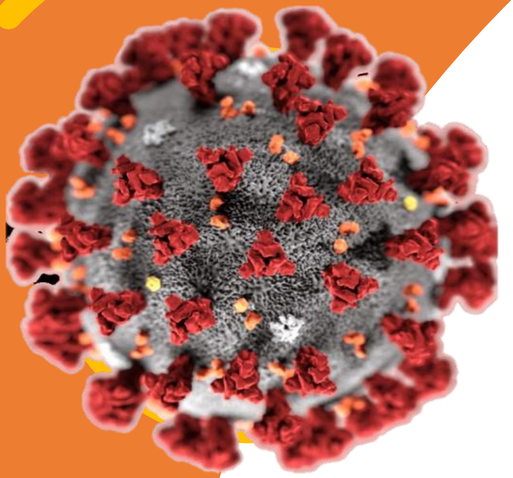


COVID-19 CONSIDERATION ON FINANCIAL REPORTING AND AUDIT

PANELIST 2:

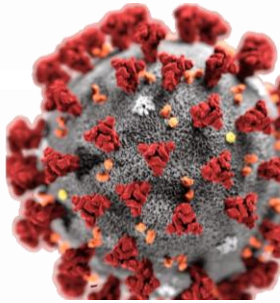
Dr. Hendang Tanusdjaja, FCPA (Aust.)

Advisory Committee Member

CPA Australia-Indonesia

Jakarta, 15 July 2020

- WHAT HAS THE IMPACT OF COVID-19 BEEN ON THE BUSINESS WORLD?



Ref: Amanda White, Webinar Untar-CPA Australia, 02 July 2020

PART 1:
HOW DOES COVID-19 AFFECT FINANCIAL REPORTS?

Financial reporting becomes more complex

- ❑ Asset values
  - ❖ significant falls and impairments
  - ❖ difficulty in determining fair value
- ❑ Effect of rapid change
  - ❖ huge increase in estimation uncertainty
  - ❖ rapid obsolescence of information
- ❑ Disclosures
  - ❖ narrative around how risks are managed
  - ❖ disclosure of judgments, assumptions and source of estimation uncertainty

Regulatory & tax update (Indonesia)

- ❑ Exemption for Article 22 Income Tax on Imports
- ❑ Article 21 Income Tax Relief for Taxpayers
- ❑ 30% Reduction of Article 25 Income Tax
- ❑ Decrease in corporate tax rate:
  a. 22% for fiscal year 2020 & 2021;
     (Listed Entity min. 40%➔ 19%)
  b. 20% for fiscal year 2022 onward
     (Listed Entity min. 40% ➔ 17%)

COVID-19 ACCOUNTING IMPLICATIONS

1. Events After The Reporting Period
2. Going Concern
3. Breath of Covenants
4. Impairment of Assets
5. Revenue Recognition
6. Income Taxes
7. Leases
8. Inventories
9. Employee Benefits and Share-based Payments
10. Other Financial Statement Disclosures

1. EVENTS AFTER THE REPORTING PERIOD (1 OF 2) REF: IAS 10

- The global situation is evolving rapidly. Management should therefore consider the requirements of IAS 10 Events after the reporting period and in particular whether the latest developments provide more information about the circumstances that existed at the reporting date.
- Events that provide more information about the spread of the virus and the related costs might be adjusting events.
- Events, such as the announcement or enactment of new measures to contain the virus or decisions taken by management are likely to be non-adjusting. Clear disclosure of non-adjusting events is required when this is material to the financial statements.
- Example of non-adjusting events after the reporting period that would generally result in disclosure (IAS 10:22 (h))
  - changes in tax rates or tax laws enacted or announced after the reporting period that have a significant effect on current and deferred tax assets and liabilities (see IAS 12 *Income Taxes*);

* World Health Organization

1. EVENTS AFTER THE REPORTING PERIOD (2 OF 2) (REF. IAS 10)

When is the reporting date?

