Date:
9 June 2020

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Q&A on requirements in MFRS that Malaysian reporting entities may need to consider in respect of the impacts of COVID-19

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Staff - Q&As

Q1 Are there aspects of financial statement presentation that may need to be reconsidered?

A1.1 Going concern

A1.1.1 MFRS 101 *Presentation of Financial Statements*, paragraph 25 says:

> 25 *When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern. An entity shall prepare financial statements on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. When management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties. When an entity does not prepare financial statements on a going concern basis, it shall disclose that fact, together with the basis on which it prepared the financial statements and the reason why the entity is not regarded as a going concern.*

A1.1.2 Some entities that until recently were operating one or more viable businesses may find that changed conditions pose an existential threat to those businesses. In considering whether an entity remains a going concern, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period. Management would need to consider its access to financial resources, measures by governments and financial institutions to provide temporary or other relief from current conditions, and the prospects and likely timing for any expected rebound in its business activities.

A.1.1.3 MFRS 101.25 requires that:

(a) When there are material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity discloses those uncertainties [MFRS 101.25].

(b) When an entity does not prepare financial statements on a going concern basis, it discloses that fact, together with the basis on which it prepared the financial statements and the reason why the entity is not regarded as a going concern [MFRS 101.25].

A.1.1.4 MFRS 101 does not explain the recognition and measurement requirements that might apply in the event an entity is judged not to be a going concern. Depending on the facts and circumstances, the carrying amounts of assets might best be measured by applying some or all of the requirements in MFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*; for example, because the best available option is to sell the entity or its individual businesses. Please see Section A18 below. Alternatively, MFRS 136 *Impairment of Assets* might be relevant. Please see Section 12 below.

A1.2 Current versus non-current asset classification

A1.2.1 MFRS 101.66 says:

> *66 An entity shall classify an asset as current when:*
>
> *(a) it expects to realise the asset, or intends to sell or consume it, in its normal operating cycle;*
>
> *(b) it holds the asset primarily for the purpose of trading;*
>
> *(c) it expects to realise the asset within twelve months after the reporting period; or*
>
> *(d) the asset is cash or a cash equivalent (as defined in MFRS 107) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.*
>
> *An entity shall classify all other assets as non-current.*

A1.2.2 Some entities may find that they need to suspend some business activities for a period due to government or other restrictions. In some cases, the suspensions will not affect classification because activities are expected to remain within the normal operating cycle. For example, for an entity with a long operating cycle, a six-month suspension may be within normal bounds.[1]

A1.2.3 Alternatively, previously current assets might now be non-current because there is no longer a prospect of selling, consuming, or realising those assets within the normal operating cycle for that entity. For example, an asset under construction that was previously expected to be completed and sold within a year, may now be expected to be completed and sold in 18-months' time, either because of the direct impacts of COVID-19-related government actions or due to a consequential expected deterioration in business conditions.

A1.2.4 Judgement would need to be applied in determining whether the impacts of COVID-19 have led to changed circumstances that are sufficiently different from 'normal' to warrant a changed asset classification. Please note that, if a line item includes amounts expected to be recovered: (a) no more than twelve months after the reporting period, and (b) more than twelve months after the reporting period; the entity discloses the amount expected to be recovered after more than twelve months [MFRS 101.61].

A1.3 Current versus non-current liability classification

A1.3.1 MFRS 101.69 says:

> *69 An entity shall classify a liability as current when:*
>
> *(a) it expects to realise the liability in its normal operating cycle;*
>
> *(b) it holds the liability primarily for the purpose of trading;*
>
> *(c) the liability is due to be settled within twelve months after the reporting period; or*

1 MFRS 101.68, 70 and 71 identify that the operating cycle is determined at the entity level (rather than the asset or liability level).

> (d) *it does not have an unconditional right to defer settlement for at least twelve months after the reporting period (see paragraph 73). Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.*[2]
>
> *An entity shall classify all other liabilities as non-current.*

A1.3.2 Some entities may be in a position to renegotiate loans and other payables such that repayments are deferred. There may be cases when loans and other payables previously classified as current would be reclassified as non-current.

A1.3.3 Alternatively, the impacts of COVID-19-related government actions might trigger contractual covenants that cause loans that were previously classified as non-current to be repayable on demand and to be reclassified as current.

A1.3.4 Please note that, if a line item includes amounts expected to be settled: (a) no more than twelve months after the reporting period, and (b) more than twelve months after the reporting period; the entity discloses the amount expected to be settled after more than twelve months [MFRS 101.61].

A1.4 Judgements and sources of estimation uncertainty

A1.4.1 MFRS 101.122 and 125 say:

> 122 *An entity shall disclose, along with its significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 125), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.*
>
> 125 *An entity shall disclose information about the assumptions it 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. In respect of those assets and liabilities, the notes shall include details of:*
>
> (a) *their nature, and*
>
> (b) *their carrying amount as at the end of the reporting period.*

A1.4.2 Management may be forced to make many more judgements about asset values, and the carrying amounts of liabilities (for example, employee liabilities) than is typically the case. Those judgements would need to be disclosed when they are among the most significant expected to be made, consistent with MFRS 101.122.

A1.4.3 Previously stable business environments may have provided entities with a low level of estimation uncertainty. However, recent events may have given

[2] MFRS 101.69(d) was amended in March 2020. The amended paragraph reads: "(d) *it does not have the right at the end of the reporting period to defer settlement for at least twelve months after the reporting period".* This Amendment takes effect on 1 January 2022, retrospectively in accordance with MFRS 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. At the time of writing, the IASB is considering deferring the effective date to 1 January 2023.

rise to uncertainties that were previously inconceivable. Accordingly, there may be a need for greater disclosure under MFRS 101.125.

Q2 Are there issues relating to inventories that might need to be considered?

A2.1 Lower of cost and net realisable value

A2.1.1 MFRS 102 *Inventories*, paragraph 9 says:

> 9 *Inventories shall be measured at the lower of cost and net realisable value.*

A2.1.2 MFRS 102.6 defines net realisable value as the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

A2.1.3 MFRS 102.28 says:

> 28 *The cost of inventories may not be recoverable if those inventories are damaged, if they have become wholly or partially obsolete, or if their selling prices have declined. The cost of inventories may also not be recoverable if the estimated costs of completion or the estimated costs to be incurred to make the sale have increased. …*

A2.1.4 Some inventories may need to be written down to net realisable value due to recent developments, which for example may have:

(a) reduced selling prices to below cost; or

(b) resulted in the entity being unable to sell its inventory prior to it becoming obsolete (for example, fashion clothing that could be out-of-date by the time sales are feasible).

Material write downs would need to be separately disclosed under MFRS 101.98(a).

A2.2 Allocating the cost of overheads

A2.2.1 MFRS 102.13 says (in part):

> 13 *The allocation of fixed production overheads to the costs of conversion is based on the normal capacity of the production facilities. Normal capacity is the production expected to be achieved on average over a number of periods or seasons under normal circumstances, …*

A2.2.2 In the event that an entity has a business operating at below normal capacity, when relevant, it would be expected to continue to allocate overheads to the costs of inventories based on normal capacity. Otherwise, the costs of inventory may be overstated.

