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March 13, 2020

Coronavirus: Governance, Operational, Financial Reporting, and Tax Considerations

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The number of countries reporting infections and the number of individuals infected with novel coronavirus 2019 (COVID-19) continues to increase. On March 11, 2020, the World Health Organization (WHO) declared the disease a pandemic, with cases reported on all continents except Antarctica and coronavirus deaths continuing to rise. On March 13, President Trump declared a national emergency.

The coronavirus pandemic is dynamic and wide-ranging with known and potentially unknown impacts. Travel restrictions for countries (for example, European countries, China, South Korea) have the potential to cause significant disruption to business operations. Public health agencies have issued myriad intervention recommendations to prevent spread of the coronavirus, and many sporting events, concerts, conferences, and other large gatherings have been canceled or postponed. Many schools have been closed, with some plans to transition to distance learning. Museums, theme parks, and theaters have followed suit, and some business entities have encouraged teleworking.

On March 11, 2020, President Trump addressed the nation from the Oval Office to announce a restriction on travel from impacted areas and an economic assistance package that includes loans, tax relief, and compensation for certain coronavirus-impacted individuals or businesses.

Some public companies have warned investors about the direct and indirect (for example, supply chain disruptions, employee availability, decreased sales volumes, or credit quality of customers) economic impacts of the coronavirus. On March 12, the G-20[1] discussed how the pandemic calls for a robust international response and agreed to "enhance cooperation and coordination to control the outbreak, protect people, mitigate the economic impact, and maintain economic stability, while avoiding stigmatization." G20 finance ministers and Central Bank governors issued a statement on March 6 agreeing to use all available policy tools, including appreciate fiscal and monetary measures. Stock markets around the world are reacting to coronavirus uncertainties.

Governance and operational considerations

The direct and indirect impacts of a pandemic can be significant depending on an entity's facts and circumstances. Domestic and international governments have already taken steps to slow the spread of the virus. These steps are disrupting global supply chains and the demand for goods and services in affected economies, in addition to a multitude of other potential impacts.

In times of crisis, it can be easy for management to make choices based upon emotions. However, those charged with governance can be instrumental in making sure that company leaders are taking appropriate, measured responses with targeted, identified objectives based upon the best information available.

Company leaders and those charged with governance should focus on providing a clean, safe, and welcoming environment for their customers and employees that best complies with any federal, state, or local agency intervention guidance to minimize the risk of exposure. Companies with international operations are encouraged to closely monitor the ongoing developments in the countries where the entity has business interests (for example, the location of the entity, its suppliers, or its customers).

Those charged with governance should understand management's process to evaluate the impacts of the pandemic on the company's operations, including any associated risks, which might require a variety of responses including, but not limited to:

People and workforce impacts:

- Evaluating policies on internal (for example, workforce and board) communication, travel restrictions, event attendance, plant or location closing, and self-quarantining of individuals
- Establishing a formal crisis response plan with defined roles and responsibilities for the board and management
- Assessing the ability of quickly enabling a remote workforce, determining laptop and internet availability, and stress-testing VPN access
- Transitioning to video-based conferencing and work-from-home (WFH) strategies
- Understanding the impact of WFH strategies on families, including children at home due to school or child care facility closure
- Testing and enacting business continuity and mass absenteeism plans, including on-site vs. WFH rotations
- Determining employee compensation requirements, including the potential impact on paid time off and/or compensation if an employee is unable to work remotely when locations are closed or operations are limited

Non-workforce operational impacts:

- Assessing current impacts on the company's operational, financial, and strategic plans
- Establishing external communication policies, including any necessary restrictions related to securities transactions.
- Considering changes to physical location access procedures and controls
- Evaluating policies and procedures to supplement normal cleaning procedures
- Deferring or canceling large scale events and gatherings
- Evaluating the impacts of any applicable travel or cargo restrictions
- Performing targeted reviews of exposure to industries and parties affected by the pandemic (for example, customers, supply chain, vendor management, credit)
- Assessing current state of supply chains to better understand where potential breakdowns might affect the ability to meet customer demands (such as limited transportation, sub-supplier failures, and tooling needs)
- Considering the impacts of tax policy announcements

Financial reporting considerations

SEC reporting considerations

On Feb. 19, 2020, the SEC and PCAOB issued a joint statement covering, among other items, the effects of the coronavirus on financial reporting, including an issuer's disclosures and the audit firm's audit quality (for example, audit firm access to information and company personnel). The joint statement acknowledges that the coronavirus is dynamic and the effects on any particular industry or issuer might not be known. However, users might need disclosure of how issuers plan for and respond to coronavirus events.

