it has not yet been endorsed for use within the EU. Indications are that it will be endorsed fairly quickly, although possibly not before many June interim results are reported.

Audit

Trust in the financial information put out by a company has never been more important than in these very uncertain circumstances. Auditors will face their own challenges around carrying out audits under lockdown or social distancing measures, in particular, being able to gain sufficient appropriate audit evidence over key areas of judgement, like going concern. Here are just a few of the key considerations for the audit during the pandemic.

1. Audit timings and evidence gathering

The FRC guidance for audit firms seeks to help overcome challenges in obtaining audit evidence. The FRC notes that more modifications of audit opinions and audit reports will be expected during this disrupted period. Companies may need to provide additional evidence and information to auditors around areas impacted by COVID-19, in particular around going concern, and the auditor may need to develop alternative audit procedures to gather sufficient, appropriate audit evidence. Companies need to be open to all these possibilities. Additional time may be required to complete audits and this could result in delays in issuing audited results or it could mean that there are limitations of scope in audit reports where sufficient audit evidence was not available or audits couldn't be completed as planned.

Recognising the current restrictions on travelling, movement and visiting client sites, the FRC updated its COVID-19 guidance to include guidance on gathering audit evidence through remote means

2. Implications for audit reports and opinions

In its COVID-19 Bulletin issued in March, the FRC said it may be likely that the current circumstances lead to more modified opinions in auditors' reports than would typically be the case. With this in mind, it's important that companies, shareholders and the market understand the different types of modifications that may arise. As a reminder, the different types of opinion are as follows:

- *Qualified opinion*
  In situations where:

  - an auditor hasn't been able to obtain sufficient audit evidence over a particular account balance or class of transactions (i.e. a limitation of scope); or
  - there are unresolved disagreements with management over an accounting treatment; or
  - there are misstatement(s) that have not been corrected and the impact is material,

  the audit opinion will be qualified due to error or limitation of scope. The opinion is otherwise "clean" except for this particular matter.

- *Adverse opinion*
  If, in the situation where there is an unresolved disagreement or uncorrected misstatement(s) that is material AND it is pervasive to the financial statements (for example, correcting the error would change a profit into a loss) then an adverse opinion would be issued, which means the auditor considers that the financial statements do not give a true and fair depiction of the company's financial position and performance.

- *Disclaimer of opinion*
  Where a limitation of scope is pervasive, a disclaimer of opinion will be issued, which means the auditor did not have enough evidence to form an opinion at all.

Audit (cont'd)

Emphasis of matter and material uncertainties relating to going concern
There may also be an Emphasis of Matter (EoM) in an audit report. An EoM serves to draw attention to a specific disclosure in the financial statements (for example, an ongoing uncertainty around the valuation of an asset). Until recently, EoMs were also used to highlight material uncertainties in relation to going concern. These uncertainties now fall under a separate header in the audit report, 'material uncertainties related to going concern', (although it will continue to be an EoM in a half year review report). **It's important to note that, on its own, the inclusion of an EoM or material uncertainty over going concern is NOT a modification or qualification of the audit opinion, the audit opinion is still 'clean'.** However, these are important disclosures and it is possible we will see more of them due to the impact of COVID-19, as highlighted in the FRC's COVID-19 update.

The FRC has also published guidance on modified auditors' opinions and reports during the COVID-19 pandemic.

- Previous guidance, issued on 16 March, highlighted the possibility that current circumstances may require auditors to consider modifying their audit opinion.

- The latest guidance expands on this and includes a helpful flowchart setting out the circumstances in which modifications (qualifications) to the auditor's opinion are made, and those in which additional disclosures are made in the auditor's report. A material uncertainty over going concern is an example of an additional disclosure.

3. Specific audit considerations

IFRS 9 and COVID -19 guidance for banks
ICAEW's Financial Services Faculty has published a guide to help banks and their auditors deal with the effects of coronavirus (COVID-19) on financial reporting under IFRS 9 'Financial Instruments'.

Auditing going concern
The Audit and Assurance Faculty of the ICAEW has issued a two part guide for auditors, covering COVID-19 implications when considering going concern, and how to report when a material uncertainty relating to going concern exists. Companies may find this a useful reference point in considering the information their auditor may require.

Half year report reviews
The FRC has updated its previous guidance to companies on reporting the effects of COVID-19 to include guidance in relation to interim reports. In the updated guidance, the FRC provides insights on considering going concern at the half year and also stresses the feedback it has received from investors that interim reviews by auditors provide valuable assurance.

Independence

The impact of audit firm or audit partner rotation on audit quality in a time of uncertainty has been considered by the regulators, as well as auditor involvement in company applications for government support.

1. Audit tenders and rotation

Audit tenders
In the FCA/FRC/PRA joint statement companies are encouraged to consider delaying tenders for new auditors, even when mandatory rotation is due (the FRC have the ability to extend audit mandates for up to two years where the initial appointment commenced after 17 June 1994). In some situations, tenders currently in train are being held well in advance of the mandatory rotation date; in these situations it may be possible to defer activity until later in 2020 and still complete the tender and choose a successor auditor with time for an orderly transition. Unfortunately, the FRC has no ability to extend mandates for pre-17 June 1994 appointments. Companies in that specific situation could discuss their approach to tendering and rotation directly with the FRC.