A2.2.3 The 'excess' overheads would be recognised immediately as expenses in profit or loss.

A2.2.4 MFRS 102.10 says:

> *10 The cost of inventories shall comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.*

By way of example, an entity that includes the costs of storing partly manufactured goods among the costs of inventories would include only those storage costs that are normally necessary during the production process. If the production process has been temporarily interrupted, any additional storage costs would be expensed.

Q3 Might accounting policies and estimates need to be reconsidered?

A3.1 Accounting policies

A3.1.1 Provided the entity remains a going concern, it would not be expected that accounting policies would change based on recent events. MFRS 108 requires that accounting policies be applied consistently for similar transactions, other events and conditions [MFRS 108.13].

A3.2 Accounting estimates

A3.2.1 The current circumstances may lead to an entity changing its accounting estimates. For example, the expected pattern of consumption of the future economic benefits embodied in property, plant and equipment may change if it were to become idle in the short to medium term.

A3.2.2 MFRS 108.36 and 37 say (in part):

> *36 The effect of a change in an accounting estimate, other than a change to which paragraph 37 applies, shall be recognised prospectively by including it in profit or loss in:*
>
> *(a) the period of the change, if the change affects that period only; or*
>
> *(b) the period of the change and future periods, if the change affects both.*
>
> *37 To the extent that a change in an accounting estimate gives rise to changes in assets and liabilities, or relates to an item of equity, it shall be recognised by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.*

Q4 What type of subsequent event might COVID-19 constitute?

A4.1 Events after the reporting period

A4.1.1 MFRS 110 *Events after the Reporting Period*, paragraph 3 says (in part):

> *3 Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. Two types of events can be identified:*

> *(a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and*
>
> *(b) those that are indicative of conditions that arose after the reporting period (non-adjusting events after the reporting period).*

A4.1.2 Entities reporting for the year ending 31 December 2019 that have not yet finalised their financial statements would need to assess whether recently available information about the impact of COVID-19 and related government actions on their businesses would affect amounts recognised as at 31 December. For example, if by the time the financial statements are completed, a large debtor that was already regarded at balance date as credit-impaired, has been bankrupted by recent events and the debt remains unpaid, it would usually be relevant to adjust the receivable as at 31 December 2019 [MFRS 110.9].

A4.1.3 Events that are non-adjusting would include, for example, an entity's investments that have deteriorated in value in February and March 2020, but which were not considered overvalued as at 31 December 2019 [MFRS 110.11].

A4.1.4 Entities need to exercise considerable judgement in respect of the events surrounding COVID-19, particularly for periods ending on and around 31 December 2019. In general terms, little was known about COVID-19 as at 31 December 2019, and nothing would have been known about the forthcoming government restrictions on movements and physical distancing that have been introduced since early 2020. Accordingly, it would be generally expected that the impacts of COVID-19 would not be adjusting events for periods ending on 31 December 2019.

A4.1.5 For reporting periods ending subsequent to December 2019, such as 31 March 2020, COVID-19 might have resulted in asset impairments. By the time the financial statements are authorised for issue, the impacts of COVID-19 since 31 March 2020 may be clearer and might provide information indicating that assets were impaired as at the end of the reporting period.

Q5 Might income tax assets and liabilities be affected?

A5.1 Temporary differences

A5.1.1 MFRS 112 *Income Taxes*, paragraph 15 says (in part):

> *15 A deferred tax liability shall be recognised for all taxable temporary differences, except to the extent that the deferred tax liability arises from:*
>
> *(a) the initial recognition of goodwill; or*
>
> *(b) the initial recognition of an asset or liability in a transaction which:*
>
> *(i) is not a business combination; and*
>
> *(ii) at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss).*

A5.1.2 There may be asset impairments and other expenses recognised for accounting purposes that are not deductible for tax purposes in the same period. Accordingly, new temporary differences may emerge as a result of the impacts of COVID-19.

A5.2 Deferred tax assets

A5.2.1 MFRS 112 *Income Taxes*, paragraph 24 says (in part):

> *24 A deferred tax asset shall be recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised, …*

A5.2.2 An entity with deferred tax assets in respect of temporary differences may need to review the likelihood of sufficient future profits being available against which those assets might be recovered. In assessing probability of recovery, judgement would need to be exercised in considering the current circumstances and the prospects of medium to long-term recovery.

A5.3 Deferred tax liabilities

A5.3.1 MFRS 112 *Income Taxes*, paragraph 39 says (in part):

> *39 An entity shall recognise a deferred tax liability for all taxable temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint arrangements, except to the extent that both of the following conditions are satisfied:*
>
> *(a) the parent, investor, joint venturer or joint operator is able to control the timing of the reversal of the temporary difference; and*
>
> *(b) it is probable that the temporary difference will not reverse in the foreseeable future.*

A5.3.2 Recent events may mean that an entity which previously did not expect a temporary difference in an investee to reverse in the foreseeable future is now faced with such a reversal being probable. For example, the recently changed circumstances might mean an investor is now having to repatriate dividends that it had previously planned to retain in the investee entity.

Q6 Might the accounting for property, plant and equipment be affected?

A6.1 Carrying amounts and useful lives

A6.1.1 MFRS 116 *Property, Plant and Equipment*, paragraph 6 includes the following definitions:

> *Carrying amount is the amount at which an asset is recognised after deducting any accumulated depreciation and accumulated impairment losses.*
>
> *Depreciable amount is the cost of an asset, or other amount substituted for cost, less its residual value.*

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Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

Recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

Useful life is:

(a) the period over which an asset is expected to be available for use by an entity; or

(b) the number of production or similar units expected to be obtained from the asset by an entity.

A6.1.2 The carrying amounts of some property, plant and equipment might be affected by recent events for one or more of the following.

(a) The carrying amount may be above the recoverable amount due to current conditions, which would lead the entity to impair the relevant assets. This could be the result of decrements in fair value less costs of disposal and value in use and/or in the residual value.

(b) The residual value of an asset may have fallen.

A6.1.3 The entity would need to consider an appropriate timeframe in judging whether any of these changes are relevant. For example, when measuring value in use, an entity would consider likely economic conditions over the remaining useful life of the asset.

A6.2 Revaluations

A6.2.1 MFRS 116.29 and 31 say:

29 An entity shall choose either the cost model in paragraph 30 or the revaluation model in paragraph 31 as its accounting policy and shall apply that policy to an entire class of property, plant and equipment.

31 After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.

A6.2.2 An entity that applies the revaluation model to a class of assets, would need to consider whether the fair values for any of those assets are materially different from their carrying amounts in light of the current circumstances for the whole class of assets [MFRS 116.36].

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Q7 Could there be impacts on employee benefit costs and liabilities?

