Going Concern

Management, when preparing financial statements, has to make an assessment of an entity's ability to continue as a going concern and whether the going concern assumption is appropriate. In assessing whether the going concern assumption is appropriate, the standard requires that all available information about the future, which is at least, but not limited to, 12 months from the end of the reporting period, should be taken into account.

Management takes into consideration the existing and anticipated effects of the outbreak on the entity's activities along with the following factors:

- operations have been suspended before or after the reporting date
- current adverse situation including, expected impact on liquidity and profitability
- Available information about the future which was obtained after the reporting date including measures taken by Governments and banks to provide relief to affected entities in their assessment of going concern.

Check List

(a) Whether the entity has prepared future cash flow statement based on revised future estimates for the next year?
(b) Whether future revised estimates are based on conclusive evidence and documentation?
(c) If the entity prepares the financial statements under the going-concern assumption, whether it has disclosed all material uncertainties in the financial statements in order to make clear that the going-concern assumption used by management is subject to such material uncertainties

Revenue Recognition

The coronavirus outbreak could affect revenue estimates in ongoing customer contracts, including future revenue contracts, in many areas like variable considerations (e.g., schemes and discounts, refunds/returns, price concessions, performance bonuses and penalties), collectability and stand-alone selling prices. The entity may need to update its estimates of variable consideration (including any amounts that are constrained) to reflect an entity's revised expectations about the amount of consideration to which it expects to be entitled, considering uncertainties related to the COVID-19 outbreak.

Check List

(a) Whether there is any change in the estimates of schemes and discounts (including price concession, performance incentives, volume discounts etc.) to be given to customers?
(b) Whether there is a change in the expectations of higher stock return? The entity has to change the basis of provisioning considering effect of COVID-19.
(c) Whether the entity has assessed its customers' ability to pay which require either to defer revenue or additional provisioning?
(d) Whether the entity has followed cut-off procedure to recognise revenue? E.g. Exports are based on shipment or Domestic Sales are based on INCO terms like FOR, FOB, CIF
(e) When the goods are in transit, the entity has to demonstrate at what point the control of goods has been transferred to the customer to recognise revenue.
(f) When the goods are ready for dispatch but could not be dispatched to customers due to lockdown, can the entity recognize the revenue based on bill-and-hold guidance of Ind AS 115?
(g) Whether there is any change in the scheme of loyalty points and its redemption period which affects deferment of revenue?

Financial Instruments

The occurrence of large-scale business disruptions that potentially give rise to liquidity issues for certain entities might also have consequential impacts on the credit quality of entities along the supply chain. The deterioration in credit quality of loan portfolios, such as that of trade receivables, as a result of the outbreak will have a significant impact on the expected credit loss (ECL) measurement. In responding to these challenges, Governments or regulatory bodies have announced relief measures for extension of payment terms or have asked lenders to allow such relief measures. Further, in many cases, borrowers have approached lenders for renegotiation of terms.

Check List

(a) Whether to calibrate the matrix, the entity has adjusted its historical credit loss experience with forward-looking information, including impacts of the coronavirus outbreak. (The entity should also consider grouping trade receivables based on the industry or geographical location).

(b) Whether the entity has considered the following in computation of ECL variables?

- Probability of default: probability of default might increase due to adverse impact of the outbreak on businesses/ employment of borrowers.
- Exposure at default: some of the borrowers may be having unused borrowing facilities and might draw down on those facilities due to liquidity issues or might cease making discretionary over payments. These are expected to result in an increase in exposure at default.
- Loss given default: loss given default might increase as there might be change in credit standing of the financial guarantors or in the fair value of assets pledged as collateral due to market volatility.

Best efforts should be made to consider all reasonable and supportable information available

(c) Due to increase in credit risks, whether the entity has analysed some of the financial assets which were not posing significant challenges (e.g., security deposits given).

