Securities Regulation Daily Wrap Up, PUBLIC COMPANY REPORTING AND DISCLOSURE—CorpFin staff issues additional COVID-19 guidance, Teotia stresses importance of financial controls, (Jun. 23, 2020)

Securities Regulation Daily Wrap Up

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Staff has offered additional views regarding COVID-19 disclosures involving operations, liquidity, and capital resources, while the Commission's chief accountant reminded issuers of the continued need for high-quality reporting in the wake of the pandemic.

Staff of the SEC's Division of Corporation Finance has issued additional guidance regarding operations, liquidity, and capital resources disclosures that companies should consider with respect to business and market disruptions related to COVID-19. In supplementing CF Disclosure Guidance Topic No. 9, the Division continues to encourage companies to provide disclosures that allow investors to understand and evaluate how management and the board of directors are analyzing the current and expected impact of COVID-19 on a company's operations and financial condition. Separately, SEC Chief Accountant Sagar Teotia published a statement reminding public companies of the need to provide decision-useful information to investors as they prepare for 2020's second-quarter financial reporting cycle.

Operations, liquidity, and capital resources. In CF Disclosure Guidance Topic No. 9A, staff notes that companies are making a diverse range of operational adjustments in response to the effects of COVID-19, such as a transition to telework; supply chain and distribution adjustments; and suspending or modifying certain operations to comply with health and safety guidelines. Companies are also engaging in a complex range of financing activities in response to the pandemic, sometimes novel terms and structures.

Accordingly, the guidance states that companies should provide robust and transparent disclosures about how they are dealing with short- and long-term liquidity and funding risks in the current economic environment, particularly to the extent efforts present new risks or uncertainties to their businesses. While companies have made some of these disclosures in their earnings releases, staff encourages firms to evaluate whether any of the information should also be included in MD&A in light of its potential materiality.

The staff encourages companies to consider a broad range of questions when analyzing their disclosure obligations in the area, including, among others:

- What are the material operational challenges that management and the board are monitoring and evaluating?
- How is the company's overall liquidity position and outlook evolving?
- Has the company accessed revolving lines of credit or raised capital in the public or private markets to address liquidity needs?
- Is the company at material risk of not meeting covenants in its credit and other agreements?
- If the company includes metrics such as cash burn rate or daily cash use in its disclosures, do the disclosures clearly define the metrics and explain how they are used by management?
- Has the company altered terms with its customers, and if so, how have those actions materially affected the company's financial condition or liquidity?
- Is the company relying on supplier finance programs to manage cash flow?

Financial assistance under the CARES Act. The guidance states that companies receiving federal assistance under the Coronavirus Aid, Relief, and Economic Security (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. Some of the questions for companies to consider here include, among others:

- How does a loan impact the company's financial condition, liquidity and capital resources? What are the material terms and conditions of any assistance, and does the company anticipate being able to comply with them?
- Is the company taking advantage of any recent tax relief, and if so, how does that relief impact its short- and long-term liquidity?
- Does the assistance involve new material accounting estimates or judgments that should be disclosed or materially change a prior critical accounting estimate?

Ability to continue as a going concern. Management should also consider whether conditions and events raise substantial doubt about the company's ability to meet its obligations as they become due within one year after the issuance of the financial statements. When substantial doubt exists about a company's ability to continue as a going concern or the substantial doubt is alleviated by management's plans, management should provide the appropriate disclosures in the financial statements and consider the following questions, among others, regarding the MD&A disclosure:

- 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, has the company defaulted on outstanding obligations or faced labor challenges or a work stoppage?
- What are the company's plans to address these challenges?

Chief accountant's statement. In his statement, Chief Accountant Teotia emphasized the importance of disclosure controls and procedures (DCP) and internal control over financial reporting (ICFR). He acknowledged that preparers have had to adapt their financial reporting processes as they respond to the changing environment, including changes involving how controls operate or can be tested and if there is any change in the risk of the control operating effectively in a telework environment. In addition, changes to the business and additional uncertainties may require the implementation of new or enhanced controls in order to mitigate additional risks of material misstatement to the financial statements. The chief accountant reminded preparers that if any change materially affects, or is reasonably likely to materially affect, an entity's ICFR, that change must be disclosed in quarterly filings in the fiscal quarter in which it occurred (or fiscal year in the case of a foreign private issuer).

Complex or emerging financial reporting issues. Teotia observed that a number of complex financial reporting issues arose during the first quarter 2020 reporting cycle. He noted that the Office of the Chief Accountant (OCA) has processes in place to provide staff views on the application of U.S. GAAP and International Financial Reporting Standards (IFRS) to complex, unique, or novel issues. Several of these matters that arose during the first quarter reporting cycle were resolved through the OCA consultation process. Issues that the OCA addressed over the quarter included the financial reporting ramifications of the CARES Act, debt modifications, hedging, consolidation, business combinations, lease concessions, revenue recognition, and income taxes. Teotia encourages stakeholders to contact his office with questions they encounter as a result of COVID-19 or other emerging issues.

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