A7.1 Short-term benefits

A7.1.1 MFRS 119 *Employee Benefits*, paragraph 13 says:

> *13 An entity shall recognise the expected cost of short-term employee benefits in the form of paid absences under paragraph 11 as follows:*
>
> *(a) in the case of accumulating paid absences, when the employees render service that increases their entitlement to future paid absences.*
>
> *(b) in the case of non-accumulating paid absences, when the absences occur.*

A7.1.2 Work absences may increase in the current environment, which may have a number of differing impacts on an employer's obligations to employees, depending on the circumstances.

A7.1.3 In some cases, entities may grant special paid (or partly-paid) leave as a way of retaining key employees, which would be recognised as expenses when they are incurred. In many cases, employees are being retained but compelled to take previously accumulated leave, which would be adjusted against that relevant leave liability.

A7.2 Profit-sharing and bonuses

A7.2.1 MFRS 119.19 says:

> *19 An entity shall recognise the expected cost of profit-sharing and bonus payments under paragraph 11 when, and only when:*
>
> *(a) the entity has a present legal or constructive obligation to make such payments as a result of past events; and*
>
> *(b) a reliable estimate of the obligation can be made.*
>
> *A present obligation exists when, and only when, the entity has no realistic alternative but to make the payments.*

A7.2.2 Previously accrued amounts expected to be paid to employees under profit-sharing and bonus schemes may need to be partially or fully reversed as the current conditions mean the entity is no longer obligated to pay some or all of the previously accrued amounts. In some cases, an entity will be unable to make a reliable estimate of any liability for profit-sharing and bonus schemes due to the high degree of uncertainty about whether the conditions (such as a particular level of profits) will be achieved.

A7.3 Post-employment benefits – plan assets

A7.3.1 Defined contribution post-employment plans are effectively pay-as-you-go arrangements for an employer. However, for defined benefit plans, an employer bears the investment risk, which can leave an employer with a liability for post-employment benefits.

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A7.3.2 MFRS 119.58 says:

> 58 *An entity shall determine the net defined benefit liability (asset) with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the end of the reporting period.*

A7.3.3 Current conditions may cause a reduction in the carrying amounts of plan assets, which are required to be at fair value [MFRS 119.113], meaning that a net deficit may have emerged or grown larger than previously assessed. Worse than expected investment performance gives rise to a lower than expected return on plan assets and the impacts of this would be recognised in other comprehensive income [MFRS 119.120(c)].

A7.4 Post-employment benefits – assumptions

A7.4.1 Post-employment defined benefit obligations (and other similar long-term employee benefits) would generally be measured using assumptions about future wages and assumptions about employee demographics (including rates of employee turnover) [MFRS 119.76, 77 & 87]. (Under MFRS 119.154, other long-term employee benefits may also be measured using discounted cash flows techniques in a manner similar to post-employment benefits.) Post-employment defined benefit obligations (and other similar long-term employee benefits) are discounted using market yields at the end of the reporting period based on high-quality corporate bonds (or government bonds denominated in that currency when a deep market in high-quality corporate bonds does not exist) [MFRS 119.83].

A7.4.2 Recent events may affect each of these assumptions and therefore affect the amount of long-term employee benefit liabilities. For example, assumed salary increases may now be much lower (which would tend to lower the liability) and discount rates might be lower (which would tend to increase the liability).

A7.4.3 MFRS 119.145 says:

> 145 *An entity shall disclose:*
>
> *(a) a sensitivity analysis for each significant actuarial assumption (as disclosed under paragraph 144) as of the end of the reporting period, showing how the defined benefit obligation would have been affected by changes in the relevant actuarial assumption that were reasonably possible at that date.*
>
> *(b) the methods and assumptions used in preparing the sensitivity analyses required by (a) and the limitations of those methods.*
>
> *(c) changes from the previous period in the methods and assumptions used in preparing the sensitivity analyses, and the reasons for such changes.*

A7.4.4 Historically, a sensitivity analysis may have involved small reasonably possible changes in assumptions. Current events may cause an entity to regard increasingly large possible changes in assumptions as being reasonable. Accordingly, there may be a number of disclosures that need to be made to comply with MFRS 119.145(c).

Q8 Might MFRS 120 be relevant in accounting for some forms of government relief?

A8.1 Recognition of grants

A8.1.1 Some entities may find that they are, for the first time, in receipt of government grants or other government assistance due to impacts of recent events. Those entities may not be acquainted with MFRS 120 *Accounting for Government Grants and Disclosure of Government Assistance*.

A8.1.2 MFRS 120.3 includes the following definitions.

> *Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria.*
>
> *Government assistance for the purpose of this Standard does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.*
>
> *Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.*
>
> *Grants related to assets are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held.*
>
> *Grants related to income are government grants other than those related to assets.*

A8.1.3 Some forms of government assistance may fall within the scope of MFRS 120. Government grants are recognised only when there is reasonable assurance that: (a) the entity will comply with the conditions attaching to them; and (b) the grants will be received [MFRS 120.7].

A8.1.4 Once the entity has reasonable assurance it will meet the conditions attaching to grants and will receive the grants, by way of illustration:

(a) government grants that are intended to support continuing salaries for idle or under-utilised staff would be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the salaries it pays to those staff [MFRS 120.12]; and

(b) government grants related to assets are presented in the statement of financial position either by setting up the grant as deferred income or by

deducting the grant in arriving at the carrying amount of the asset [MFRS 120.24].

A8.1.5 Government grants do not include other forms of government assistance which cannot reasonably have a value placed upon them, such as the provision of guarantees. However, it would be necessary for an entity to consider disclosure of the nature, extent, and duration of the assistance because such disclosure may be necessary in order for the financial statements not to be misleading [MFRS 120.36].

A8.1.6 MFRS 120.39 also requires disclosures about government grants, including in respect of government grants related to assets, the accounting policy choice applied.

Q9 Might the capitalisation of borrowing costs be affected under a loan repayment moratorium?

A9.1 Identifying borrowing costs

A9.1.1 An entity that has borrowings costs that are directly attributable to the acquisition, construction or production of a qualifying asset would be recognising them as part of the cost of that asset in accordance with MFRS 123 *Borrowing Costs* [in particular, see MFRS 123.8].

A9.1.2 If the loan repayments are suspended for a period, but interest continues to accrue on the outstanding balance and the relevant acquisition, construction or production activity continues, the accrued interest would be a borrowing cost. This is because the borrowing costs continue to be incurred. In the (probably unlikely) circumstances that interest does not continue to accrue because there is an interest 'holiday', then no borrowing costs would be incurred and, therefore, there would be no interest to be capitalised to the qualifying asset.

A9.2 Suspension of activity

A9.2.1 In the circumstance that recent events mean the entity must suspend its acquisition, construction, or production activity in respect of qualifying assets for an extended period, the entity would also suspend capitalisation of borrowing costs [MFRS 123.20]. Any interest that continues to accrue is a cost of holding partially completed assets and does not qualify for capitalisation. Instead it would be recognised as an expense as incurred.

A9.2.2 Judgement would need to be applied to determine what constitutes a suspension of activity. When an entity is still carrying out substantial technical and administrative work on a qualifying asset it would not normally suspend capitalisation of borrowing costs [MFRS 123.21].

A9.2.3 Judgement would also need to be applied to determine whether a suspension is for an 'extended period'.

