Impact of covid-19 on the classification of financial statement elements in accordance with IASs/IFRSs

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Abstract:

This study discusses key accounting and financial reporting considerations for economic entities related to conditions that may result from the COVID-19 pandemic. The purpose of this study is to highlight some of the key issues to be considered by entities in classification of elements when preparing their financial statements applying IFRS Standards. Ultimately, the study concluded with several important outcomes, whereby the impact of liquidity matters and credit risks arising from Covid-19 on classifying financial assets and liabilities as current and non-current to be the most significant.

Keywords: classification; elements; current; non-current; Covid-19.

Jel Classification Codes: M41.

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1. Introduction:

COVID- 19 was first reported to the World Health Organization (WHO) in December 2019 and it has rapidly spread to many other countries. WHO has declared it as global pandemic. COVID-19 has not only affected the health of people across the globe and it has also caused severe disturbances in the global economic environment which has consequential impact on financial statements and reporting.

Financial statements are considered as fundamental part within the financial report, where through them the accounting measurement outcomes are communicated to its users in the form of financial data and information. The method of the financial statement elements' presentation is one of the most important factors of the financial information quality that the entity is provided to the both internal and external users of the financial statements, because it represents the basis for making various decisions. For example, the lenders are relied on the entity's ability to fulfill its financial liabilities in due course to grant credit. This depends on a set of financial assessments that the lender is performed to evaluate the entity's credit capacity, such as solvency and liquidity, as well as this mainly is depended on the classification of financial statements as current and non-current. All of the above makes the lender able to get an accurate view at the entity’s credit capacity and the extent of its entitlement to obtain credit, so that it can recover its funds in due course and without significant risk.

On March 2020, the Government of many countries announced a temporary lock down as a measure to reduce the spread of the COVID – 19. Complying with the lockdown, the entity suspended its production from March 2020. The lockdown has also caused disruptions in supply chain including supply of produced goods to the customers of the entity and receipt of trade debts. The daily economic loss to the entity from the suspension amounts to significant value (in the form of gross profit for expected sales and production in the suspended period) and the entity is also facing liquidity problems on account of delayed payments from its customers. The entity has also applied to the commercial banks for relaxation in repayment of principal of its credit facilities by one year. The impact of measures to reduce the

COVID 19 has also impacted the credit risk of the customers of the entity, which along with other macro-economic factors will also impact the expected credit losses in the subsequent periods. Due to the impacts and duration for which the abovementioned measures will continue, the entity cannot avoid the overall impact on the entity's financial report, in particular, the classification of the financial statements elements in accordance with the applicable accounting standards, which are often based on IASs.

For by means what already stated can ask this question:

How does quarantine and social distancing measures to contain the corona pandemic affect the classification of financial statement elements for economic entities in the preparation of their financial reports under IASs?

Importance of searching

- Research derives importance from the significant importance of financial information in decision-making;
- The impact of covid-19 on all areas in the economic entity, in particular, with regard to the preparation and presentation of financial statements;
- The impact of covid-19 on the entity's liquidity, which is one of the most important basis for the classification of financial statement elements;
- The significant impact of covid-19 on the operation of the entity, which is also adopted as the basis in the classification of financial statement elements;
- The ever-increasing of the number of infected and deceased people as a result of the Covid-19 infection, which threatens the continuation of the closure and government constrained measures on some social and economic freedoms. Consequently the continuation of the economic, financial and accounting effects on the affected economic entities.

Targets of Search

- Presentation of financial statements of general purpose in accordance with international accounting standards;
- Definition of financial statement elements in accordance with international accounting standards;

- Explain the basis for the classification of the elements of the financial statements in accordance with international accounting standards;
- Highlighting the impact of COVID-19 on the classification of financial statements elements as current and non-current;
- Highlighting the impact of COVID-19 on the financial and non-financial elements' classification of the financial statements;
- Helping both preparers and auditors in their respective areas in discharging their professional responsibilities more effectively.

Research methodology

This topic was studied by following the descriptive approach to clarify the various concepts as well as the analytical approach in order to facilitate the full understanding of the topic by highlighting all its parts.