For many Indonesian companies with fiscal year-ends of December 31, COVID-19 may not have been a pervasive event on December 31st and therefore impacts related to COVID-19 should be considered based on the reporting date.

Should the impact of COVID-19 be considered related to:	December 31, 2019 and prior year ends	March 31, 2020 and subsequent period ends
Adjustments to measurement and recognition of financial statement items that occurred prior to year end	No	Yes
Adjusting subsequent events	No	Yes
Subsequent events disclosure	Yes	It Depends
Going concern assessment	Yes	Yes

2. GOING CONCERN: (REF. IAS 1)

The degree of consideration depends on the facts in each case, such as:

- ❖ Current and expected profitability
- ❖ Debt repayment schedules
- ❖ Potential sources of replacement financing

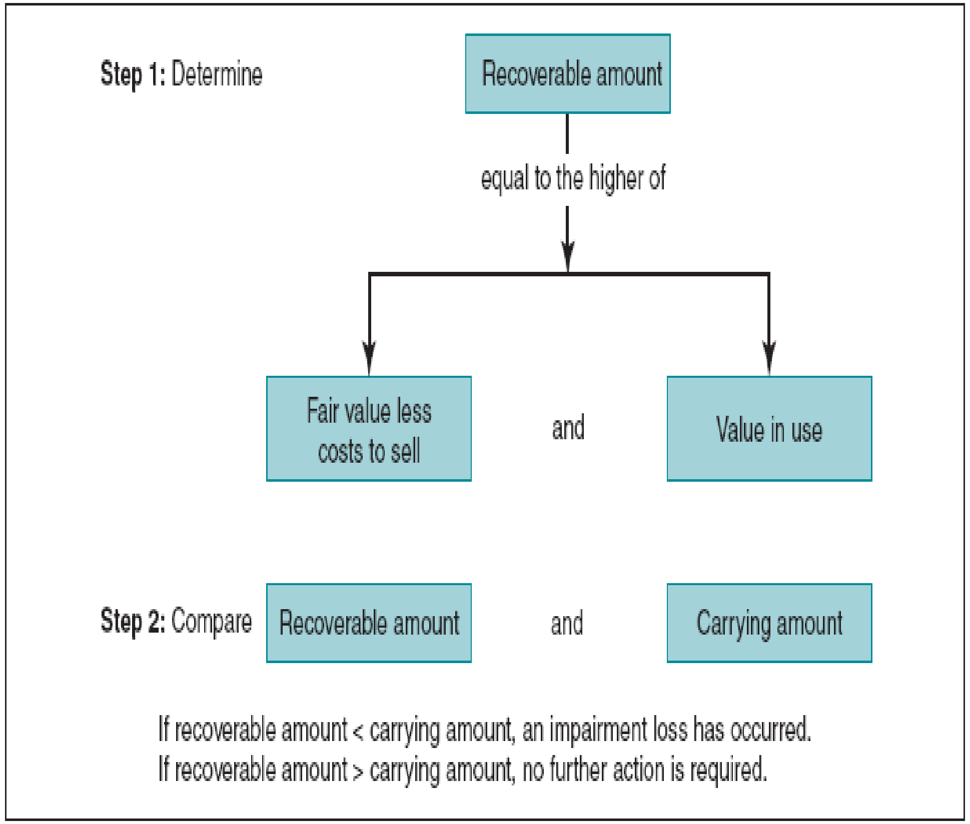
- Management should consider the potential implications of COVID-19 and the measures taken to control it when assessing the entity's ability to continue as a going concern.
- An entity is no longer a going concern if management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.
- Management should consider the impact of measures taken by governments and local banks in its assessment of going concern. Management should also remember that events after the reporting date that indicate an entity is no longer a going concern are always adjusting events.
- Material uncertainties that might cast significant doubt upon an entity's ability to continue as a going concern should be disclosed in accordance with IAS 1.