Q10 Are there potential issues to be addressed for investments in associates and joint ventures?

A10.1 Equity method – losses on investments in associates or joint ventures

A10.1.1 MFRS 128 *Investments in Associates and Joint Ventures* generally requires investors to account for their interests in associates and joint ventures by applying the equity method [MFRS 128.10].

A10.1.2 On acquiring its investment, when the cost is greater than the investor's share of the net fair value of the investee's identifiable assets and liabilities, the difference is accounted for as goodwill. When the net fair value acquired exceeds the cost, the difference is recognised in profit or loss [MFRS 128.32].

A10.1.3 There are effectively two ways in which losses might need to be recognised in respect of interests in associates and joint ventures:

(a) losses from the activities of the associates or joint ventures themselves (recognised via application of the equity method); and

(b) impairment of investments in associates or joint ventures.

A10.1.4 Losses recognised using the equity method that are in excess of the investor's investment in ordinary shares are applied to the other components of the entity's interest in an associate or a joint venture in the reverse order of their seniority (that is, priority in liquidation) [MFRS 128.38]. Once an investor's interest is reduced to zero, additional losses are provided for, and a liability is recognised, only to the extent that the entity has incurred legal or constructive obligations or made payments on behalf of the associate or joint venture. If the associate or joint venture subsequently reports profits, the entity resumes recognising its share of those profits only after its share of the profits equals the share of losses not recognised [MFRS 128.39].

A10.1.5 After the equity method is applied, in the event that there remains a positive investment in an associate or joint venture, objective evidence is considered to determine whether an investment in an associate or joint venture is impaired. The investment is considered as a single unit of account, including any goodwill [MFRS 128.42]. That is, the investment as a whole is tested for impairment under MFRS 136 *Impairment of Assets* (goodwill is not tested separately).

A10.1.6 The recoverable amount of an investment in an associate or a joint venture is assessed for each associate or joint venture, unless the associate or joint venture does not generate cash inflows from continuing use that are largely independent of those from other assets of the investor [MFRS 128.43].

Q11 Are there interim reporting issues that should be considered?

A11.1 Significant events since last annual period end

A11.1.1 MFRS 134 *Interim Financial Reporting*, paragraph 15 requires an entity to include in its interim financial report an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the entity since the end of the last annual reporting period. Information disclosed in relation to those events and transactions updates the relevant information presented in the most recent annual financial report.

A11.1.2 Recent events may have had a significant impact on an entity's financial position and performance. If that is the case, interim financial reports for each quarter or the half year in 2020 would need to explain the impacts of events since the 31 December 2019 annual report for entities reporting on a calendar financial year basis.

A11.1.3 MFRS 134.15B provides a non-exhaustive list of matters that might need to be disclosed. Given the wide variety of impacts on entities of COVID-19, entities would need to consider whether there are any additional disclosures specific to its circumstances (that are not mentioned in MFRS 134.15B) that need to be made to explain changes in financial position and performance of the entity since the last annual reporting period end.

A11.2 Year-to-date measurements

A11.2.1 MFRS 134.28 says (in part):

> 28 *… the frequency of an entity's reporting (annual, half-yearly, or quarterly) shall not affect the measurement of its annual results. To achieve that objective, measurements for interim reporting purposes shall be made on a year-to-date basis.*

A11.2.2 The current rapidly changing environment may cause an entity to change its views on a range of matters throughout an annual reporting period. For example, a contract might be assessed to be onerous in quarter two of a calendar reporting period and a loss recognised, while being assessed not to have been onerous by the end of quarter three. The quarter three financial report would not include the impact of the contract being onerous at the end of quarter two because the loss would be reversed in quarter three and the contract is not onerous on a year-to-date basis. (Goodwill impairment is an exception to this principle – see Section A12.2.)

Q12 How will the application of non-financial asset impairment requirements be impacted?

A12.1 Impairment indicators, testing and loss recognition

A12.1.1 MFRS 136 *Impairment of Assets* requires entities to consider whether there is one or more indicators of impairment for most assets [MFRS 136.9]. In the event there is an indication of impairment, impairment testing must be

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performed. Some assets are automatically tested annually for impairment, such as intangible assets with indefinite useful lives and goodwill acquired in a business combination [MFRS 136.10].

A12.1.2 External impairment indicators include observable asset value declines and significant adverse market conditions [MFRS 136.12]. Internal impairment indicators include events that have an adverse effect on the actual or expected use of assets, including assets being idle [MFRS 136.12]. In the current environment, an overall contraction in demand for the entity's goods and services might be an impairment indicator.

A12.1.3 Accordingly, it would be expected that many entities will be performing unprecedented levels of impairment testing in 2020.

A12.1.4 MFRS 136.6 includes the following definition:

> *The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs of disposal and its value in use.*

A12.1.5 When the recoverable amount is less than an asset's carrying amount, the asset is written down [MFRS 136.59] and an impairment loss recognised [MFRS 136.60]. The current circumstances may also be likely to result in significant asset impairments being recognised for some entities, depending on how their businesses are being affected by COVID-19.

A12.1.6 Some assets are part of a cash-generating unit and the requirements around impairment indicators, impairment testing and impairment loss recognition are conducted for the CGU as a whole [MFRS 136.66 to 108].

A12.2 Impairment reversals

A12.2.1 Once the prevailing conditions improve, entities would need to consider whether there are indicators of impairment reversal.

A12.2.2 To the extent there is a change in estimates used to determine an asset's recoverable amount since an impairment was recognised, due to the conditions which gave rise to an impairment being reversed, impairment write downs and losses are reversed up to the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior periods [MFRS 136.117]. However, goodwill impairment is never reversed [MFRS 136.124].

Q13 What will be the impact for provisions and contingent assets and liabilities?

A13.1 Provisions

A13.1.1 MFRS 137 *Provisions, Contingent Liabilities and Contingent Assets*, paragraph 10 includes the following definition:

> *A provision is a liability of uncertain timing or amount.*

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A13.1.2 A provision is recognised when:

(a) the entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation [MFRS 137.14].

A13.1.3 In the current environment, new provisions may need to be recognised. Examples might include the following:

(a) Some of an entity's existing business activities may need to be restructured, including business closures. Those closures might involve employee retrenchments that trigger a need to make future retrenchment payments, which would be recognised in a provision when there is a detailed formal plan for a restructuring and management has raised a valid expectation in the affected employees that the plan will be implemented [MFRS 137.72].

(b) An entity may have entered into long-term contracts to receive goods or services that the entity can no longer use, but must continue to pay for. Those contracts may have become onerous and a provision may need to be recognised.

A13.2 Contingent liabilities

A13.2.1 MFRS 137.10 includes the following definition:

> *A contingent liability is:*
>
> *(a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or*
>
> *(b) a present obligation that arises from past events but is not recognised because:*
>
> *(i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or*
>
> *(ii) the amount of the obligation cannot be measured with sufficient reliability.*

A13.2.2 Contingent liabilities are not recognised [MFRS 137.27]. Instead, contingent liabilities that are not remote are disclosed [MFRS 137.86], including a brief description of the nature of the contingent liability and, where practicable:

(a) an estimate of its financial effect;

(b) an indication of the uncertainties relating to the amount or timing of any outflow; and

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(c) the possibility of any reimbursement.