2. Conditions for recognition and basis for classification of elements of financial statements

A complete set of financial statements under IAS 1 comprises the following: (IASC Foundation staff, 2008, p. 1)

(a) a statement of financial position as at the end of the period;

(b) a statement of profit or loss and other comprehensive income for the period to be presented either as: (Ernst & Young, 2019, p. 116)

(i) one single statement of comprehensive income with a section for profit and loss followed immediately by a section for other comprehensive income; or

(ii) by presenting the profit or loss section in a separate statement of profit or loss, immediately followed by a statement presenting comprehensive income beginning with profit or loss. (Deloitte , 2021)

In this case, the former must be presented immediately before the latter;

(c) a statement of changes in equity for the period;

(d) a statement of cash flows for the period;

(e) notes, comprising a summary of significant accounting policies and other explanatory information; and

(f) a statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

An entity disclosing comparative information shall present, as a minimum, two statements of financial position, two of each of the other statements, and related notes. When an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements or when it reclassifies items in its financial statements, it shall present, as a minimum, three statements of financial position, two of each of the other statements, and related notes. (International Accounting Standards Board, 2008, p. 894)

IAS 1, Presentation of Financial Statements, is applicable to all general-purpose financial statements both to consolidated and separate financial statements, (Alibhai, et al., 2018, p. 46) that is suitable for profit-oriented entities, including public sector business entities (IFRS Foundation(IFRS F), 2013, p. 3). General purpose financial statements (referred to as 'financial statements') are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs. (Alibhai, et al., 2018, p. 47)

General purpose financial reports are prepared to provide resource providers with information to make their resource allocation decisions such as lending or investing. (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 816)

2.1. Elements of the Financial Statements

The elements directly related to financial position are assets, liabilities, and equity. These are defined as follows**.**

2.1.1. Elements of the Statement of Financial Position

Assets. Resources controlled by the entity as a result of past events, from which future economic benefits are expected (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 65). An economic resource is a right that has the potential to produce economic benefits. (Coby Harmon, 2013, p. 217)

The future economic benefit embodied in an asset is the potential to contribute, directly or indirectly, to the flow of cash and cash equivalents to the entity. The potential may be a productive one that is part of the operating activities of the entity. (Barry Elliott, Jamie Elliott, 2019, p. 418) It may also take the form of convertibility into cash or cash equivalents or a capability to reduce cash outflows, such as when an alternative manufacturing process lowers the costs of production. (IFRS Foundation(IFRS F), 2013, p. 15)

An asset is a resource: (Barry Elliott, Jamie Elliott, 2019, p. 24)

- controlled by the enterprise;
- as a result of past events;
- from which future economic benefits are expected to flow.

The future economic benefits embodied in an asset may flow to the entity in a number of ways. For example, an asset may be: (International Accounting Standards Board, 2008, pp. 83, 84)

(a) used singly or in combination with other assets in the production of goods or services to be sold by the entity;

(b) exchanged for other assets;

(c) used to settle a liability; or

(d) distributed to the owners of the entity.

Liabilities. Liabilities are defined by the IASB (Jerry J. Weygandt; Paul D. Kimmel; Donald E. Kieso, 2018, pp. 11-41) in the Conceptual Framework as ‘a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits. (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 816)

A liability is that the entity has a present obligation:

- An obligation is a duty or responsibility to act or perform in a certain way. Obligations may be legally enforceable as a consequence of a binding contract or statutory requirement. Obligations also arise, however, from normal business practice, custom and a desire to maintain good business relations or act in an equitable manner. (International Accounting Standards Board, 2008, p. 84)
- arising from past events; (Barry Elliott, Jamie Elliott, 2019, p. 24)
- the settlement of which is expected to result in an outflow of resources.

(Barry Elliott, Jamie Elliott, 2019, p. 24)

The settlement of a present obligation usually involves the entity giving up resources embodying economic benefits in order to satisfy the claim of the other party. Settlement of a present obligation may occur in a number of ways, for example, by: (International Accounting Standards Board, 2008, p. 85)

(a) payment of cash;

(b) transfer of other assets;

(c) provision of services;

(d) replacement of that obligation with another obligation; or

(e) conversion of the obligation to equity.

An obligation may also be extinguished by other means, such as a creditor waiving or forfeiting its rights.