3. BREACH OF COVENANTS (REF. IAS 1)

Non-current liabilities → Current Liabilities
Going cocernm issue??

- The financial impact of the virus might cause some entities to breach covenants on borrowings or trigger material adverse change clauses. This could result in loan repayment terms changing and some loans becoming repayable on demand.
- Management should consider whether the **<u>classification of loans and other financing liabilities between noncurrent and current is affected and in extreme situations whether the entity remains a going concern.</u>**
- Management should consider particularly the impact of any cross-default clauses.
- Management should also consider the effect of any changes in the terms of borrowings as a result of the circumstances described above and treat waivers obtained after the reporting date as non-adjusting events.

4. IMPAIRMENT OF ASSETS (1 OF 3) (REF. IAS 36)



- Among the many consequences of COVID-19, impacts such as business and production disruptions, supply chain interruptions, negative impacts on customers, volatility in the equity and debt markets, reduced revenue and cash flows, and other economic consequences may occur. The entities whose operations are negatively affected by COVID-19 may need to consider testing their assets for impairment.
- <u>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.</u>
- When estimating the recoverable amount based on the VIU, <u>the forecasted cash flows should reflect management's best estimate of the economic conditions that will exist over the remaining useful life of the asset</u>.

4. IMPAIRMENT OF ASSETS (2 OF 3) (REF. IAS 36)

What type of non-financial assets does IAS 36 apply to ?

- Fixed assets measured at cost or revaluation model
- Investment property measured at cost model
- Right-of-use assets
- Indefinite-lived intangible assets , intangible assets not yet available for use, and goodwill acquired in a business combination
- Investment properties measured at cost
- Investments in associates and joint ventures
- Other non-financial assets → When there are triggering events, such as:
  - ✓ Significant changes with an adverse effect such as technological, market, economic, legal environment
  - ✓ Carrying amount value > market capitalization

4. IMPAIRMENT OF ASSETS (3 OF 3) (REF. IAS 36)

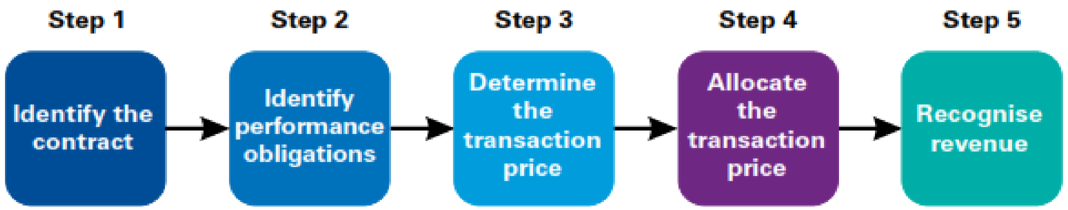
External indicators include:

- **Decline in market value**
- **Adverse changes in entity's environment/ market**
- **Increases in interest rates**
- **Market capitalisation**

Internal indicators include:

- **Obsolescence or physical damage**
- **Change in asset use**
- **An asset's economic performance being worse than expected**

- Entities are required to determine whether the outbreak is considered to be an **impairment indicator** at the reporting date, which results in an impairment assessment. In respect of the impairment test that was performed at 31 December 2019, management needs to be mindful that the assumptions being used to determine the recoverable amounts reflected the conditions existing at that date. Entities need to consider providing detailed disclosures on the assumptions and sensitivities



- The parties to the contract have approved the contract
- Each party's rights in relation to the goods or services to be transferred can be identified
- The contract has commercial substance
- The payment terms and conditions for the goods or services to be transferred can be identified
- The collection of an amount of consideration to which the entity is entitled to in exchange for the goods or services is probable

5. REVENUE RECOGNITION (REF. IFRS 15) (1 OF 2)

Impact of Covid-19

To help its customers or to provide incentives for them to continue purchasing its goods or services, an entity may:

- revise its agreements to reduce any purchase commitments;
- allow customers to terminate agreements without penalty; or
- provide price concessions, discounts on the purchase of future goods or services, free goods or services, extended payment terms or extensions of loyalty programmes.