A13.2.3 In the current environment, entities may be disclosing contingent liabilities, on the basis that there are possible obligations arising from COVID-19 events to date, but when the obligation will only be confirmed by future events. For example, an entity that has contracted to lease premises that it has been prevented by government restrictions from occupying and that the entity can terminate based on a force majeure clause. There may currently be uncertainty about whether the entity will need to follow through with the contract in this example.

Q14 What will be the impact for intangible assets?

A14.1 New or enhanced intangible assets

A14.1.1 MFRS 138 *Intangible Assets*, paragraphs 21 and 22 say:

> *21 An intangible asset shall be recognised if, and only if:*
>
> *(a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and*
>
> *(b) the cost of the asset can be measured reliably.*
>
> *22 An entity shall assess the probability of expected future economic benefits using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset.*

A14.1.2 Some entities, particularly those in office-based service industries might be in the process of enhancing their capacity to have employees working from home in the current environment. In some cases, new systems are being created, such as new software platforms that might constitute recognisable intangible assets.

A14.1.3 In other cases, entities may be making greater use of subscriptions to software as a service, platforms as a service, infrastructure as a service and information technology management as a service. These are not assets of the subscribing entity, unless the entity has prepaid for the services.

A14.2 Impairment of intangible assets and useful life

A14.2.1 The carrying amounts of some intangible assets might be affected by recent events for one or more of the following:

(a) changes to useful lives – for example, an intangible asset previously thought to have an indefinite useful life may now thought to have a finite useful life;

(b) the carrying amount may be above the recoverable amount due to current conditions, which would lead the entity to impair the relevant assets.

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A14.2.2 The entity would need to consider an appropriate timeframe in judging whether an intangible asset is impaired. For example, when measuring value in use of a long-lived intangible asset, an entity would consider economic conditions over the remaining useful life of the asset.

Q15 How might investment property be impacted?

A15.1 Fair value model accounting

A15.1.1 MFRS 140 *Investment Property*, paragraph 30 permits an entity to choose to subsequently measure investment property using the fair value model or the cost model. There are property investment entities in Malaysia that apply the fair value model under which a gain or loss arising from a change in the fair value of investment property is recognised in profit or loss for the period in which it arises [MFRS 140.35].

A15.1.2 In many cases, broad-based COVID-19-related government actions have meant that some investment properties may have lost value because, for example, some tenants are unable to pay their rent. There may be a high level of uncertainty about the extent and length of impacts of government actions that might supress property values. Accordingly, managements will need to exercise judgement in determining whether their entities will need to recognise losses on investment property, particularly given that some investment property is being held for long-term capital appreciation rather than for short-term sale in the ordinary course of business [MFRS 140.8(a)].

A15.1.3 While there is a rebuttable presumption that an entity can reliably measure the fair value of an investment property on a continuing basis [MFRS 140.53], a possible concern is that information about current investment property value may be much more limited than is typically the case. However, even if comparable market transactions become less frequent or market prices become less readily available, the entity is required to continue to measure the property at fair value until disposal (or until the property becomes owner-occupied property, or the entity begins to develop the property for subsequent sale in the ordinary course of business) [MFRS 140.55].

A15.1.4 There are only very limited circumstances in which an entity that has a policy of applying the fair value model to its investment property would be justified in applying the cost model, for example, when an existing property controlled by the entity is first reclassified as an investment property when there is a change in use. There would need to be clear evidence when the investment property is first reclassified that the fair value of the property is not reliably measurable, for example, because the market for comparable properties is inactive and alternative reliable measurements of fair value (for example, based on discounted cash flow projections) are not available [MFRS 140.53].

A15.2 Cost model accounting

A15.2.1 The cost model involves applying:

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(a) MFRS 5 to investment property that meets the criteria to be classified as held for sale (or is included in a disposal group that is classified as held for sale);

(b) for lessees, MFRS 16 *Leases* to a right-of-use over an investment property; and

(c) MFRS 116 for all other investment property.

A15.3 Third-party compensation

A15.3.1 In the event that an entity receives compensation from a third party, for example, due to an impairment of an investment property, that compensation is recognised in profit or loss when it becomes receivable [MFRS 140.72]. For example, an entity may suffer a loss due to tenants being unable to pay rents and be compensated under a loss of rent insurance contract.

A15.3.2 There may be cases of the impairment or loss being evident and being recognised as an expense in the current reporting period, while the entity's entitlement to compensation is not clear and might meet the definition of a 'contingent asset', which is not recognised [MFRS 137.31], but would be the subject of disclosures [MFRS 137.89]. A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity [MFRS 137.10].

Q16 How might share-based payments be affected?

A16.1 Measurement of share-based payment transactions

A16.1.1 MFRS 2 *Share-based Payment* requires goods or services acquired through share-based payments to be recognised when the entity obtains the goods or as the entity receives services. A corresponding increase in equity is recognised if the goods or services were received in an equity-settled share-based payment transaction [MFRS 2.7]. When the goods or services received or acquired in a share-based payment transaction do not qualify for recognition as assets, they are recognised as expenses [MFRS 2.8].

A16.1.2 For equity-settled share-based payment transactions, the goods or services received and the corresponding increase in equity are both measured at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the fair value of goods or services cannot be estimated reliably, the goods or services received and the corresponding increase in equity are measured indirectly, by reference to the fair value of the equity instruments granted.

A16.1.3 The fair value of equity instruments is determined at the 'measurement date' [MFRS 2.16]. For transactions with employees and others providing similar services, the measurement date is grant date. For transactions with parties other than employees (and those providing similar services), the measurement date is the date the entity obtains the goods or the counterparty renders service.

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A16.1.4 Given the recent volatility of quoted equity prices, an entity measuring goods or services indirectly by reference to the fair value of equity instruments granted might experience a high level variability in the amounts recognised for similar goods obtained or services received from day-to-day.

A16.2 Equity instruments granted

A16.2.1 Employees are often granted options over the acquisition of shares in the entities that employ them as part of their remuneration. Those options are valued at the grant date [MFRS 2.16] using an option pricing model (if traded options with similar terms and conditions do not exist). Those option pricing models take into account, as a minimum, the following factors, [MFRS 2.B6]:

(a) the exercise price of the option;

(b) the life of the option;

(c) the current price of the underlying shares;

(d) the expected volatility of the share price;

(e) the dividends expected on the shares (if appropriate); and

(f) the risk-free interest rate for the life of the option.

A16.2.2 A number of these factors may have been affected by recent events, in particular, the current share price, expected volatility of the share price, and expected dividends.