Equity. The residual interest in the assets of the entity after deducting all its liabilities (Obert, 2003, p. 58).Equity is also called net assets or residual equity. (John J. Wild, Ken W. Shaw, Barbara Chiappetta, 2018, p. 12)

2.1.1. Elements of The income statement

The income statement (sometimes called the statement of profit and loss by firms applying IFRS), provides information on profitability. (Eddie McLaney ; Peter Atrill, 2016, p. 16)

The elements directly related to the measurement of performance in the income statement are income and expenses. (International Accounting Standards Board, 2008, p. 82)

The elements of income and expenses are defined as follows. (Coby Harmon, 2013, p. 137)

Income. Increases in economic benefits during the accounting period in the form of inflows or enhancements of assets that result in increases in equity, other than those relating to contributions from equity participants. (Alibhai, et al., 2018, p. 84) (Greuning, 2006, p. 5)

Expenses. Decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurring liabilities that result in decreases in equity, other than those relating to distributions to equity participants. (Alibhai, et al., 2018, p. 84)

2.2. Recognition and classification of financial elements

2.2.1. Recognition of financial elements

Recognition is the process of recording in the financial reports any item that meets the definition of an element and satisfies the criteria for recognition. If you look at a statement of profit or loss or statement of financial position you will see each item depicted both in words and with a monetary amount. (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 815)

A financial statement element (assets, liabilities, equity, income and expenses) should be recognised in the financial statements if: (Greuning, 2006, p. 5)

• It is probable that any future economic benefit associated with the item will flow to or from the entity; and

• The item has a cost or value that can be measured with reliability.

These are the basic criteria that are applied when recognizing assets, liabilities, revenues and expenses. (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 836)

Based on these general criteria:

Assets should be recognised when it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured with reliability. (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 16)

Assets that satisfy the recognition criteria should be incorporated in the statement of financial position when: (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 815)

(a) it is probable that the future economic benefits will flow to the entity

(b) the asset has a cost or value that can be measured with reliability.

A liability is recognised in the statement of financial position when it is probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably. (Barry Elliott, Jamie Elliott, 2019, p. 327)

Income should be recognised when an increase in future economic benefits related to an increase in an asset or a decrease of a liability has arisen that can be measured reliably. (Shirley CARLON, Rosina MCALPINE-ML ADENOVIC,Chrisann PALM, Lorena MITRIONE, Ngaire KIRK, Lily WONG, 2016, p. 821)

Expenses are recognised in the statement of comprehensive income when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably. (Barry Elliott, Jamie Elliott, 2019, p. 496)

2.2.2. Classification of the Financial Position Statement's elements

Statement of financial position —describes a company's financial position (types and amounts of assets, liabilities, and equity) at a point in time. (John J. Wild, Ken W. Shaw, Barbara Chiappetta, 2018, p. 18)

An entity shall present current and non-current assets, and current and non-current liabilities, as separate classifications on the face of its statement of financial position. When an entity supplies goods or services within a clearly identifiable operating cycle, separate classification of current and non-current assets and liabilities in the statement of financial position provides useful information by distinguishing the net assets that are continuously circulating as working capital from those used in the entity's long-term operations. It also highlights assets that are expected to be realised within the current operating cycle, and liabilities that are due for settlement within the same period. Except when a presentation based on liquidity provides information that is reliable and is more relevant. When that exception applies, all assets and liabilities shall be presented broadly in order of liquidity. (International Federation of Accountants (IFAC), 2020, p. 179)

The operating cycle of a business, mentioned above, is the time between buying and/ or creating a product or service and receiving the cash on its sale. (Peter Atrill, Eddie McLaney, 2017, p. 43)

The operating cycle is the average time between when a company acquires materials and supplies and when it receives cash for sales of the product (for which it acquired the materials and supplies). The cycle operates from cash through inventory, production, receivables, and back to cash. (Donald E. Kieso; Jerry J. Weygandt; Terry D. Warfield, 2014, p. 187)

The operating cycle is the time span over which a business pays cash to produce goods and services, which then are sold to bring cash back into the business. (C. William (Bill) Thomas, Wendy M. Tietz, Walter T. Harrison Jr., Charles T. Horngren, 2019, p. 148)

The operating cycle is the period of time required to convert cash into salable goods and services, sell those goods and services to customers, and receive cash from customers in payment. A firm's business model determines its operating cycle. The operating cycle can be as short as one to three months (Eddie McLaney ; Peter Atrill, 2016, p. 112)

For some entities, such as financial institutions, a presentation of assets and liabilities in increasing or decreasing order of liquidity provides information that is reliable and more relevant than a current/non-current presentation because the entity does not supply goods or services within a clearly identifiable operating cycle. An entity is permitted to present some of its assets and liabilities using a current/non-current classification and others in order of liquidity when this provides information that is reliable and more relevant. The need for a mixed basis of presentation might arise when an entity has diverse operations. (International Accounting Standards Board, 2008, p. 898)

2.2.2.1. Current/ non-current - assets

IAS 1 requires an asset to be classified as current when it satisfies any of the following criteria, with all other assets classified as non-current. The criteria are: (Ernst & Young, 2019, p. 122)

(a) it is expected to be realised in, or is intended for sale or consumption in, the entity's normal operating cycle (discussed above);

(b) it is held primarily for the purpose of trading;

(c) it is expected to be realised within twelve months after the end of the reporting period; or

(d) it is cash or a cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the end of the reporting period.