Further, because the entity itself may be experiencing financial difficulties and supply disruptions, it may:

- request up-front payments from its customers;
- delay the delivery of goods or services;
- pay penalties or refunds for failing to perform, not meeting service-level agreements, or terminating agreements; or
- incur unexpected costs to fulfil its performance obligations.

5. REVENUE RECOGNITION (2 OF 2) (REF. IFRS 15)

Impact of Covid-19

Therefore, as a result of the changes in circumstances experienced by both an entity and its customers due to the COVID-19 pandemic, an entity may need to consider the following when assessing revenue from contracts with customers:

- ❖ Contract enforceability
- ❖ Collectability
- ❖ Contract modification
- ❖ Variable consideration
- ❖ Material right
- ❖ Significant financing component
- ❖ Implied performance obligations
- ❖ Recognition of revenue
- ❖ Costs to obtain or fulfil a revenue contract and up-front payments from its customers
- ❖ Disclosure requirements

6. INCOME TAXES (REF. IAS 12)

DTD x tax rate % = DTA

TTD x tax rate % = DTL

The tax rate % is that which is expected to apply when the asset will be realised or the liability settled

- The virus could affect future profits as a result of direct and indirect (effect on customers, suppliers, service providers) factors.
- Asset impairment may also reduce the amount of deferred tax liabilities and/or create additional deductible temporary differences.
- <u>Entities with deferred tax assets should reassess forecast profits and the recoverability of deferred tax assets in accordance with IAS 12 Income taxes taking into account the additional uncertainty arising from the virus and the steps taken to control it</u>.
- Management might also consider whether the impact of the virus affects its plans to distribute profits from subsidiaries and whether it therefore needs to reconsider the recognition of any deferred tax liability in connection with undistributed profits.
- <u>Management should disclose any significant judgements and estimates made in assessing the recoverability of deferred tax assets, in accordance with IAS 1.</u>

7. LEASES (IFRS 16): RENT CONCESSION

- What's the issue? Accounting for rent concessions granted as a result of COVID-19 could be complex under IFRS 16. The IASB has issued an amendment to IFRS 16 in response.
- What has changed? The IASB has provided lessees (but not lessors) with relief in the form of an **optional exemption** from assessing whether a rent concession related to COVID-19 is a lease modification.
- When does it apply? The practical expedient only applies to rent concessions occurring as a direct consequence of the COVID-19 pandemic and only if all of the following conditions are met:
  - the change in lease payments results in revised consideration for the lease that is substantially **the same as, or less than**, the consideration for the lease immediately preceding the change;
  - any reduction in lease payments affects **only payments due on or before 30 June 2021**; and
  - there is **no substantive change to other terms and conditions of the lease**.
- When is it effective? The amendments are mandatory for annual reporting periods **beginning on or after 1 June 2020**. Earlier application is permitted, including in interim or year end financial statements not yet authorised for issue at 30 May 2020 (Indonesia), to permit application of the relief as soon as possible.

8. INVENTORIES (REF. IAS 2)

- ❖ Presentation of Inventories:

  The Lower of Cost or Net Relizable Value

  Net Reliazable Value = **S/P – Cost to complete –Cost to sell**

- ❖ potential increase in write downs and obsolescence due to Covid-19
  - ➢ Reduced demand
  - ➢ Price falls

- ❖ Allocation of overheads may be difficult during shutdown
  - ➢ variable overhead based on actual cost
  - ➢ The actual level of production may be used if it approximates normal capacity. The amount of fixed overhead allocated to each unit of production is not increased as a consequence of low production or idle plant.
  - ➢ fixed overhead based on normal capacity, with the difference goes to P/L.

