



CAPITAL MARKETS | SEC Staff Guidance on Disclosures and Financial Reporting in Light of COVID-19

On June 23, 2020, the Division of Corporation Finance (Division) of the US Securities and Exchange Commission (SEC) issued CF Disclosure Guidance: Topic No. 9A (CF 9A),¹ providing guidance on operations, liquidity, and capital resources disclosures that companies should consider with respect to COVID-19-related disruptions. On that same date, the SEC's Office of the Chief Accountant (OCA) issued a Statement on the Continued Importance of High-Quality Financial Reporting for Investors in Light of COVID-19 (Statement).²

CF Disclosure Guidance: Topic No. 9A

CF 9A encourages companies to provide, and to revise and update, disclosures in order to enable investors to evaluate both the current and expected impact of COVID-19 through management's eyes. CF 9A supplements CF Disclosure Guidance Topic No. 9,³ which the Division issued in March 2020 regarding disclosure considerations and other securities law obligations related to COVID-19.⁴

Operations, Liquidity and Capital Resources. CF 9A observes that companies have made, or are in the process of making, operational adjustments to respond to the pandemic, such as the transition to telework, supply chain and distribution adjustments, suspension or modification of certain operations to comply with health and safety guidelines and transition back to the workplace. Because these adjustments could impact a company in a way that would be material to an investment or voting decision, CF 9A advises that affected companies carefully consider their disclosure obligations. CF 9A also focuses on the financing activities that companies have undertaken, including the entry into, or entry into amendments to, credit facilities, public and private financings, etc., each of which may have novel terms and structures. CF 9A reminds companies to provide robust and transparent disclosure

regarding short- and long-term liquidity and funding risks, especially new risks or uncertainties. CF 9A encourages companies to evaluate whether such information, in light of its potential materiality, should be discussed in management's discussion and analysis.

CF 9A suggests companies consider a broad range of questions as they evaluate the impacts of COVID-19. CF 9A includes a non-exclusive series of inquiries that companies should consider as potentially relevant to their analysis. Among those questions are the following:

- What are the material operational challenges that management and the board of directors are monitoring and evaluating, and how and to what extent have operations been altered?
- How is the company's overall liquidity position and outlook evolving?
- Has the company accessed revolving lines of credit or raised capital to address its liquidity needs, and do disclosures regarding these actions and any unused liquidity sources provide investors with a complete discussion of the company's financial condition and liquidity?
- Have COVID-19-related impacts affected the company's ability to access traditional funding sources on the same or reasonably similar terms as were available to it in recent periods?
- Is the company at material risk of not meeting covenants in its credit and other agreements?
- Are metrics, such as cash burn rate or daily cash use, included in company disclosures providing a clear definition of the metric and explanation of how management uses the metric in managing or monitoring liquidity?
- Have capital expenditures been reduced and if so, how?
- Is the company able to timely service its debt and other obligations?
- Have terms with customers been altered, such as extended payment terms or refund periods, and if so, how have those actions materially affected the company's financial condition or liquidity?
- Is the company relying on supplier finance programs, otherwise referred to as supply chain financing, structured trade payables, reverse factoring, or vendor financing, to manage its cash flow?
- Has the company assessed the impact that material events occurring after the end of the reporting period, but before the issuance of financial statements, have had or are reasonably likely to have on its liquidity and capital resources; and has it considered whether disclosure of subsequent events in the financial statements and known trends or uncertainties in MD&A is required?

CARES Act. CF 9A also addresses financial assistance that companies may have received under The Coronavirus Aid, Relief, and Economic Security Act (CARES Act), stating that companies receiving federal assistance should consider the impact of that assistance on their financial condition, results of operations, liquidity, and capital resources, as well as related disclosures and critical accounting estimates and assumptions. CF 9A also contains some suggested questions for consideration regarding CARES Act assistance, including:

- How does a loan impact the company's financial condition, liquidity and capital resources, and what are the material terms and conditions of any assistance received?
- Is the company taking advantage of any recent tax relief, and if so, how does that relief impact 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?

Going Concern. CF 9A states that management needs to provide appropriate financial statement disclosures when there is substantial doubt about a company's ability to continue as a going concern or such substantial doubt is alleviated by management's plans. In that regard, CF 9A suggests questions for consideration, such as:

- Are there conditions and events that give rise to substantial doubt about the company's ability to continue as a going concern?
- What are the company's plans to address these challenges, and has any portion of those plans been implemented?

Statement on the Continued Importance of High-Quality Financial Reporting for Investors in Light of COVID-19

Recognizing that many public companies are now preparing for their second-quarter financial reports, the Statement emphasizes that financial reporting system participants play an important role both in the functioning of the capital markets and in the national effort to mitigate the economic effects of the COVID-19 pandemic. The Statement highlights some of the significant accounting, auditing and financial reporting issues recently addressed by OCA.