A16.2.3 In measuring grants currently being made, careful consideration would need to be given to expectations over the life of the options, not simply the existing conditions. MFRS 2.24 acknowledges that, in rare cases, the entity may be unable to estimate reliably the fair value of the equity instruments granted. In these rare cases only, the entity:

(a) measures the equity instruments at their intrinsic value,[3] initially at the date the entity obtains the goods or the counterparty renders service and subsequently at the end of each reporting period and at the date of final settlement, with any change in intrinsic value recognised in profit or loss; and

(b) recognises the goods or services received based on the number of equity instruments that ultimately vest or (where applicable) are ultimately exercised.

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3 Intrinsic value = The difference between the fair value of the shares to which the counterparty has the (conditional or unconditional) right to subscribe or which it has the right to receive, and the price (if any) the counterparty is (or will be) required to pay for those shares. For example, a share option with an exercise price of CU15 on a share with a fair value of CU20, has an intrinsic value of CU5.

Q17 How might business combinations be affected?

A17.1 Contingent consideration

A17.1.1 MFRS 3 *Business Combinations* requires an acquirer of a business to recognise the value of contingent consideration as part of the consideration transferred in exchange for the acquiree [MFRS 3.39]. Contingent consideration is usually an obligation of the acquirer to transfer additional assets or equity interests to the former owners of an acquiree as part of the exchange for control of the acquiree if specified future events occur or conditions are met. An example would be an additional payment contingent on the acquired entity achieving a particular sales target.

A17.1.2 MFRS 3.58 distinguishes between:

(a) changes in the fair value of contingent consideration that the acquirer recognises after the acquisition date that result from additional information obtained after that date about facts and circumstances that existed at the acquisition date – these are 'measurement period adjustments'; and

(b) changes resulting from events after the acquisition date, such as meeting an earnings target, reaching a specified share price, or reaching a milestone on a research and development project – these are not measurement period adjustments.

A17.1.3 Measurement period adjustments are adjustments to provisional amounts recognised for a business combination (and can change goodwill etc.). These adjustments can be made up to 12 months after the acquisition date [MFRS 3.45].

A17.1.4 Changes in the fair value of contingent consideration that relate to events subsequent to the acquisition date (that are not measurement period adjustments) are accounted for as follows [MFRS 3.58]:

(a) contingent consideration classified as equity is not to be remeasured and its subsequent settlement is accounted for within equity;

(b) contingent consideration that is not equity and is:

(i) within the scope of MFRS 9 is measured at fair value at each reporting date and changes in fair value recognised in profit or loss under MFRS 9;

(ii) not within the scope of MFRS 9 is measured at fair value at each reporting date and changes in fair value recognised in profit or loss.

A17.1.5 If the acquisition date is prior to a time when the transacting parties had knowledge of COVID-19, and contingent consideration depends on meeting targets after the acquisition date that will be affected by events surrounding

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COVID-19, there may be adjustments to the fair value of the contingent consideration which need to be recognised in profit or loss.

Q18 How might the accounting for non-current assets held for sale and discontinued operations be relevant?

A18.1 Assets held for sale and disposal groups

A18.1.1 The events surrounding COVID-19 may result in an entity changing the way it classifies and measures assets and liabilities.

A18.1.2 For example, non-current assets that were previously deployed to make a product sold for profit might now be idle because demand for the product has fallen dramatically. If that means the carrying amounts will be principally recovered through a sale, the relevant assets would need to be classified as held for sale and measured at the lower of its carrying amount and fair value less costs to sell [MFRS 5.15], with any impairment loss recognised in profit or loss [MFRS 5.20].

A18.1.3 Although less common, there may be cases when previously under-utilised assets that had been held for sale might be re-purposed to produce a product that is in demand due to events surrounding COVID-19. In that case, some impairment losses may be reversed and assets values restated and the assets reclassified as non-current.

A18.2 Discontinued operations

A18.2.1 In some cases, the events surrounding COVID-19 might result in a disposal group that is either a major line of business or geographical area of operations, or is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations. In those cases, the entity classifies the disposal group as a discontinued operation [MFRS 5.32].

A18.2.2 There are specific presentation and disclosure requirements that apply to discontinued operations, including separate disclosure of:

(a) the post-tax profit or loss of discontinued operations [MFRS 5.33(a)(i)], analysed into various components [MFRS 5.33(b)];

(b) the post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation [MFRS 5.33(a)(ii)];

(c) earnings per share in respect of discontinued operations [MFRS 133 *Earnings per Share*, paragraph 68].

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Q19 How might financial instrument disclosures be affected?

A19.1 Market risks – sensitivity analysis

A19.1.1 Under MFRS 7 *Financial Instruments: Disclosures*, when relevant, entities must disclose some form of sensitivity analysis in respect of financial assets and liabilities for the various types of market risk [MFRS 7.40 and 41]. The types of market risk are currency risk, interest rate risk and other price risk. The sensitivities to which the entity is exposed at the end of the reporting period are those which are reasonably possible at that date.

A19.1.2 Changes from the previous period in the methods and assumptions used, and the reasons for such changes, must be disclosed. Given that the level of volatility may be much greater for reporting periods ending during times affected by events surrounding COVID-19, it would be expected that some entities will need to disclose information about the facts and circumstances that led to a changed level of volatility being applied.

Q20 Are there implications for operating segment reporting?

A20.1 Reliance on major customers

A20.1.1 MFRS 8 *Operating Segments*, when relevant, requires an entity to provide information about the extent of its reliance on its major customers. When revenues from transactions with a single external customer amount to 10% or more of an entity's revenues, the entity discloses that fact, the total amount of revenues from each such customer, and the identity of the segment or segments reporting the revenues [MFRS 8.34].

A20.1.2 A group of entities known to a reporting entity to be under common control is considered a single customer. However, judgement is required to assess whether a government (including government agencies and similar bodies whether local, national or international) and entities known to the reporting entity to be under the control of that government are considered a single customer. In assessing this, the reporting entity considers the extent of economic integration between those entities.

A20.1.3 The impacts of COVID-19 can include major shifts in an entity's customer base. In some cases, an entity might find it is supplying a large proportion of its goods or services to a government entity that has intervened to ensure the continued supply of essential services. For example, a medical supplies entity might find itself selling mainly to government-operated hospitals for a prolonged period.

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Q21 Are there implications for financial instrument accounting?

A21.1 Expected credit loss model[4]

A21.1.1 Under MFRS 9 *Financial Instruments*, many loan and financing receivables are measured at amortised cost and some financial assets are investments measured at fair value through other comprehensive income (FVOCI). These assets are subject to the recognition of expected credit losses.

A21.1.2 On initial recognition, a loss allowance of *12-month expected credit losses* is recognised, based on the risk of a default occurring in the next 12 months [MFRS 9.5.5.5]. At a subsequent reporting date, if the credit risk on those financial assets has increased significantly since initial recognition, the loss allowance is equal to the *lifetime expected credit losses*, based on the risk of a default occurring over the entire expected remaining lives of the receivables [MFRS 9.5.5.3].

A21.1.3 In measuring expected credit losses, an entity considers all reasonable and supportable information, including forward-looking information [MFRS 9.5.5.4]. Reasonable and supportable information is that which is reasonably available at the reporting date without undue cost or effort, including information about past events, current conditions and forecasts of future economic conditions [MFRS 9.B5.5.49], and judgement needs to be exercised in measuring expected credit losses [MFRS 9.B5.5.50].