(d) The outbreak is likely to have an impact on the liquidity position of the group entity and accordingly, it may not be in a position to repay the loan if demanded on the reporting date. In such case, whether the entity has considered the ECL assessment in respect of the expected manner of recovery and recovery period of the intragroup loan? (As the entity is expecting to fully recover the loan, the ECL will be limited to the effect of discounting the amount due on the loan at the loan's effective interest rate over the period until the loan is recovered. Even if full recovery is expected but delayed, ECL measurement should take into account the time value of money.

(e) Whether the entity has applied for and availed moratorium from payment of interest and principal for any period? [Payment moratorium results in changes in contractual cash flows (timing and amount (additional interest component) of cash flows) of the financial liability and accordingly will be considered as modification of the contractual terms].

(f) Whether the modification to contractual terms is substantial? If yes, whether modification is recorded as extinguishment of financial liability. (The carrying value of financial liability should be derecognized and new financial liability should be recognized at its fair value. Any difference between the carrying value and new financial liability will be recognized in profit and loss. Costs and fees incurred on such modification will also be recognized in profit and loss).

(g) If the modification is not substantial, whether the entity has recalculated the gross carrying amount of the financial liability and recognize a modification gain/loss in profit or loss statement? (The gross carrying amount of the financial liability is recalculated as the present value of the modified contractual cash flows that are discounted at the financial liability's original effective interest rate).

(h) Whether any renegotiation, rollover or rescheduling of cash flows occurred? If yes, refer point (f) and (g) above.

(i) Significant volatility in markets, due to the outbreak, might represent risk assumptions that market participants are making under current conditions. Ind AS 113 specifies that in case of availability of level 1 inputs, the same should be used for fair value measurement. It would not be appropriate to adjust or disregard observable transactions unless those transactions are determined to not be orderly. Whether the fair value of an investment in an active market would continue to be calculated based on quoted prices, even in times of significant market volatility?

(j) Due to the coronavirus outbreak, the entity will need to consider whether the transaction is still a highly probable forecasted transaction? This includes whether the volume or amounts involved will be lower than forecasted or whether it is now no longer probable that the forecasted transaction will occur. Depending on conclusions reached, accounting will be as follows:
   - If forecasted transaction is no longer highly probable, but is still expected to occur, the entity must discontinue hedge accounting prospectively. In this case, the accumulated gain or loss on the hedging instrument that has been recognized in other comprehensive income will remain recognized separately in equity until the forecasted transaction occurs.
   - If forecasted transaction is no longer expected to occur, the entity must discontinue hedge accounting prospectively. Further, it should immediately reclassify any accumulated gain or loss on the hedging instrument that has been recognized in other comprehensive income to profit or loss.
   - If forecasted transaction is expected to be delayed, change in timing of forecasted transaction is a source of hedge ineffectiveness. If the entity decides to retain the derivative and continue to apply the hedge accounting, it should test the effectiveness of the hedge. Ineffective portion of the hedge will be recognized in profit and loss. Amount recognized in OCI will be reclassified to profit and loss when forecasted transaction occurs.
   - Where forecast transaction is no longer expected to occur, amount reclassified to profit or loss may be presented under other expenses or other income and should not be grouped with revenue or purchases.

(k) Is there any non-compliance of debt covenants of a long-term loan resulting from the coronavirus outbreak and whether the same has become repayable on demand? The classification of such borrowing in its financial statement is based on the following:
   - **Breach of minor provision**
     Guidance note on Division II – Ind AS Schedule III to the Companies Act, 2013 issued by the Institute of Chartered Accountants of India ("ICAI") provides that in case of minor breach of debt covenants, loan may continue to be classified as non-current unless lenders have recalled the loan before the date of approval of the financial statements on breach of a loan covenant that occurred before the year-end.
   - **Breach of major provision**
     Ind AS 1 requires classifying long-term loan as current where there is a breach of material provision which makes it payable on demand as on reporting date. However, it should be classified as non-current if the lender agreed not to demand payment, after the reporting period but before the approval of the financial statements for issue. Accordingly, classification would depend whether or not an entity is able to obtain waiver from the lender before approval of financial statements.

