KPMG

Financial Reporting Webinar Series: 2020 Year End Considerations

Monday, 14 December 2020

1

Pay careful attention to disclosures in all areas of annual report

Areas include:

- Going concern in close call situations, business continuity, liquidity risk, high estimation uncertainties and other financial risk exposures
- Significant judgements made, assumptions applied and sensitivity analyses

Narrative disclosures (e.g. ESG report / MD&A) and assumptions applied for accounting should be coherent

KPMG

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited (“KPMG International”), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

2

Classification requirements apply as usual to presentation in the financial statements

- The amount of expenses described as ‘COVID-19-related’ should be classified **by function or nature**, in the same way as expenses not relating to COVID-19
- Presenting COVID-19 impacts as a separate line item on the face of the income statement is **not allowed** under PRC GAAP

KPMG

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited (“KPMG International”), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

3

Using non-GAAP measures to discuss COVID-19 impact

- All requirements continue to apply (**HKEX GL 103-19**)
- Relevant, meaningful and not misleading
- Any changes in presentation or definition should be explained
  - How the metrics are calculated
  - Why management finds them useful
- Direct vs. indirect (e.g. assets impairment charges) and comparability

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited (“KPMG International”), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

Increased uncertainties adequately reflected in cash flow projections for impairment purposes

- Multiple scenarios analyses expected
- Discount rate - beware of ‘double counting’ of risks factored into cash flows
- Greater weight to be given to external sources of information to support assumptions

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited (“KPMG International”), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

Appropriate treatment of ROU asset for impairment test

- Right-of-use asset is tested for impairment as part of the larger CGU to which it relates
- Recoverable amount of ROU asset is the higher of VIU and FVLCD
- Impairment losses are allocated to the ROU assets similar to other assets in the CGU

KPMG

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited ("KPMG International"), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

6

Fair value of investment properties should reflect an exit price and factor in estimation uncertainties

- Valuation principles remain unchanged under current economic conditions
- Risk adjustments required for significant measurement uncertainties
- Take note of caveats and limitations in valuation reports and make appropriate disclosures

KPMG

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited ("KPMG International"), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

Example: disclosures for users to understand the uncertainties factored into valuation

II. Valuation technique and significant unobservable inputs[a]

Commercial property

The commercial property held by the Group in [*Country X*] is leased out to 10 tenants, mainly apparel retailers. Due to the economic disruption caused by the COVID-19 coronavirus pandemic, the Group has granted a two-month rent holiday to several tenants that have been significantly hit by the pandemic. The highly uncertain economic outlook for the period may have a material adverse effect on the tenants' operations, the viability of their business and their ability to meet their rental obligations. This uncertainty is factored into the valuation of investment property, specifically in estimating rent payments from existing tenants, the void periods, occupancy rates, expected market rental growth rates and the discount rate, all of which are significant inputs into the fair value determination.

- Uncertainty factored in includes possible rent defaults, void periods.
- Changes to assumptions also require disclosures

As at 31 December 2020, the valuer has factored in the potential impact of the COVID-19 pandemic by modifying the previous year's assumptions for the period 2021–22 as follows:

– prolonged void periods (increased by three months);

– lower expected market rental growth (decreased to 1%);

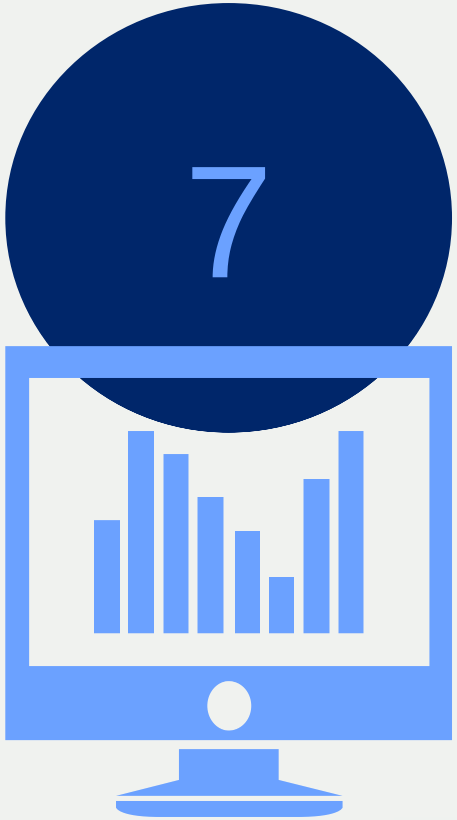
– lower levels of occupancy rates (decreased by 5%); and

– a decrease in sales-based rents.