2.2.2.2. Current/ non-current - liabilities

IAS 1 requires a liability to be classified as current when it satisfies any of the following criteria, with all other liabilities classified as non-current. The criteria for classifying a liability as current are: (Ernst & Young, 2019, p. 122)

(a) it is expected to be settled in the entity's normal operating cycle (discussed above);

(b) it is held primarily for the purpose of trading;

(c) it is due to be settled within twelve months after the end of the reporting period; or

(d) the entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the end of the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

3. Impact of covid - 19 on the classification of current and non-current assets and liabilities under IASs

COVID-19 may result in changed expectations about when assets are expected to be realised, altering their classification as current/non-current.

Likewise, COVID-19 may result in changed expectations about when assets are expected to be realised, altering their classification as current/non-current. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 47)

Companies should consider the classification of assets and liabilities as current or non-current at the reporting date. For example, a loan for which provisions are breached at the reporting date, such that the liability becomes repayable on demand, would need to be classified as current, unless the company obtained a waiver before the reporting date. (Gabriela Kegalj, 2020, p. 4)

The implications of COVID-19 on the classification of assets and liabilities, but not limited to, may include:

3.1. Classification of financial liabilities

Entities need to consider whether the classification of loans and other financing liabilities between non-current and current has been affected. (Accountants, A. F. Ferguson & Co. Chartered, 2020, p. 12)

The conditions of the COVID-19 may lead to a breach of solvency or contractual ratios (covenants), which would involve reclassifying certain liabilities subject to early cancellation clauses as current liabilities. (Rödl & Partner, 2020, p. 4)

As a result of the COVID - 19, some entities might find themselves in breach of loan covenants and in some cases material adverse change clause might be triggered. This could result in loan repayment terms changing and some loans becoming repayable on demand. (Accountants, A. F. Ferguson & Co. Chartered, 2020, p. 12)

Unstable trading conditions and shortages of cash flows in the affected regions may increase the risk that entities breach financial covenants. Entities should consider how the breach of a loan covenant may affect the timing of repayment of the related loan and other liabilities (e.g. it becomes repayable on demand) and how it affects the classification of the related liabilities at the reporting date. (deloitte, 2020, p. 33)

Where debt covenants are at risk of being breached. In these circumstances financing terms may need to be renegotiated if the debt is to continue to be classified as non-current. If financial terms are not renegotiated before the year-end, it may lead to classification of the debt as current. If a waiver of a breach is received before the year-end, this could also affect classification. (The Australian Institute of Company Directors (AICD), Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia., 2020, p. 48)

If a breach occurs on, or before, the reporting date and the breach provides the lender with the right to demand repayment within 12 months of the reporting date, the liability should be classified as current in the entity's financial statements in the absence of any agreements made on or prior to the reporting date that give the entity a right to defer payment beyond 12 months after the reporting date. (deloitte, 2020, p. 33)

Disruptions in production and reduced sales can have implications on an entity's working capital and could lead to a breach of a debt covenant resulting in the liability becoming current. (deloitte, 2020, p. 14)

Entities may look for ways to manage this risk, including the use of alternative sources of funding, such as later payment to suppliers. When entities have previously determined that liabilities in these scenarios are presented as trade or other creditors rather than as borrowings, any increase in the repayment term will require a reassessment of the classification to ensure it remains appropriate. Disclosure of these facilities will be critical particularly when they are material to the entity's funding or viability. (deloitte, 2020, p. 14)

3.2. Classification of financial assets

An increase in frequency and value of sales may result in the need to consider whether there has been a change in the entity's business model or whether a new business model has been initiated. (deloitte, 2020, p. 15)