9. EMPLOYEE BENEFITS AND SHARE-BASED PAYMENTS (1 OF 2) (REF. IAS 19 & IFRS 2)

- Need to revise assumptions used to measure employee benefits and share based payments?
  - For example, the yield on high-quality bonds or the risk-free interest rate in a particular currency might have changed as a result of recent developments or the probability of an employee meeting the vesting conditions for bonuses or share based payments might have changed.
- How is the impact of any changes made to the terms of, for example, a share-based payment plan, to address the changes in the economic environment and the likelihood that performance conditions will be met?
  - To the extent that such changes are beneficial to the employee, they would be accounted for as a modification and an additional expense recognised. Management should be aware that cancelling a share based payment award even if the vesting conditions are unlikely to be satisfied results in the immediate recognition of the remaining expense

9. EMPLOYEE BENEFITS AND SHARE-BASED PAYMENTS (2 OF 2) (REF. IAS 19 & IFRS 2)

- Consider whether it has a legal or constructive obligation to its employees in connection with the virus,
  - For example, sick pay or payments to employees that self-isolate, for which a liability should be recognised.
- Consider reducing its work-force as a result of the virus. IAS 19 Employee benefits requires that a liability for employee termination is recognised only when the entity can no longer withdraw the offer of those benefits or the costs of a related restructuring are recognised in accordance with IAS 37.
- IFRS 2 Share based payment requires that entities explain modifications to share based payments, along with the incremental fair value granted, as well as information about how the incremental fair value was determined.
- IAS 19 requires extensive disclosure of the assumptions used to estimate employee benefit liabilities, together with sensitivities and changes in those assumptions.

10. OTHER FINANCIAL STATEMENT DISCLOSURES (1 OF 2) - JUDGEMENTS AND ESTIMATES MADE BY MANAGEMENT

Assumptions and sources of estimation uncertainty

- The assumptions the entity makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year
- Examples of the types of disclosures to be made:
  a. the nature of the assumption or other estimation uncertainty;
  b. the sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity
  c. the expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year in respect of the carrying amounts of the assets and liabilities affected; and
  d. an explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved.

10. OTHER FINANCIAL STATEMENT DISCLOSURES - COVID-19 RELATED DISCLOSURES (2 OF 2)

Entity must consider whether disclosure is required to address the potential impact of Covid-19 on business operations and financial results.

- Consider the following:
  - ✓ Risk factor, such as liquidity
  - ✓ Forward looking information
  - ✓ Measurement uncertainty
  - ✓ Critical accounting estimates

- Avoid boilerplate disclosure concerning COVID-19 in upcoming filings
  - ✓ Focus on entity-specific information that is clear and relevant to allow investors to fully understand how the business is impacted by the virus
  - ✓ Continue to monitor and update these disclosures

PART II
HOW DOES COVID-19 AFFECT AUDITS?

- Auditing just become more difficult
  - Forward-looking estimates and judgments
  - Increased risk of fraud and misstatement
- Same as last year will not work
  - Increased number of significant risks
  - Different business conditions
  - Different nature of operations and control environments
  - Greater uncertainty increases requirement for audit evidence
- Disclosures becomes more important
  - Increased level of risk and user scrutiny
  - Increased uncertainty around estimates and judgments
  - Going concern

Impact on Audit Process **1/6**

No		Audit Approach
1	Key auditor’s judgements ❖ Reassess previous judgements made during earlier phases of the audit	Areas impacted could include: a. Audit risks (identification and assessment) b. Materiality c. Need for EQCR d. Use of experts e. Communications with TCWG
2	Risk identification and assessment: ❖ Consider practicalities of obtaining necessary level of understanding. (Ref. ISA 315)	• The auditor will need to determine how practicable it will be to obtain an appropriate level of understanding, and to perform evaluations relating to audit risk identification and assessment. • This may be particularly challenging for new clients or for existing clients who have undergone significant change since the prior audit.