Significant Estimates and Judgments; Reasonable Judgments. The Statement observes that many companies have had to make significant judgments and estimates in order to address various accounting and financial reporting matters. According to the Statement, OCA does not object to well-reasoned judgments. OCA advises companies to "ensure that significant judgments and estimates are disclosed in a manner that is understandable and useful to investors, and that the resulting financial reporting reflects and is consistent with the company's specific facts and circumstances."

Disclosure Controls and Procedures and Internal Control over Financial Reporting. The Statement emphasizes that robust internal accounting controls are important to high-quality, reliable financial reporting. Public companies are required to maintain both disclosure controls and procedures (DCP) and internal control over financial reporting (ICFR), with management evaluating the effectiveness of a public company's DCP as of the end of each fiscal quarter and the effectiveness of its ICFR at the end of each fiscal year. Noting that companies are adapting financial reporting processes as they respond to the changing COVID-19 environment, the Statement reminds companies that if any change materially affects, or is reasonably likely to materially affect, their ICFR, they have to disclose the change in quarterly filings in the fiscal quarter in which it occurred (or fiscal year if the company is a foreign private issuer).

Ability to Continue as a Going Concern. US generally accepted accounting principles presume that a reporting entity has the ability to continue as a going concern. The Statement reminds management that, in each reporting period, including interim periods, they need to consider whether relevant conditions and events, taken as a whole, raise substantial doubt about the entity's ability to meet its obligations as they become due within one year after the issuance of the financial statements and whether management's plans alleviate such substantial doubt. If so, the company needs to provide appropriate disclosures, including information about the principal conditions giving rise to the

substantial doubt, management's evaluation of the significance of those conditions, and management's plans that alleviated the substantial doubt. If substantial doubt about an entity's ability to continue as a going concern is not alleviated, additional disclosure is required, including in the notes to the financial statements. Consultation with OCA. Noting that companies are entering the second-quarter financial reporting season, the Statement indicates that OCA is available for consultation and encourages stakeholders to contact it with questions they encounter as a result of COVID-19 or other emerging issues.

Audit Committees. The Statement highlights the critical oversight role played by audit committees, especially with the rapid change and increased uncertainty arising from the COVID-19 pandemic.

Practical Considerations

The quarter ending June 30, 2020, will be the first quarter in which the COVID-19 pandemic has had a dramatic impact on the US, as well as the global, economy for the entire period. Although COVID-19 disclosures may have been included in periodic reports for prior periods, the ongoing, pervasive impact of COVID-19 requires companies to evaluate their current situation to assess whether they need to add, supplement or revise their disclosures. As part of that process, companies should carefully review CF 9A and the Statement.

Company disclosures related to COVID-19 need to reflect specific circumstances. CF 9A sets forth many questions that companies may need to consider. However, companies should not limit their analyses to those questions. They need to assess all facts that are relevant to their particular business. In order to take into account all aspects of their operations, companies may need to reach out to business units that may not normally be part of their disclosure controls and procedures to gather additional facts.

Companies should begin drafting their COVID-19-related disclosures well in advance of their filing date in order to allow sufficient time for review by management, the audit committee and possibly the full board of directors. Disclosures should then be reassessed immediately prior to filing to confirm that circumstances have not changed materially. Particular care should be taken with respect to the management's discussion and analysis section, particularly since that section is intended to provide trend information, as well as liquidity information.

While this latest set of SEC staff guidance does not address forward-looking information as directly as the staff has in prior statements, it is clear from the illustrative questions that a high premium is being placed on disclosure that provides investors with insights into a reporting company's prospects.

The SEC has announced that Chairman Jay Clayton will moderate a roundtable entitled, "Q2 Reporting: A Discussion of COVID-19 Related Disclosure Considerations," which will be webcast live on [SEC.gov](https://www.sec.gov) at 4:00 p.m. EDT on June 30, 2020. That discussion may provide further insights for upcoming disclosures.

If you wish to receive regular updates on the range of the complex issues confronting businesses in the face of the novel coronavirus, please [subscribe](#) to our COVID-19 "Special Interest" mailing list.

And for any legal questions related to this pandemic, please contact the authors of this Legal Update

or Mayer Brown's COVID-19 Core Response Team at FW-SIG-COVID-19-Core-Response-Team@mayerbrown.com.

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¹ <https://www.sec.gov/corpfin/covid-19-disclosure-considerations>.

² <https://www.sec.gov/news/public-statement/teotia-financial-reporting-covid-19-2020-06-23>.

³ <https://www.sec.gov/corpfin/coronavirus-covid-19>.

⁴ For more information regarding CF Disclosure Guidance Topic No. 9, see our Legal Update, "SEC Extends Conditional Reporting Relief and Issues COVID-19 Guidance for Public Companies," dated March 26, 2020, available at https://www.mayerbrown.com/-/media/files/perspectives-events/publications/2020/03/sec-extends-conditional-reporting-relief-and-issues-covid19-guidance-for-public-companies_3.pdf