

# CORONAVIRUS

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## SEC Issues New Guidance on COVID-19 Considerations for Financial Reporting and Form 10-Q Disclosures & Highlights Vital Role of Audit Committees

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On June 23, 2020, the Division of Corporation Finance of the Securities and Exchange Commission (“SEC”) issued [CF Disclosure Guidance: Topic No. 9A, Coronavirus \(“COVID-19”\)—Disclosure Considerations Regarding Operations, Liquidity, and Capital Resources](#), which provides new guidance regarding “disclosures companies should consider with respect to business and market disruptions related to COVID-19;” and SEC Chief Accountant, Sagar Teotia, issued a [Statement on the Continued Importance of High-Quality Financial Reporting for Investors in Light of COVID-19](#).

Both the Division of Corporation Finance (“Division”) disclosure guidance and the Office of the Chief Accountant (“OCA”) statement issued on June 23rd provide additional guidance to public companies as they begin preparing their second quarter financial reports (in the case of calendar year end companies). This new guidance builds on and amplifies disclosure and financial reporting themes related to COVID-19 included in the Division’s initial [March 25th guidance](#) and the OCA’s [April 3rd statement](#) issued in connection with the companies’ preparation of their first quarter financial reports (in the case of calendar year end companies).

The Division made it clear in its June 23rd guidance that it continues to: (i) “monitor how companies are disclosing the effects and risks of COVID-19 on their businesses, financial condition, and results of operations;” and (ii) encourage companies to provide disclosures that would enable investors to “understand how management and the Board of Directors are analyzing the current and expected impact of COVID-19 on the company’s operations and financial condition, including liquidity and capital resources.”

The Division acknowledged that companies are making disclosures regarding their operational adjustments and financing activities related to COVID-19 in their earnings releases, however, the Division encouraged companies to evaluate whether any of such disclosures should also be included in their Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) in light of their potential materiality for investors’ decision-making process. To assist with such evaluation, the Division included sample questions for companies to consider (see questions listed below).

In addition, the Division highlighted the fact that companies receiving financial assistance under the Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”) “should consider the short- and long-term impact of that assistance on their financial condition, results of operations, liquidity, and capital resources, as well as the related disclosures and critical accounting estimates and assumptions.” The Division also reminded companies that if conditions or events raise “substantial doubt about a company’s ability to continue as a going concern, or the substantial doubt is alleviated by management’s plans,” companies should provide appropriate disclosures in their financial statements and MD&A. To assist companies in considering their disclosure obligations related to the financial assistance that they receive and their ability to continue as a going concern, the Division included sample questions for companies to review (see questions listed below). Finally, the Division reminded companies to consider whether COVID-19 materially impacts other disclosure items, such as the effectiveness of disclosure controls and procedures and changes to internal control over financial reporting.

The OCA’s statement states that, as companies begin preparing for their second quarter reporting period, it expects the financial reporting system to continue to provide a “steady flow of timely, decision-useful information to investors and ... public capital markets” during the pandemic. The OCA’s statement reminds companies of their disclosure obligations related to significant estimates and judgements, the importance of disclosure controls and procedures and internal control over financial reporting and related disclosures, and going concern disclosures. In addition, the OCA pointed out that they are available for consultation with companies related to any questions that arise in preparing their second quarter financial reports due to COVID-19 or other emerging issues. The OCA also emphasized that in “these times of rapid change and increased uncertainty, the need for the oversight role that audit committees play is as critical as ever” and that it expects audit committees to be fully engaged and to execute their responsibilities with diligence, which “significantly enhances the financial reporting output.”