Impairment of Non-Financial Assets

An asset is impaired when an entity is not able to recover its carrying value, either by using it or selling it. An entity estimates the recoverable amount of the asset for impairment testing. Recoverable amount is the higher of the fair value less costs of disposal (FVLCD) and the value in use (VIU). Value in use is defined as the present value of the future cash flows expected to be derived from an asset or cash generating unit. The calculation of an asset's value in use incorporates an estimate of expected future cash flows and expectations about possible variations of such cash flows.

Check List

(a) With the recent developments of the coronavirus outbreak, there are both external and internal sources of information, such as the fall of stock and commodity prices, decrease of market interest rates, manufacturing plant shutdowns, shop closures, reduced demand and selling prices for goods and services, indicating that an asset may be impaired. Whether impairment is required?

(b) Whether the remaining useful life, the depreciation /amortization method or the residual value for the asset needs to be reviewed and adjusted even if no impairment loss is recognized for the asset?
(c) Whether deferred tax in respect of any deductible temporary difference on account of impairment has been recognized only to the extent that it is probable that taxable profit will be available against which the underlying deductible temporary differences can be utilized?
(d) Whether the entity has suspended ongoing capex projects due to liquidity/manpower / restrictions imposed by local authorities or the project may no longer remain viable owing the current economic outlook? If yes, whether the entity has considered the impairment losses?

Inventory

The economic disruption caused by coronavirus will pose challenges with respect to determination of NRV at the reporting date. Further, due to disrupted production in the last quarter of a financial year, determination of cost of inventories with respect to allocation of excess overheads also needs to be assessed.

Check List

(a) Whether price realized of inventory post reporting period has been considered as an evidence of the NRV of inventories at the end of the period?
(b) Whether there is a need to write down raw material and WIP below cost if FG is valued below cost?
(c) Is there any contract cancelled before reporting date due to coronavirus outbreak? If yes, then it should not be valued at contract price but at general selling price.
(d) Whether the amount of fixed overhead allocated to each unit of production is not increased because of low production or idle plant?
(e) The incremental cost and wastages (including work-in-progress stocks, if any) incurred as a consequence of the coronavirus outbreak shall be treated as abnormal amount of wasted material, labour and production cost. Ind AS 2 excludes such abnormal cost from capitalization as part of the inventories. Accordingly, such costs shall be recognized as expenses in the profit and loss during the period in which they are incurred.
(f) Whether there are any expiry stocks at the end of the year as well as stocks expired during lockdown period? If yes, whether adequate provision made for expired and near to expiry stocks?
(g) Whether stock dormancy provision is made looking into COVID-19 circumstances?

Leases

A lessor and lessee might renegotiate the terms of the lease or any concessions in lease payment may be received by a lessee because of the coronavirus outbreak. When any concessions in lease payments are received by a lessee, it is necessary to evaluate whether Ind AS 116 applies to such lease concessions.

Check List

(a) Whether there are any lease concessions agreed by the lessee and lessor before the year end? (the effective date of the modification is defined as the date when both parties agree to the lease modification).
(b) If lease modification is not contemplated under the original terms and conditions of the lease, whether at the effective date of the lease modification, remeasurement of the lease liability by discounting revised lease payments using a revised discount rate (revised incremental borrowing rate) with a corresponding adjustment to right-of-use asset has been done?

(c) If the modification decreases the scope of the lease (including cancellation), whether the remeasurement of the lease liability by decreasing the carrying amount of the right-of-use asset to reflect the partial or full termination of the lease has been done and whether profit or loss any gain or loss relating to the partial or full termination has been recognise in the profit and loss.
(d) Whether there are plans to close down stores due to Coronavirus outbreak? If yes, whether impairment of ROU Asset and Leasehold improvement has been done? (This is in addition to normal business plan to close down non-viable stores).
(e) Whether the lease which is entered but not commenced due to disruptions caused by Coronavirus outbreaks? If yes, whether such lease is going to continue or will terminate? If such lease is going to terminate, whether initial direct cost incurred for such lease has been charged to profit and loss?