The 31 December 2020 valuation contains a 'material valuation uncertainty' clause due to the market disruption caused by the COVID-19 pandemic, which resulted in a reduction in transactional evidence and market yields. This clause does not invalidate the valuation but implies that there is substantially more uncertainty than under normal market conditions. Accordingly, the valuer cannot attach as much weight as usual to previous market evidence for comparison purposes, and there is an increased risk that the price realised in an actual transaction would differ from the value conclusion. As a result of this increased uncertainty, the assumptions may be revised significantly in 2021. A sensitivity analysis on these assumptions is included in Note 2(C).

...Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited ("KPMG International"), a private ...limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential



Expected credit losses (ECL) allowance should reflect the current environment

- ECLs are financial losses due to credit risk (no credit risk is very rare)
- “Expected” means probability-weighted
- ECL allowance should reflect the impact of Covid-19 (e.g. customer segmentation, payment profiles)

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited (“KPMG International”), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

8

Timing and amount of revenue estimates (assumptions such as price concession, return rates, breakage) may require continuous assessment

- Customer behavior change should be factored in for changes that would impact on timing and amount of revenue
- Assumptions using past historical data for estimates such as return rates and breakage may be less relevant
- Customers with credit issues could constrain the amount of revenue to be recognised

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited ("KPMG International"), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

9

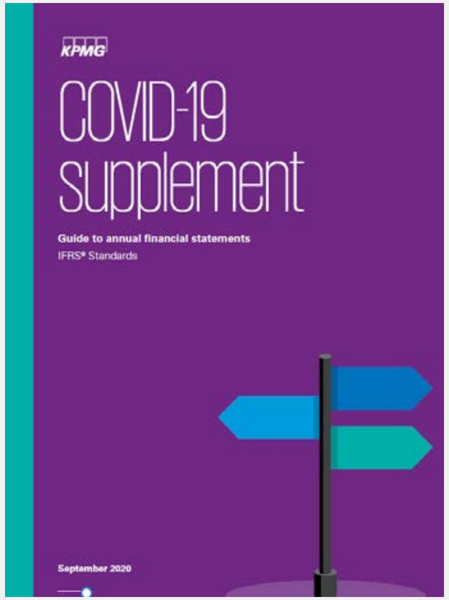
Reminders on applying the rent concession practical expedient

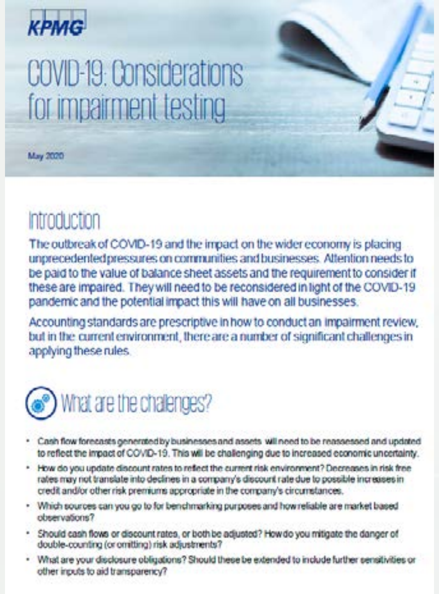
- Lessees are not required to assess whether eligible rent concessions are lease modifications
- Rent concession amendments issued has no detailed application guidance, there may be more than 1 acceptable approaches in rent deferral situation

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited ("KPMG International"), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