The joint statement reminds companies to work with their audit committees and auditors to "ensure that their financial reporting, auditing and review processes are as robust as practicable in light of the circumstances in meeting the applicable requirements."

An issuer should carefully consider whether the following items in filings should discuss the current or potential future impact of the coronavirus:

- Risk factors
- Description of business
- Management's discussion and analysis (including the requirements of Item 303 of Regulation S-K to discuss known trends and uncertainties on liquidity, capital resources, and results of operations
- Quantitative and qualitative disclosures about market risk
- Board risk oversight disclosures pursuant to Item 407(h) of Regulation S-K and Item 7 of Schedule 14A

An issuer with significant operations in areas disrupted by the coronavirus might face difficulties obtaining the appropriate information to prepare its financial statements or financial statements of other entities (for example, under Rule 3-05 or Rule 3-09 of Regulation S-X). On March 4, 2020, the SEC issued an order that provides conditional regulatory relief of an additional 45 days to file certain reports for companies affected by the coronavirus. This order affects reports that would have been due between March 1, 2020, and Apr. 30, 2020, if certain criteria are met.

To avail itself of the relief, a domestic entity must file a Form 8-K (or Form 6-K for foreign private issuers) that discusses 1) why circumstances relating to COVID-19 have resulted in the issuer being unable to file on a timely basis; 2) the date the entity estimates they will make the filing; and 3) if material and appropriate, risk factors describing the impact of COVID-19 on the issuer's business.

In a statement issued concurrent with the order, the SEC reminded issuers of their disclosure obligations under federal securities laws, including impacts on securities transactions. The statement asserts that where an entity has "become aware of a risk related to the coronavirus that would be material to its investors, it should refrain from engaging in securities transactions with the public and…take steps to prevent directors and officers (and other corporate insiders who are aware of these matters) from initiating such transactions until investors have been appropriately informed about the risk."

Accounting and internal control considerations

The SEC and PCAOB joint statement reminds issuers of their responsibility to assess subsequent events for disclosure. Under ASC 855, subsequent events can be recognized or unrecognized, depending on whether the event provides additional evidence about conditions that existed on the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Accounting implications of the coronavirus could include, but are not limited to, disclosure of the potential for or recognition of impacts in the following areas:

- Impairment of inventory, goodwill, intangibles, or long-lived assets (Accounting Standards Codification (ASC) 330, 350, and 360)
- Idle or vacant facilities (ASC 330 and 360)
- Collectability of loans, securities, or trade receivables (ASC 310 or 326 as applicable), including financial institutions with loans to customers with significant direct or indirect exposure to entities with operations in areas affected by the coronavirus or general market disruptions (for example, commodity prices)
- Sales of HTM securities (ASC 320)
- Income tax valuation allowances (ASC 740)
- Loss contingencies (ASC 450), for example, legal matters or other contingency accruals
- Changes in fair value (ASC 820) of items carried at fair value on the balance sheet
- Insurance recoveries, for example business interruption
- Going concern (ASC 205-40)
- Derivative or hedging issues (ASC 815), for example, probability of forecasted transactions in a cash flow hedge or volumes under contracts qualifying for the normal purchase normal sale scope exception
- Debt classification, including covenant violations (ASC 470) such as the triggering of material adverse change (MAC) provisions
- Employee benefits, including compensated absences (ASC 710), termination benefits (ASC 712), and share-based payment arrangements (ASC 718)
- Risk and uncertainty disclosures (ASC 275), for example supply chain disruptions
- Potential need to post or request additional collateral under certain contracts

Companies might need to consider how the risk of the coronavirus affects internal control over financial reporting (ICFR). For example, a company might be required to change or implement new internal controls to account for the noted issues. Other ICFR considerations include potential IT control changes to allow for modified employee access to systems, new controls for entering into new or modified business contracts, or controls required for new financial reporting processes due to the coronavirus.