Employee Benefits

The coronavirus outbreak will affect various estimates and actuarial assumptions that the management has been making in measurement of employee benefit obligations. For instance, there may be an impact on discount rate used to discount employee benefit obligations and future salary growth rates may no longer hold good. Entities may also have to modify their existing employee stock option plans ("ESOP") to ensure that employees are fairly compensated for the decrease in share prices.

Check List

(a) Whether there is any change in the terms and conditions of ESOP Schemes?
(b) Whether there is any change in the Employee benefit policies, like cancellation of accumulated leave balance etc.?
(c) Whether the assumptions regarding discount rate, employee turnover, salary growth have been taken into account for actuarial valuation of employee benefits considering COVID-19 impact?

Provisions, Contingent Liabilities and Contingent Assets

Entities will need to assess whatever action they take because of the coronavirus outbreak results in recognition of any additional provisions including provision for onerous contract (Onerous contract is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it).

Check List

(a) Whether there is virtual certainty that the entity will be compensated for at least some of the consequences of the coronavirus outbreak under a valid insurance policy? If yes, then insurance recovery shall be recognized as an asset separately without netting off.
(b) Whether there is any liquidated damages or penalty provision for non-delivery of goods? If yes, whether it has been provided adequately or the entity may be relieved by a clause like force majeure?

Income Tax

Entities affected by current market conditions of coronavirus pandemics may be incurring unexpected losses and may need to re-evaluate and change their conclusions about the realizability of their deferred tax assets. Future realization of deferred tax assets ultimately depends on the existence of sufficient taxable income of appropriate character during the carry forward period. Recent cumulative losses or the expectations that an entity will have cumulative losses constitutes significant negative evidence about the realizability of the deferred tax assets.

Check List

(a) Whether Management has considered with adequate documentation whether DTA on carry forward losses can be recovered in future against future taxable profits?

Check list related to Other Matters

(a) Whether the entity has suspended capitalizing borrowing cost when the construction is disrupted due to current coronavirus situation? (Ans: Entity has to suspend capitalisation).
(b) Whether the entity has continued to depreciate the assets as per their current accounting policy and estimate of useful lives? (Ans: Entity has to continue providing depreciation).
(c) Whether the entity has relooked at the risk and restriction on short term highly liquid investments that are readily convertible into cash?

AUDIT PROCEDURES

Physical Verification of Inventory

1. Obtain assistance from internal auditor on whose work the statutory auditors can rely; **OR**
2. Entities may determine to perform physical verification of inventories on a subsequent date after the period end date in consultation with their statutory auditors; **OR**
3. Obtain assistance from an external party (such as, an independent chartered accountant firm in that location). **OR**
4. They could also perform rollback procedures to give comfort to their statutory auditors with respect to the inventory that is recorded as at the reporting date.
    - Obtain list of location wise inventory (including godowns) inventory count and value as on current date as well as year-end date;
    - Select on the basis of ABC Analysis, sample locations for rollback procedure;
    - Verify movement of inventory from reporting date to current date with documentary evidence
    - If no material discrepancy found, rely on year-end inventory statement for valuation purpose.

Balance Confirmation Certificate

1. Send the electronic confirmation requests in consultation with the statutory auditors. The confirmation request should clearly indicate the name, address and other identifying information of the requesting entity. The confirmations may be sent in an electronic file format or alternatively the confirmation requests can be prepared on the body of an e-mail to be sent to third parties.
2. Communicate with your vendors and customers for performing balance confirmations electronically.
3. If response of confirmation request is low, then subsequent period movement in the balance to be checked. The entity has to prepare statement showing movement in vendor and customer balances post balance sheet date up to the date of audit.

Internal Financial Control over Financial Reporting

1. Entities may need to implement additional controls or make changes to existing controls that are in place, e.g. if any of the controls in place may not be effective during the time of lockdown when people are working remotely from home and look for the alternate controls that can be implemented.