Resources




KPMG

COVID-19: Considerations for impairment testing

May 2020

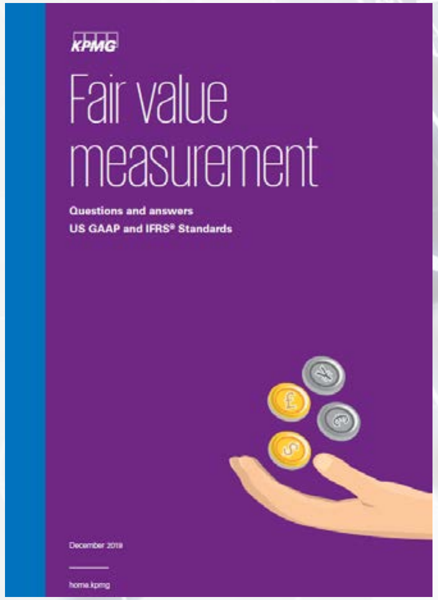
Introduction

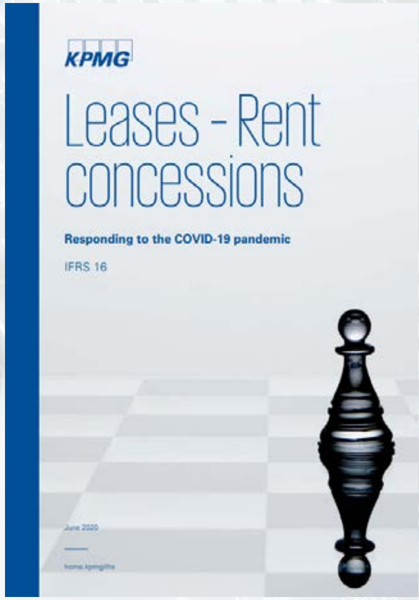
The outbreak of COVID-19 and the impact on the wider economy is placing unprecedented pressures on communities and businesses. Attention needs to be paid to the value of balance sheet assets and the requirement to consider if these are impaired. They will need to be reconsidered in light of the COVID-19 pandemic and the potential impact this will have on all businesses.

Accounting standards are prescriptive in how to conduct an impairment review, but in the current environment, there are a number of significant challenges in applying these rules.

What are the challenges?

- Cash flow forecasts generated by businesses and assets will need to be reassessed and updated to reflect the impact of COVID-19. This will be challenging due to increased economic uncertainty.
- How do you update discount rates to reflect the current risk environment? Decreases in risk free rates may not translate into declines in a company's discount rate due to possible increases in credit and/or other risk premiums appropriate in the company's circumstances.
- Which sources can you go to for benchmarking purposes and how reliable are market based observations?
- Should cash flows or discount rates, or both be adjusted? How do you mitigate the danger of double-counting (or omitting) risk adjustments?
- What are your disclosure obligations? Should these be extended to include further sensitivities or other inputs to aid transparency?





© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

Webinar dates and topics for 2020

- **15 May – Sailing through the storm with clarity (COVID-19 related accounting issues)**
- **12 June – ESG reporting: latest developments**
- **17 July – Use of non-GAAP measures and IASB's primary financial statements project**
- **18 September – The search for value in Goodwill**
- **13 November – Beyond compliance – ESG reporting**
- **14 December – Key year-end reporting considerations**

For more details and access to our webinar series:

https://home.kpmg/cn/en/home/services/audit/ifrs-news/financial-reporting-webinar-series.html

KPMG

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. Printed in Hong Kong, China.

Document Classification: KPMG Confidential

Speakers

Paul Lau

Head of Professional Practice and Capital Markets
KPMG China

E paul.k.lau@kpmg.com

Ko Sin

Partner
Department of Professional Practice
KPMG China

E sin.ko@kpmg.com

Yifei Gong

Senior Manager
Department of Professional Practice
KPMG China

E yifei.gong@kpmg.com

Serene Seah-Tan

Partner
Department of Professional Practice
KPMG China

E serene.seah-tan@kpmg.com

Thank you

kpmg.com/cn/socialmedia

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG, a Hong Kong partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited ("KPMG International"), a private English company limited by guarantee. All rights reserved. Printed in Hong Kong, China.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.