A21.1.4 In view of the unprecedented speed with which events have been unfolding amidst the COVID-19 outbreak, in determining whether they have reasonable and supportable information that is available without undue cost or effort to make forecasts of future economic conditions, entities need to make a judgement based on the information on-hand, which is believed to be still limited under the current unprecedented circumstances. Accordingly, reporting entities may need to adapt the information they already possess on potential scenarios involving a general deterioration in credit risks.

A21.1.5 Given the inherent level of uncertainty and the sensitivity of judgements and estimates, sufficient disclosures of the key assumptions used, and the judgements made in estimating the expected credit losses above are particularly important in the financial statements of reporting entities.

A21.1.6 Reporting entities are reminded that they are required to incorporate forecasts of future conditions over the entire remaining expected life of a financial instrument only to the extent of the availability of reasonable and supportable information in estimating *lifetime expected credit losses*.

A21.1.7 In the event that forecasts are made to measure expected credit losses, reporting entities take into account the range of information available, including the expected impacts of government measures to mitigate the

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4 Please also see MASB Media Release (25 March 2020) on COVID-19: MFRS 9 *Financial Instruments: Expected Credit Loss Considerations*.

effects of the expected challenges, the expected duration and the extent of the current challenging conditions.

A21.1.8 It is likely to be difficult at this time to incorporate the specific effects of COVID-19 and government support measures on a reasonable and supportable basis. However, changes in economic conditions should be reflected in macroeconomic scenarios applied by entities and in their weightings. If the effects of COVID-19 cannot be reflected in models, post-model overlays or adjustments would need to be considered. The environment is subject to rapid change and current information should continue to be monitored.

A21.1.9 Ordinarily, modifications or rescheduling / restructuring of receivables undertaken by a lender would automatically indicate a significant increase in credit risk and the need to recognise loss allowances for lifetime expected credit losses. However, in the current environment, in which regulatory action may be driving payment moratoriums, it may not be appropriate to simply assume that rescheduling / restructuring, of itself, would necessarily mean that *lifetime expected credit losses* are relevant for all receivables. In addition, consideration would need to be given to whether the payment moratoriums could enable the obligors who are affected by the COVID-19 outbreak to resume regular payments in foreseeable future, which would affect the potential amount of any *lifetime expected credit losses*.

A21.2 Modification of cash flows

A21.2.1 For some fixed rate contracts, a repayment moratorium period has been introduced under which the same payments must be made as originally agreed, but each of the payments is to be made later than originally agreed. In this scenario, there is an economic loss because, although a financial institution may be no less likely to receive all the relevant instalments as they would in the absence of the moratorium, they are forgoing interest/profit rate for the moratorium period on the outstanding amounts.

A21.2.2 Depending on the circumstances, the deferral of cash flows associated with the moratorium might also give rise to a 'modification of contractual cash flows' under MFRS 9.5.4.3, which would require the recognition of a modification gain or loss in profit or loss, determined using the original effective interest rate.

A21.3 Hedging relationships

A21.3.1 The events surrounding COVD-19 might distort some relationships previously designated as hedge relationships. For example, there may be cases when there is no longer an economic relationship between the hedged item and the hedging instrument, or the effect of credit risk starts to dominate the value changes that result from that economic relationships. In those cases, a hedging relationship is discontinued in its entirety [MFRS 9.B6.5.26(c)].

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Q22 How might fair value measurements be affected?

A22.1 Fair value measurement

A22.1.1 MFRS 13 *Fair Value Measurement* does not require fair value measurement to be applied – instead it provides the framework for determining fair value when another MFRS requires or permits fair value measurement.

A22.1.2 MFRS 13.9 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A fair value measurement assumes that the asset or liability is exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date under current market conditions [MFRS 13.15].

A22.1.3 The events surrounding COVID-19 may mean that the markets normally considered when determining fair values are less liquid (that is, they have fewer, if any, trades). This, in turn, may necessitate determining fair values using fewer observable inputs and, for example, having to use more 'level 3' inputs in valuation techniques [MFRS 13.67 to 90], including information generated by the entity itself.

A22.1.4 The entity would need to ensure that it updates the information included in its notes to the financial statements because the inputs and valuation techniques used in determining fair value measurements (which may be different from previous reporting periods) must be disclosed [MFRS 13.91].

Q23 What might be the impacts on revenue recognition?

A23.1 Refund liabilities

A23.1.1 An entity that receives consideration from customers in respect of providing a good or service is required to recognise a refund liability if the entity expects to refund some or all of that consideration to those customers [MFRS 15.55]. This might arise because COVID-19-related government restrictions mean the entity is unable to meet some or all of the relevant performance obligations to their fullest extent.

A23.1.2 A refund liability is measured at the amount of consideration received (or receivable) for which the entity does not expect to be entitled, and these amounts are not included in the transaction price. The refund liability (and corresponding change in the transaction price and, therefore, the contract liability) is updated at the end of each reporting period for changes in circumstances. That is, there could be a reclassification from 'contract liability' to 'refund liability'.

A23.1.3 Previously recognised refund liabilities might need to be remeasured, or refund liabilities may need to be recognised for the first time, if the impacts of COVID-19 make the prospect of refunds more likely. For example, as a gesture of good faith, a supplier may agree to take back previously supplied goods that the customer is currently unable to use.

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A23.1.4 As further impacts of COVID-19 have become apparent and change over time, an entity would need to update its refund liabilities, where refunds are considered to be relevant.

A23.2 Non-refundable amounts

A23.2.1 Many industries involve accepting fully or partially non-refundable consideration in advance of providing the relevant goods or services. For example, the airline industry, tourist accommodation industry and tour operators all commonly take bookings and deposits, and sometimes full payment, in advance and all these industries have had their activities curtailed or stopped due to the events surrounding COVID-19.

A23.2.2 To the extent that the entity has a policy of not refunding the deposits and the entity is entitled to retain the deposits and will not need to provide the related goods or services, the entity would recognise the deposits as revenue [MFRS 15.B46]. However, the entity would need to take into account the extent to which its usual policies regarding refundability remain applicable – for example, there may be market pressure to show 'good faith' with customers and potentially refund some or all of the deposits.

A23.3 Significant financing components

A23.3.1 In some cases, the entity might be able to retain the consideration received in advance and postpone providing the goods or services (or establish the consideration as a credit against goods or services of a similar value), in anticipation of the impacts of COVID-19 subsiding.

A23.3.2 In this case, depending on the length of the postponement, the entity would need to consider whether there is a significant financing component involved, with a corresponding adjustment to the transaction price, for the effects of the time value of money [MFRS 15.60].

A23.3.3 As a practical expedient, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between when the entity transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less [MFRS 15.63]. For example, if an airline had sold a fare and accepted the consideration on 28 February 2020 for a flight on 27 April 2020, there would initially be no need to recognise a financing component. However, circumstances might change as follows:

(a) On reporting as at 31 March 2020, if the airline has arranged to substitute the original flight for a postponed flight to occur some time after 1 April 2021, an estimate would need to be made about whether and to what extent there is a significant financing component.