### **Questions for Companies to Consider from** [CF Disclosure Guidance: Topic No. 9A](#)

#### *General Disclosure Obligations*

- What are the material operational challenges that management and the Board of Directors are monitoring and evaluating? How and to what extent have you altered your operations, such as implementing health and safety policies for employees, contractors, and customers, to deal with these challenges, including challenges related to employees returning to the workplace? How are the changes impacting or reasonably likely to impact your financial condition and short- and long-term liquidity?
- How is your overall liquidity position and outlook evolving? To the extent COVID-19 is adversely impacting your revenues, consider whether such impacts are material to your sources and uses of funds, as well as the materiality of any assumptions you make about the magnitude and duration of COVID-19’s impact on your revenues. Are any decreases in cash flow from operations having a material impact on your liquidity position and outlook?
- Have you accessed revolving lines of credit or raised capital in the public or private markets to address your liquidity needs? Are your disclosures regarding these actions and any unused liquidity sources providing investors with a complete discussion of your financial condition and liquidity?
- Have COVID-19 related impacts affected your ability to access your traditional funding sources on the same or reasonably similar terms as were available to you in recent periods? Have you provided additional collateral, guarantees, or equity to obtain funding? Have there been material changes in your cost of capital? How has a change, or a potential change, to your credit rating impacted your ability to access funding? Do your financing arrangements contain terms that limit your ability to obtain additional funding? If so, is the uncertainty of additional funding reasonably likely to result in your liquidity decreasing in a way that would result in you being unable to maintain current operations?

- Are you at material risk of not meeting covenants in your credit and other agreements?
- If you include metrics, such as cash burn rate or daily cash use, in your disclosures, are you providing a clear definition of the metric and explaining how management uses the metric in managing or monitoring liquidity? Are there estimates or assumptions underlying such metrics the disclosure of which is necessary for the metric not to be misleading?
- Have you reduced your capital expenditures, and, if so, how? Have you reduced or suspended share repurchase programs or dividend payments? Have you ceased any material business operations or disposed of a material asset or line of business? Have you materially reduced or increased your human capital resource expenditures? Are any of these measures temporary in nature, and, if so, how long do you expect to maintain them? What factors will you consider in deciding to extend or curtail these measures? What is the short- and long-term impact of these reductions on your ability to generate revenues and meet existing and future financial obligations?
- Are you able to timely service your debt and other obligations? Have you taken advantage of available payment deferrals, forbearance periods, or other concessions? What are those concessions and how long will they last? Do you foresee any liquidity challenges once those accommodations end?
- Have you altered terms with your customers, such as extended payment terms or refund periods, and, if so, how have those actions materially affected your financial condition or liquidity? Did you provide concessions or modify terms of arrangements as a landlord or lender that will have a material impact? Have you modified other contractual arrangements in response to COVID-19 in such a way that the revised terms may materially impact your financial condition, liquidity, and capital resources?
- Are you relying on supplier finance programs, otherwise referred to as supply chain financing, structured trade payables, reverse factoring, or vendor financing, to manage your cash flow? Have these arrangements had a material impact on your balance sheet, statement of cash flows, or short- and

long-term liquidity, and, if so, how? What are the material terms of the arrangements? Did you or any of your subsidiaries provide guarantees related to these programs? Do you face a material risk if a party to the arrangement terminates it? What amounts payable at the end of the period relate to these arrangements, and what portion of these amounts has an intermediary already settled for you?

- Have you assessed the impact material events that occurred after the end of the reporting period, but before the financial statements were issued, have had or are reasonably likely to have on your liquidity and capital resources and considered whether disclosure of subsequent events in the financial statements and known trends or uncertainties in MD&A is required?

#### *CARES Act*

- How does a loan impact your financial condition, liquidity, and capital resources? What are the material terms and conditions of any assistance you received, and do you anticipate being able to comply with them? Do those terms and conditions limit your ability to seek other sources of financing or affect your cost of capital? Do you reasonably expect restrictions, such as maintaining certain employment levels, to have a material impact on your revenues or income from continuing operations or to cause a material change in the relationship between costs and revenues? Once any such restrictions lapse, do you expect to change your operations in a material way?
- Are you taking advantage of any recent tax relief, and, if so, how does that relief impact your short- and long-term liquidity? Do you expect a material tax refund for prior periods?
- Does the assistance involve new material accounting estimates or judgments that should be disclosed or materially change a prior critical accounting estimate? What accounting estimates were made, such as the probability a loan will be forgiven, and what uncertainties are involved in applying the related accounting guidance?

## *Going Concern*

- Are there conditions and events that give rise to the substantial doubt about the company's ability to continue as a going concern? For example, have you defaulted on outstanding obligations? Have you faced labor challenges or a work stoppage?
- What are your plans to address these challenges? Have you implemented any portion of those plans?

## **For additional information, please contact:**

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