Under the current scenario. As part of their strategy to manage their credit and liquidity risks. Entities may decide to sell some of the securities because of the change in underlying credit risk on those securities. Such sale of financial assets does not affect the business model classification of the existing 'Held to Collect' securities. In accordance with IFRS 9, an increase in the frequency or value of sale of financial assets in a particular period is not necessarily inconsistent with an objective to hold financial assets in order to collect contractual cash flows, if an entity can explain the reasons for those sales and demonstrate why those sale of financial assets do not reflect a change in entity's business model. IFRS 9 gives an example that when an entity expects that it will sell a particular portfolio of financial assets only in a stress case scenario, that scenario would not affect entity's assessment of the business model for those assets if entity reasonably expects that such a scenario will not occur. (Accountants, A. F. Ferguson & Co. Chartered, 2020, p. 3)

Some entities that have assets that are held under a "held to collect and sell" or "held to sell" business model may find that previously anticipated sales are no longer expected to take place due to a reduction in asset values or in the liquidity of the relevant market. IFRS 9 states that neither a change in intention related to a particular asset (even in circumstances of significant changes in market conditions), nor a temporary disappearance of a particular market represent a change in an entity's business model. (deloitte, 2020, p. 15)

Reclassifications triggered by a change in business model are expected to be highly infrequent and to incur only when the activity is significant to the entity's operations; they are applied prospectively from the reclassification date. (deloitte, 2020, p. 15)

Entities may also need to reconsider the existing classification of certain investments as cash equivalents under IAS 7 Statement of Cash Flows. To be classified as a cash equivalent, an investment, for example in a money market fund, must be held for the purpose of meeting short-term cash commitments and must be readily convertible to known amounts of cash and subject to insignificant changes in value. Current economic conditions are likely to increase the volatility in prices of many investments and reduce their liquidity. (deloitte, 2020, p. 14)

Cash and cash equivalents IAS 7 defines cash equivalents as short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Entities may need to consider whether investments classified as cash equivalents continue to meet the requirement for such a classification. If this is not the case, a change in classification of the investments may be required. (deloitte, 2020, p. 36)

For example, entities should consider whether investments in funds, such as money market funds, have experienced a more than insignificant decrease in value. Also, clauses in the fund's documents may grant the fund manager the ability to restrict redemption in exceptional circumstances that may apply to the COVID-19 pandemic. When considering the impact of restrictions that may limit an investor's ability to redeem the units in the fund, consideration should be given as to whether those conditions exist at the reporting date, or are expected to exist in the short term following the reporting date, and therefore will limit the investor's ability to readily convert its units into a known amount of cash. (deloitte, 2020, p. 36)

A change in classification as the result of a change in facts and circumstances is applied prospectively (i.e. the comparative period is not restated). (deloitte, 2020, p. 36)

3.3. Consolidation

3.3.1 Reporting time lags

When a subsidiary prepares financial statements for a different reporting period, it is also necessary to review the subsidiary's statement of financial position to ensure that items are still correctly classified as current or non-current at the end of the group's reporting period. For example a breach in covenant that is determined to be a non-adjusting event in the financial statements of a subsidiary may require reclassification of the affected liabilities in the consolidated financial statements if these are prepared at a date after the date of the breach in covenant and if the lender has not waived its right to demand repayment for a period of at least 12 months from the date of the consolidated financial statements. (deloitte, 2020, p. 26)

3.3.2 Long-term intra-group foreign investments

Paragraph 32 of IAS 21 The Effects of Changes in Foreign Exchange Rates provides an exception that allows gains and losses on certain intragroup foreign currency items of a long-term investment nature to be recognised in other comprehensive income instead of being recognised in profit or loss. For an item to qualify as a long-term investment, the entity must be able to assert that "settlement is neither planned nor likely to occur in the foreseeable future". An entity that has characterised an intra-group item as part of its net investment in the entity may need to reassess whether that designation is still appropriate in the current economic environment. For example, an entity that plans to undergo restructuring because of the COVID-19 pandemic may need to reassess whether certain intercompany loans that had previously been determined to be of a "long-term investment nature" should continue to be accounted for as such if the loans could now be settled in the "foreseeable future" in connection with the restructuring plan. (deloitte, 2020, p. 30)

3.4. Disclosure requirements

Companies need to disclose any loan default or breach of a loan agreement that has not been remedied on or before the reporting date. (Gabriela Kegalj, 2020, p. 4)

Entities should consider how the use of working capital enhancement or management techniques is reflected in the entity's disclosure of its liquidity risk management as required by IFRS 7 Financial Instruments: Disclosures. Entities should consider providing sufficiently detailed quantitative and qualitative disclosures about: (deloitte, 2020, p. 14)

- their access to cash and sources of finance;
- any changes or likely changes to the existing financing arrangements;
- any new arrangements entered into;

• credit gradings and any changes which impact cost or access to funding (e.g. if the grading falls below investment grade); and

• any developments subsequent to the reporting date.

