



## Securities Law ADVISORY ■

**JUNE 30, 2020**

### When in Doubt, SEC Wants You to Consider COVID-19 Disclosures

On June 23, 2020, the staff of the Division of Corporation Finance of the Securities and Exchange Commission (SEC) issued [CF Disclosure Guidance: Topic No. 9A](#) to provide additional views of what the staff believes that companies should consider for COVID-19-related business and market disruptions. This guidance supplements [CF Disclosure Guidance Topic No. 9](#), which we discussed in an [earlier client advisory](#).

Additionally, on June 23, 2020, the SEC's Office of the Chief Accountant (OCA) issued a [statement](#) to reiterate its April 3, 2020 statement while highlighting its recent engagement with stakeholders and addressing certain accounting, auditing, and financial reporting issues that arose.

#### **Guidance from Division of Corporation Finance**

The staff continues to monitor companies' disclosures on the effects of COVID-19 on business and has issued new guidance to discuss additional disclosure considerations companies are encouraged to provide to allow investors to evaluate the impact of COVID-19 through the eyes of management.

#### ***Operations***

As companies continue to transition to teleworking arrangements, make changes to supply chain, suspend or modify certain operations, and make other adjustments in response to COVID-19, the SEC encouraged companies to consider how these adjustments and responses are impacting their operations. These operational changes are likely to be material to investors' decision-making and included in a company's disclosure.

#### ***Liquidity and capital resources***

Given liquidity concerns from the unprecedented downturn in economic activity in the second quarter, financing activities have been a significant aspect of a company's COVID-19 response. The staff understands that funding from credit facilities, accessing public and private markets, implementing supplier finance programs, and new or modified customer payment terms have been used to bolster liquidity. These funding sources should be carefully considered for disclosure since they may contain novel terms and structures.

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Disclosures should also discuss how companies are dealing with short- and long-term liquidity and funding risks, particularly to the extent there are new risks or uncertainty to business.

Importantly, the staff noted that although some companies have already been making some of these disclosures in their earning releases, these disclosures have not found their way into MD&A in quarterly reports. The staff directed companies to evaluate the potential materiality of the information and consider including the information in MD&A.

### ***Disclosure questions to consider***

As companies consider disclosure obligations, the staff highlighted a range of questions that could be useful for companies to analyze specific facts and circumstances in fulfilling their disclosure obligations:

- How and to what extent have you altered your operations, such as implementing health and safety policies for employees, contractors, and customers, to deal with these challenges, including challenges related to employees returning to the workplace?
- Are any decreases in cash flow from operations having a material impact on your liquidity position and outlook?
- Have you accessed revolving lines of credit or raised capital in the public or private markets to address your liquidity needs?
- Have COVID-19-related impacts affected your ability to access your traditional funding sources on the same or reasonably similar terms as were available to you in recent periods?
- Are any measures (such as reducing or suspending share repurchase programs or dividend payments and reducing or increasing human capital resource expenditures) temporary, and if so, how long do you expect to maintain them?
- Have you taken advantage of available payment deferrals, forbearance periods, or other concessions? If so, what are the concessions and how long will they last?
- Have you modified other contractual arrangements in response to COVID-19 in such a way that the revised terms may materially impact your financial condition, liquidity, and capital resources?
- Have these arrangements had a material impact on your balance sheet, statement of cash flows, or short- and long-term liquidity and if so, how?
- Have you assessed the potential impact material events may have on your liquidity and capital resources and considered whether subsequent events in the financial statements and known trends or uncertainties in MD&A is required?

Companies and their disclosure committees should consider these questions early in the quarter-closing process to ensure adequate time to assess and address these questions and potential disclosure obligations.

### ***Government assistance – The CARES Act***

Companies receiving federal assistance under the Coronavirus Aid, Relief, and Economic Security (CARES) Act should consider the short- and long-term impacts of the assistance on their financial condition, results

of operations, liquidity, and capital resources. Companies should consider the following questions when evaluating disclosures of government assistance:

- Do the terms and conditions of any assistance received limit your ability to seek other sources of financing or affect your cost of capital?
- Are you taking advantage of any recent tax relief, and if so, how does that relief impact your 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?
- What accounting estimates were made, such as the probability a loan will be forgiven, and what uncertainties are involved in applying the related accounting guidance?

