SEC's Division of Corporation Finance Provides Updated Guidance on Disclosure Considerations Regarding Operations, Liquidity and Capital Resources in Light of COVID-19

Jul 1, 2020

Reading Time : **4 min**

By: Rosa A. Testani, John Patrick Clayton

In broad terms, Topic No. 9A emphasizes that disclosure should allow investors to understand how a company's board and senior management are evaluating the current and expected impact of COVID-19 on its operations and financial condition, including liquidity and capital resources. Additionally, Topic No. 9A points out that companies should monitor their facts and circumstances so that they can "proactively revise and update" disclosures to investors in response to any changes in facts and circumstances.

Operations, Liquidity and Capital Resources

Topic No. 9A provides various considerations in the form of questions that companies should weigh as they assess the adequacy of their disclosure about the impact of COVID-19. These considerations are intended to help companies provide robust and transparent disclosures about any operational adjustments they have made and any financing activities they have undertaken in the current economic environment. Below are some highlights of the considerations covered in Topic No. 9A.

- **Operations**: Companies should consider disclosing the operational challenges they are monitoring and evaluating as a result of COVID-19, the extent to which they have altered operations in response to COVID-19 and the impact such changes have had on their financial condition and short- and long-term liquidity.
- **Liquidity**: Companies should consider how their overall liquidity position and outlook is evolving in light of COVID-19. For example, companies should consider the extent to

which COVID-19 has affected revenues and whether such impact is material to their sources and uses of funds. Companies are also urged to disclose material assumptions made about the magnitude and duration of COVID-19's impact on revenues and discuss whether decreases in cash flows from operations would have a material impact on their liquidity position and outlook.

- **Indebtedness**: Companies should consider disclosing whether they have accessed revolving lines of credit or raised capital to address liquidity needs. Additionally, companies should discuss whether COVID-19 affects their ability to access traditional funding sources on the same or reasonably similar terms as previously available. If companies find it necessary to provide additional collateral or guarantees, or have incurred an increased cost of capital, they should consider disclosing this information. Further, companies that are concerned about complying with their debt service obligations or debt covenants in the future, or that are taking advantage of available payment deferrals, forbearance periods or concessions should consider disclosing such information so that investors have a clear understanding of any liquidity challenges.
- **Cash Burn**: Companies that disclose information relating to cash burn rate or daily cash use should also consider whether they are providing a clear definition of the metric and explaining how management actually uses the metric in managing and monitoring liquidity. Additionally, to avoid misleading investors, such companies are urged to consider the reasonableness of any underlying estimates and assumptions relating to cash burn.
- **Capital Expenditures and Other Cash Outlays**: Companies should provide information regarding any capital expenditure reductions in response to COVID-19, including reductions in human capital resource expenditures. Companies should also disclose if they have decided to suspend or reduce any share repurchase program or dividend payments in response to COVID-19. In discussing the foregoing, companies should clarify whether such measures are temporary and what factors will be considered when deciding whether any such measures are extended or curtailed. Companies should also consider discussing the short- and long-term impact of reductions, including any impacts to their ability to generate revenues, and meet existing and future financial obligations.
- **Payment Terms**: If companies alter terms with customers (e.g., extended payment terms or refund periods), provide concessions (e.g., as a landlord or lender) or otherwise modify contractual arrangements in response to COVID-19, they should

discuss any material impact that such actions would have on their financial condition, liquidity and capital resources.

- **Supplier Finance Programs**: Companies relying on a supplier finance program should disclose the material terms of such an arrangement and any material impact of the arrangement on their balance sheet, statements of cash flow or short- and long-term liquidity. Additionally, companies should consider discussing any guarantees related to such a program (including subsidiary guarantees) and any material risk if a party to the arrangement terminates.
- **Subsequent Events**: When assessing events occurring after the end of a reporting period, companies should consider whether the impact of such events is material enough to warrant disclosure as a subsequent event in the financial statements and as a known trend or uncertainty in management's discussion and analysis (MD&A).

Government Assistance – CARES Act

According to Topic No. 9A, companies should consider disclosure relating to any loans and tax relief received under the CARES Act. In particular, companies should consider discussing material terms of such loans, whether such terms limit their ability to seek other sources of financing or increase the cost of capital, whether any loan restrictions have a material impact on their revenues or income from operations and whether any lapse in loan restrictions will result in a material change in their operations. For any tax relief, companies should consider disclosing the impact of such relief on short- and long-term liquidity and whether they anticipate a material tax refund for prior periods. Finally, companies should consider disclosing the extent to which any assistance under the CARES Act involves new material accounting estimates or judgments or any change in prior critical accounting estimates.

Ability to Continue as a Going Concern

When preparing a company's MD&A, Topic No. 9A notes that management should consider whether conditions and events exist that raise substantial doubt about the company's ability to continue as a going concern (e.g., defaults on outstanding obligations, labor challenges or work stoppages). Management should also consider its plans to address these challenges and discuss the extent to which any of these plans have been implemented.

Additional Information

Topic No. 9A reminds companies that in addition to the disclosure topics discussed above, COVID-19 may materially impact a number of other disclosures, such as disclosure controls and procedures and internal control over financial reporting. For additional information on accounting and auditing matters related to COVID-19, Topic No. 9A refers to SEC Chief Accountant Sagar Teotia's Statement on the Continued Importance of High-Quality Financial Reporting for Investors in Light of COVID-19, which we discuss here.