Audit partner rotation
The joint statement also noted that key audit partners are required to rotate every five years. However, where there are good reasons, for example to maintain audit quality in current circumstances, the rotation can be extended to no more than seven years. This needs to be agreed with the audit committee of any affected entity and does not need to be cleared with or approved by the FRC.

2. Non-audit services fee cap and emergency funding support work

Normally, auditors of PIEs cannot earn fees for non-audit services of more than 70% of the audit fee (unless the fees are for certain non-audit services that are required by law or regulation). The FRC has the ability to allow a waiver from this rule in exceptional circumstances.

Where the provision of non-audit services is required in order to assist a PIE in obtaining emergency funding in the COVID-19 environment, we believe that the FRC may be open to granting such waivers.

The FRC is alert to the need to respond quickly to such requests, and provided the guidance on their website is complied with, our experience is that they will respond within 24-48 hrs. All applications will need to be approved by the audit committee of the PIE.

Corporate governance and investor views

Maintaining an effective governance and control environment is key at a time of such uncertainty and the FRC has put out guidance for preparers in this area. Also, investors have been active in providing their views on various aspects of the COVID-19 impact.

1. FRC guidance for preparers

The FRC guidance for companies aims to help those preparing annual reports and financial statements in the current uncertain environment. The key messages in the guidance around corporate governance are:

- On corporate governance, the guidance is particularly focused on maintaining an effective control environment in a situation where key reporting and other controls may not be operating effectively. It also emphasises the need for reliable and relevant information for decision making, including from group companies and joint ventures.

- Both of these matters are primarily the responsibility of executive teams but non-executive directors – audit and risk committee members in particular – will of course have a part to play in challenging and advising.

2. Investor group views on aspects of governance affected by the pandemic

A number of investor groups have provided guidance on aspects of the COVID-19 pandemic. The UK Investment Association (IA) whose members collectively own a third of the equity of UK plc, and proxy adviser, Institutional Shareholder Services (ISS), have set out their views on areas that boards should consider.

Measures taken by companies to postpone or hold AGMs virtually have attracted widespread investor support, and the UK Governance Institute has issued guidance in this area. Companies are, however, being encouraged to continue to communicate and engage through webcasts, conference calls and similar channels, particularly where AGMs are pushed back.

Investors are also willing to support companies who need to raise additional capital, whether through rights issues, placings and/or open offers. The IA has noted that the Pre-Emption Group guidelines should still be followed, but there is general support in the current circumstances for relaxations of the regulatory regime such as those proposed by the FCA.

Corporate governance and investor views (cont')

On 31 March the PRA released a statement welcoming the decision by the seven largest UK banks to suspend dividends and buybacks on ordinary shares until the end of 2020.The Link Group, which administers financial ownership data, has subsequently produced its UK quarterly dividend monitor. For Q1 2020 this showed that 45% of a sample of 350 UK companies (including the FTSE 100 and 60% of the FTSE 350 plus around 100 smaller listed companies) have decided against paying dividends in 2020 so far. The IA supports the need for companies to consider dividends carefully, but also notes the importance of this income for pension funds and charities, stating that: *"… shareholders would be concerned if companies unnecessarily reduced or rebased the dividend level…[and] would expect companies…to restart the dividend payments as soon as it is prudent to do so*". ISS notes that it will look for evidence of dividend cuts being used to support the business or workforce.

Both the IA and ISS comment on executive pay, with the IA explicitly linking it to a company's approach to dividends and changes in the pay and conditions of the wider workforce. ISS focuses on how it will view changes to bonus scheme metrics, goals or targets and ongoing long-term incentive plans to take account of the market conditions. As is often the case, Pensions & Investment Research Consultants (PIRC) has already taken a hard-line approach in this area, calling on companies back in March to suspend payments to executives other than basic salary from 1 April until the end of the current financial year.

The Investment Association (IA) has also been asked by remuneration committees of UK listed companies and their advisors to indicate shareholder expectations of how committees should reflect the impact of COVID-19 on executive pay. The Q&As the IA issued on 27 April explain how shareholders expect adjustments to pay to be considered where a company cancels or suspends dividends, furloughs staff or raises capital. They also provide guidance on changing performance conditions, awarding LTIP grants and updating remuneration policies. Expectations will evolve as the impact of the pandemic becomes clearer, so the IA expects to update its guidance.

Other developments

Working capital statements

The FCA acknowledges that the uncertainties around COVID-19 mean that there could be difficulty in modelling reasonable worst case scenarios that underpin working capital statements included in prospectuses and class 1 circulars. Whilst this might normally lead to qualified statements being made they do not think a wave of qualified statements solely for this reason would be helpful to investors.

In these particular circumstances, the FCA is overriding the requirement that bans assumptions from being disclosed by allowing unqualified working capital statements to include disclosure of COVID-19 related assumptions underlying the reasonable worst case scenario.

Each case needs to be considered on its own and it may be that a clean working capital statement can be made without reference to any COVID-19 related assumptions or that the statement has to be qualified.