### ***A company's ability to continue as a going concern***

In addition to liquidity and capital resources assessments, in upcoming periodic reports, companies should also consider whether circumstances raise substantial doubt about the company's ability to meet obligations that become due within one year of issuing the financial statements. If the company's ability to continue as a going concern is under substantial doubt, management should provide appropriate disclosure of that doubt and any plans to alleviate such doubt. Specifically, the MD&A should discuss any conditions or events that give rise to doubt and if any portion of management's plans have been implemented.

### **Office of Chief Accountant Statement**

The OCA issued a statement emphasizing the role financial reporting plays in well-functioning markets, engagement, and work related to high-quality financial reporting.

Stakeholder desire for decision-useful information is heightened in times of certainty, such as that surrounding the COVID-19 outbreak. Therefore, the OCA emphasized certain actions that companies should take to ensure relevant and accurate disclosures that serve investor needs.

### ***Significant estimate and judgments; reasonable judgments***

As previously stated in the April 2020 statement, the OCA understands that many companies will be required to make significant judgments and estimates to address a variety of accounting and financial reporting matters. In making those judgments, the OCA reiterated that companies should continue to use well-reasoned judgments that are understandable and useful to investors. Companies should make disclosures that are designed to meet that goal and ensure that financial reporting reflects the information it represents.

### ***The importance of disclosure controls and procedures and internal control over financial reporting***

The OCA emphasized the importance of robust internal auditing controls and reminded public companies of the requirement that they maintain disclosure controls and procedures (DCP) and internal control over financial reporting (ICFR). As part of that requirement, management is required to evaluate the effectiveness of a public company's DCP at the end of each fiscal quarter and the effectiveness of the ICFR at the end of

each fiscal year. Public companies may have adapted their disclosure controls and procedures or internal control over financial reporting processes in response to the changing environment surrounding COVID-19, including changes on how various controls operate, how controls are tested, and the risk of the control operating effectively. If any such change materially affects, or is reasonably likely to materially affect, any entity's ICFR, the change must be disclosed in the quarterly filings in the fiscal quarter the change occurred.

### ***Reminders about an entity's ability to continue as a going concern***

In each reporting period, management should consider whether relevant conditions and events raise substantial doubt about the entity's ability to meet its obligations. When substantial doubt exists, management should make plans to alleviate the substantial doubt and make disclosures to investors, including the conditions giving rise to the doubt, management's evaluation of the effect of the conditions on the entity's ability to meet its obligations, and management's plans that alleviate such doubt. If management's plans do not alleviate doubt, additional disclosure is required. The OCA noted that generally accepted accounting principles (GAAP) require such disclosure in the notes of financial statements, which may be in addition to other disclosure requirements in filings with the SEC.

A review of interim financial information is not designed to demonstrate doubt about a company's ability to continue as a going concern, but auditors may discover such doubt during reviews. If an auditor becomes aware of doubt concerning an entity's ability to continue as a going concern during a review, the auditor should confer with management and consider whether the entity's disclosures conform with GAAP. If the disclosures are inadequate, the auditor should extend the procedures, evaluate the results, and communicate with the entity and its audit committee.

### ***Addressing complex or emerging issues in financial reporting; extensive consultation with the OCA***

In the statement, the OCA reminded issuers of the processes it has in place to provide staff views on the application of GAAP and International Financial Reporting Standards for complex, novel, and unique issues, including issues relating to the CARES Act. The OCA noted that the process was essential to companies providing adequate disclosure during the first quarter and encouraged stakeholders to continue engaging them with questions that may arise as a result of COVID-19 and other issues. In addition, the OCA reminded all stakeholders that auditor independence is crucial to the credibility of financial statements.

### ***Engagement with and the vital role of audit committees***

The OCA reiterated its view that the role of audit committees in oversight is crucial in the financial reporting system, especially amid this period of increased uncertainty. The OCA again emphasized that feedback directly from audit committee members is most welcome.

Alston & Bird has formed a multidisciplinary [response and relief team](#) to advise clients on the business and legal implications of the coronavirus (COVID-19). You can [view all our work](#) on the coronavirus across industries and [subscribe](#) to our future webinars and advisories.

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