(b) On reporting as at 31 March 2020, if the airline has arranged to substitute the original flight for a postponed flight to occur some time up to 30 June 2021, an estimate would not need to be made about whether and to what

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extent there is a significant financing component, because the timing is at the customer's discretion.[MFRS 15.62(a)]

A23.3.4 MFRS 15.119 requires an entity to disclose information about its performance obligations in contracts with customers, including whether contracts have a significant financing component.

A23.4 Variable consideration

A23.4.1 An entity that sells goods or services for amounts that include variable consideration may need to reconsider previous estimates of the amounts to which the entity expects to be entitled in exchange for transferring promised goods or services to customers [MFRS 15.50 & 51].

A23.4.2 For example, an entity may have assumed it would provide a 5% discount from list price to a valued customer; however, due to market pressures created by the impacts of COVID-19, the entity may need to extend a higher discount of, say 20%, in order to foster continued good relations with that customer.

Q24 What might be the impacts on lease accounting?

A24.1 Lease term

24.1.1 The lease term is determined as the non-cancellable period of a lease, together with both:

(a) periods covered by an option to extend the lease if the lessee is reasonably certain to exercise that option; and

(b) periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option [MFRS 16.18].

24.1.2 In assessing whether a lessee is reasonably certain to exercise an option to extend a lease, or not to exercise an option to terminate a lease, an entity considers all relevant facts and circumstances that create an economic incentive for the lessee to exercise the option to extend the lease, or not to exercise the option to terminate the lease [MFRS 16.19].

24.1.3 A lessee reassesses whether it is reasonably certain to exercise an extension option, or not to exercise a termination option, upon the occurrence of either a significant event or a significant change in circumstances that:

(a) is within the control of the lessee; and

(b) affects whether the lessee is reasonably certain to exercise an option not previously included in its determination of the lease term, or not to exercise an option previously included in its determination of the lease term.

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24.1.4 The events surrounding COVID-19 might constitute a significant change in circumstances that would cause a lessee to change its view on a lease term. For example, a retailer that leases its sales premises and is currently closed for business may decide to not exercise an option to extend a lease that it previously intended exercising.

A24.2 Lease modifications

A24.2.1 A 'lease modification' is defined as:

> *A change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease (for example, adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual lease term).*

A24.2.2 On 28 May 2020, the IASB issued an amendment to IFRS 16 *Leases* to permit lessees, as a practical expedient, not to assess whether particular COVID-19-related rent concessions are lease modifications. Instead, lessees electing to apply the practical expedient would account for those rent concessions as if they were not lease modifications.

A24.2.3 The practical expedient applies only when:

(a) 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;

(b) any reduction in lease payments affects only payments originally due on or before 30 June 2021 (for example, a rent concession would meet this condition if it results in reduced lease payments on or before 30 June 2021 and increased lease payments that extend beyond 30 June 2021); and

(c) there is no substantive change to other terms and conditions of the lease.

A24.2.4 The MASB has made the same amendments to MFRS 16[5].

A24.2.5 The following commentary would apply to entities that choose not to adopt the practical expedient or where the practical expedient is not applicable.

A24.2.6 The events surrounding COVID-19 might result in reduced lease payments. For example, because a retail outlet has closed due to government action, the lessee and lessor might agree to reduce the lease payments so that the lessee can remain viable and the lessor retains a customer once the government restrictions are lifted. When the lessor and lessee have negotiated the lower lease payments outside the terms of the lease, it would be a lease modification.

5 MASB issued 'Covid-19-Related Rent Concessions (Amendment to MFRS 16) on 5 June 2020.

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(a) A lessee would need to remeasure the lease liability and right-of-use asset in accordance with MFRS 16.45 and 46.

(b) For a lessor that has a finance lease:

(i) if the lease classification (operating versus finance lease) is unaffected by the modification, the lease receivable might be impaired under MFRS 9 [MFRS 16.80];

(ii) if the lease would have been classified as an operating lease had the modification been in effect at the inception date, the lessor accounts for the lease modification as a new lease from the effective date of the modification; and measures the carrying amount of the underlying asset as the net investment in the lease immediately before the effective date of the lease modification.

(c) For a lessor that has an operating lease, a modification gives rise to a new lease from the effective date of the modification, with any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease [MFRS 16.87].

A24.2.7 In some cases, the negotiation might be judged to be within the original terms of the lease. In those cases, the changes in payments that are not lease modifications and would generally be accounted for as a variable lease payment. In this case, a lessee generally recognises the effect of the rent concession in profit or loss [MFRS 16.38]. For an operating lease, a lessor recognises the effect of a rent concession by recognising lower income from leases.

A24.3 In-substance fixed lease payments

A24.3.1 Lease payments include any in-substance fixed lease payments. In-substance fixed lease payments are payments that may, in form, contain variability but that, in substance, are unavoidable. In-substance fixed lease payments exist, for example, if: (a) payments are structured as variable lease payments, but based on facts and circumstances at the time a lease is first recognised, there is considered to be no genuine variability in those payments. Those payments contain variable clauses that do not have real economic substance [MFRS 16.B42].

A24.3.2 However, clauses in a lease contract that previously seemed of no material consequence might become significant in the facts and circumstances emerging from the impacts of COVID-19. One possible example is an entity that has previously determined that lease payments for retail space that depend on a very low minimal amount of monthly sales is in substance a fixed lease payment. That is, the lessee considered there was no genuine variability in those sales-dependent payments because, when the lease was negotiated, the lessee did not contemplate that its sales would fall below that minimum level. However, due to restrictions associated with COVID-19, that entity's sales may now be zero or close to zero and the lease payments that previously appeared to be in-substance fixed lease payments are no longer payable.

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Q25 What matters might need to be raised in Management Commentary?

A25.1 Commentary content

A25.1.1 All reporting entities are expected to need to discuss the implications for their business of COVID-19 and the related government actions to address COVID-19 within management commentary for any relevant reporting period.

A25.1.2 The commentary may include discussion of:

(a) the entity's strategy for dealing with the circumstances;

(b) risks and opportunities posed for the entity's businesses;

(c) action taken by management to address or mitigate current challenges;

(d) the potential effect on future reported results of the direct impacts of COVID-19 and the related government actions to address COVID-19 and the actions of management to mitigate current challenges.

A25.1.3 The commentary may also need to include whether the entity's businesses are expected to remain viable and, more generally, threats to the entity's status as a going concern.

~ END ~

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The Q&As have been prepared to help constituents understand and respond to COVID-19 financial reporting implications. The matters and examples included in this document are not all inclusive, and the Q&As could be updated with additional and modified information.

While all efforts are made to accurately and fairly present the Q&As, appropriate responses to the issues will depend on each entity's respective facts and circumstances. The Q&As should not be taken as a substitute for the full understanding of MFRSs or any other pronouncements (herein referred as MASB pronouncements) issued by the Board. In the event of any divergence between this document and the MASB pronouncements, the latter should be considered as the authoritative version.