Impact on Audit Process 2/6

No	Audit Approach	
3	Potential limitations of scope_(LoS): ❖ Availability of audit evidence. (Ref. ISA 500,501,705)	• Key areas to consider include: a. Access to books and records. b. Attendance for inventory observation. c. PP&E verification. • May need to consider alternative audit procedures. • Consider impact of LoS on audit opinion • Consider whether engagement terms have been agreed.
4	Quality of audit evidence: ❖ Impact to audit evidence from switching to a remote audit from a traditional on-site approach.	• Reliability (consider source and nature of evidence). • Completeness.

Impact on Audit Process 3/6

No		Audit Approach
5	Inventory: ❖ Perpetual inventory system ❖ Periodic inventory system (Ref. ISA 501)	Are there alternative procedures to attending physical inventory count?: Virtual attendance Substantive tests of detail (e.g. test sales after year-end) / Testing of other inventory controls / Use of technology such as Video conferencing, drones or robotics
6	Going concern: ❖ Going concern assessments will need to be continuously updated as Covid-19 circumstances evolve (Ref. ISA 570)	• Design audit procedures appropriate to the circumstances • Consider updated business plans and revised assessment of availability of funding • Audit going concern assessment should be current up to date of signing audit opinion

Impact on Audit Process **4/6**

No		Audit Approach
7	Valuation and measurement: (Ref. ISA 540) ❖ Likely increased complexity to measure assets and liabilities whose values may be significantly affected by Covid-19. ❖ Auditors need to consider government regulations related to Pandemic Covid-19 both in the form of relaxation, stimulus, or others. ❖ Revenue recognition may be impacted too, e.g. costs to fulfil contracts and progress to satisfy performance obligations.	Areas impacted may include: • Inventory obsolescence. • Provisions for doubtful receivables. • Provisions for liabilities for claims / refunds . • Financial instruments. • Investments • Pension assets and liabilities • *Recoverability of Carrying Amounts, such as* Deferred tax assets and *Goodwill*. • Revenue recognition. • Probability of *impairment of PPE and intangible assets for the year of* 2020, if jika terdapat segmen perusahaan yang berhenti beroperasi.

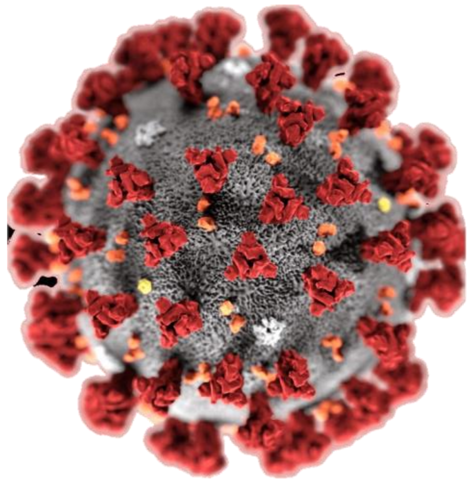
Impact on Audit Process 5/6

No.		Audit Approach
8	Taxation Added complexity from current circumstances	• There may be complexities for treatment of transactions that are unusual or one-off in nature, including application for tax relief.
9	Group audit considerations (Rf. ISA 600)	• Component audits should be properly planned and conducted in response to the changed circumstances • Impact on review of component auditor work papers, if necessary.

Impact on Audit Process **6/6**

No		Audit Approach
10	Subsequent events (Ref. ISA 560)	• Design procedures which are appropriate to the current circumstances. • Consider impact where client obtains extension to filing deadline.
11	Adjusting / non-adjusting events	Judgement may be required in determining whether or not the effects of Covid-19 represent an adjusting or non-adjusting event.
12	Presentation and disclosure	• Presentation and disclosures will need to be prepared to appropriately describe current circumstances, including sufficient description of relevant risks, estimates and judgements applied. • Disclosure of commitments and contingencies arising related to the condition of the Covid-19 Pandemic.

Q & A or Comments Session



Thank You