Any changes to ICFR might trigger a disclosure under Item 308(c) of Regulation S-K, which requires public companies to disclose any change in ICFR that occurred during the registrant's last fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's ICFR.

Tax considerations

On March 11, the president announced that he is asking the U.S. Department of the Treasury to defer tax payments without interest and penalties for certain coronavirus affected individuals and businesses. The president also asked Congress to provide payroll tax cuts, but at this time there is no clear outcome, as Congress appears to be in the process of debating this and other responses to the pandemic.

Earlier in the day, the media reported plans to delay the April 15 tax deadline for most individual taxpayers as well as small businesses as a part of the effort to address the complications caused by the spread of the coronavirus. Until the IRS issues guidance, it is not clear who will be entitled to payment deferral, how long the deferral will be, and what other relief will be provided.

On March 11, the AICPA issued a press release requesting the following:

For individuals:

- Maintain the April 15, 2020, deadline
- Provide an automatic extension to Oct. 15, 2020 without a requirement to file any forms or show reasonable cause
- Waive late payment penalties if tax is paid in 70% (lowered from 90%)
- Waive any interest penalty if paid in full by Oct. 15, 2020
- Grant additional time to file through Oct. 15, 2020, including relief for IRA contributions, for certain deadlines falling on or after March 15, 2020, and before Oct. 15, 2020
- Waive penalties associated with 2020 estimated tax payments for the first through third quarter 2020 if paid by Sept. 15, 2020

For businesses:

- Grant additional time to file through Oct. 15, 2020 for certain deadlines falling on or after March 15, 2020, and before Oct. 15, 2020
- Waive late payment penalties and interest through Oct. 15, 2020
- Provide an automatic extension without the need to file any forms or request an extension
- Provide appropriate relief for all businesses and tax-exempt organizations for filings such as payroll and excise tax

Prior to the president's announcement, the IRS issued relief on March 11 to allow high deductible medical insurance plans to cover testing and treatment of COVID-19 prior to satisfying the plan's deductible. We anticipate that the IRS might provide other employer and worker-related tax relief. This relief could include easing rules to allow early distributions from retirement plans and IRAs to help affected workers or delaying due dates for retirement plan contributions and rollovers. Other relief could also include an expanded paid leave credit for lower-income employees.

Companies with international business have additional considerations. These companies could face difficulties obtaining information from foreign affiliates that is necessary for meeting U.S. tax filing and reporting obligations. In addition, U.S. expatriates sent home early from foreign assignments might need relief to be able to claim the tax exemption for foreign earned income and housing for which they otherwise would have been eligible.

Even after the IRS provides initial relief, taxpayers likely will need additional guidance to deal with the tax consequences of canceled events, lost business, and interrupted supply chains. While business-related losses may be deductible, *Tax Cuts and Jobs Act of 2017* (TCJA) eliminated the ability to carry losses back to offset prior year income. Companies should consider alternatives such as adjusting current year estimated tax payments or applying for a quick refund of prior year estimated tax if there will now be excess overpayments going into 2020.

It is unclear whether states will provide relief for the coronavirus, and if so, what that relief would be. Interest-free deferral of tax payments might not be feasible for many state budgets, but other relief, such as extended filing due dates, might be available. For instance, Washington state has provided coronavirus-related relief for taxpayers, offering filing extensions and late payment penalty waivers upon request. Maryland has delayed filing and payment of certain business taxes without interest or penalties and has indicated it would follow the IRS's lead on whether to extend the April 15 filing due date for individuals.

Internationally, many jurisdictions already have taken steps to respond to the implications of the pandemic locally. Taxpayers are encouraged to monitor applicable jurisdictional coronavirus developments and related tax policy, tax reporting, or tax payments announcements.

Concluding thoughts

There is no doubt we are experiencing uncertainty from many facets. We are watching closely and will share developments from regulators and observations on financial reporting, tax issues and operations.

Learn more

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[1] The G-20 is an international forum of representatives from 19 countries and the European Union (EU). Its objective is to discuss policy pertaining to the promotion of international financial stability and address issues that go beyond the responsibilities of any one organization.

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