•If relevant, entities should explain the impact of government assistance programmes as part of their liquidity risk management. For example, disclosures may include how much funding is available, the likelihood that the funding will be utilised and the time horizon over which the funds are available. (deloitte, 2020, p. 15)

When the entity changes the presentation or classification of items in its financial statements, the entity shall reclassify comparative amounts unless reclassification is impracticable. When the entity reclassifies comparative amounts, the entity shall disclose: (International Accounting Standards Board, 2008, p. 894)

(a) the nature of the reclassification;

(b) the amount of each item or class of items that is reclassified; and

(c) the reason for the reclassification.

When it is impracticable to reclassify comparative amounts, an entity shall disclose:

(a) the reason for not reclassifying the amounts, and

(b) the nature of the adjustments that would have been made if the amounts had been reclassified.

4. CONCLUSION

Users of financial statements look closely at the relationship between current assets and current liabilities. This relationship is important in evaluating a company’s liquidity—its ability to pay obligations expected to be due within the next year. When current assets exceed current liabilities, the likelihood for paying the liabilities is favorable. When the reverse is true, short-term creditors may not be paid, and the company may ultimately be forced into bankruptcy.

As the spread of the pandemic increases, entities are experiencing conditions often associated with a general economic downturn, including, but not limited to, financial market volatility and erosion of market value, deteriorating credit, liquidity concerns, further increases in government intervention, increasing unemployment, broad declines in consumer discretionary spending, increasing inventory levels, reductions in production because of decreased demand and supply constraints, layoffs and furloughs, and other restructuring activities, business continuity issues, etc. The continuation of these circumstances could have a prolonged negative impact on an entity's financial condition and results.

We believe that the following accounting and reporting issues will be the most pervasive and challenging for economic entities as a result of the pandemic's impact. This may also have accounting classification implications for many entities. Therefore, institutions must carefully consider the impact of the aforementioned factors on the possibility of making adjustments to the classification of some elements in the financial statements to reflect honestly and fairly the unique circumstances surrounding the institution in light of the pandemic outbreak.

Ultimately, we can extract these outcomes:

- In the current environment, the quality of financial reports and related disclosures is more important than ever for confident and informed markets and investors;
- Entities with businesses adversely affected by the COVID-19 pandemic should focus on reporting of asset values and financial position;
- Investors expect clear disclosure about the impacts on an entity's businesses, any risks and uncertainties, key assumptions, management strategies and future prospects;
- We realise that entities may face uncertainties about future economic and market conditions, and the future impact on their businesses. Accordingly, directors, management and auditors may need to make difficult judgements on asset values and financial condition;
- Consider which impacts need addressing and whether and how these should be recognised, measured and disclosed, in either the financial report or elsewhere in the annual report. Doing this effectively will be critical to ensuring that the financial report clearly communicates the entity's financial performance and position when reporting during periods impacted by COVID-19;
- It is possible that the financial report will be subject to a greater degree of

change than in previous years as new accounting policies may need to be introduced and existing accounting policies reviewed, estimates and uncertainties identified and determined, new disclosures developed and considerations about going concern addressed;

- IFRS requires companies to classify their assets and liabilities as either current or non-current, unless presenting their balance sheet on a liquidity basis makes the balance sheet more relevant. (Banks and other financial institutions do this, starting with their most liquid asset (cash) and liabilitiy, as the current and non-current classification isn't a meaningful classification for their business*)*;
- The operating cycle of an entity is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. As a result of the implications of Covid-19, the entities may be facing a difficult to define the operating cycle accurately. The IAS1 states that when the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months;
- Concentration risk may be particularly significant to some entities when customers are concentrated in an adversely affected industry such as the hospitality and tourism and airline industries. Such entities will need to give clear disclosure of the potential impact on liquidity if significant;
- It is important to highlight that many entities may seek rescheduling / restructuring of their financial obligations. Such rescheduling and restructurings might include requests to the lenders to give relaxation in respect of certain loan covenants. Such relaxations for loan covenants should be obtained by entities before the reporting date to continue the existing loan classification between the non-current and current.

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